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ABSTRACT

This study analyzes the evolution of the regime governing private international trade law from its inception in the eleventh century through to its modern formulation in the twentieth century. It also seeks to explain its development by focusing on three theories of international relations.

The regime is defined in terms of its substantive and procedural dimensions. The nature and strength of the norms governing the substantive dimension (prices, liability for defective goods, allocation of transport costs, insurance, and financial and credit arrangements) and the procedural dimension (locus of regulation, methodology of rule creation, and dispute settlement) are analyzed over three historical phases. These three periods are the medieval period, from the eleventh to the sixteenth centuries, the early modern period, from the seventeenth to the nineteenth centuries, and the modern period in the twentieth century. The regime norms are found to exhibit significant continuity over time, although there has been considerable variation in the rules. The strength of the regime has also varied over the three phases.

Three theoretical perspectives (structural realism, functionalism, and sociological analysis) are evaluated for their relative ability to explain the origin, evolution, nature, and strength of the regime. Each perspective is found to offer important insights, but a synthesis of approaches is necessary to capture the complexity and richness of the regime's evolution. Structural realism does not account for the origin of the regime and is of limited assistance in explaining the strength of voluntary standards. It does, however, explain the influence that states' concerns for political/legal autonomy have had on the regime and offers a reasonably good account of the roles that the United States and the United Kingdom have played in the evolution of the regime. Sociological analysis assists in accounting for the origin and nature of the regime, but it does not provide a comprehensive theory of cooperation. Reference to the other approaches is required as a supplement to sociological analysis. Functionalism provides the best explanation of the origin and nature of the regime. However, it is unable to account for variations in the strength of the regime over the three historical periods. Reference to the influence of changing structures of political authority and to the ideas, knowledge, and values of the major commercial actors is necessary as a supplement to functional analysis.
### TABLE OF CONTENTS

Abstract..................................................................................................................ii  
List of Figures..........................................................................................................v

**CHAPTER I**  
The Study of International Collaboration and the Private International Trade Law Regime..........................................................1

**CHAPTER II**  
Regimes Analysis and the Private International Trade Law Regime.........................17

A. Conceptual Foundations of Regimes Analysis.........................................................17
B. Overview of the Private International Trade Law Regime.................................49
   1. Regime Scope: Constituent Issues.................................................................49
   2. Regime Nature: Relevant Principles..............................................................56
   3. Normative Structure of the Regime: Substantive Dimension.........................62
   4. Normative Structure of the Regime: Procedural Dimension.........................70
   5. Regime Strength.........................................................................................79

**CHAPTER III**  
Theoretical Perspectives on International Regimes................................................84

A. Structural Realism.............................................................................................86
B. Functionalism......................................................................................................98
C. Sociological Approach......................................................................................107

**CHAPTER IV**  
Phase I: The Medieval Law Merchant, 11th to 16th Centuries..................................119

A. Medieval Jus Commune and Jus Gentium.........................................................120
   1. Substantive Dimension..................................................................................134
      (a) Prices.....................................................................................................134
      (b) Liability for Defective Goods..............................................................140
      (c) Allocation of Transport Costs and Liabilities........................................145
      (d) Insurance..............................................................................................155
      (e) Financing and Credit............................................................................160
   2. Procedural Dimension....................................................................................168
      (a) Locus of Regulation..............................................................................168
      (b) Methodology of Rule Creation............................................................175
      (c) Dispute Settlement...............................................................................180
B. Summary............................................................................................................186
# LIST OF FIGURES

<table>
<thead>
<tr>
<th>Figure</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Figure 1</td>
<td>Regime Principles</td>
<td>56</td>
</tr>
<tr>
<td>Figure 2</td>
<td>Normative Structure</td>
<td>62i</td>
</tr>
<tr>
<td>Figure 3</td>
<td>Regime Strength</td>
<td>82</td>
</tr>
</tbody>
</table>
CHAPTER I

THE STUDY OF INTERNATIONAL COLLABORATION AND THE PRIVATE INTERNATIONAL TRADE LAW REGIME

Significant developments in the post World War II period are resulting in the increased importance of international economic relations to both the practice and study of international relations. The growth in international economic interdependencies, occasioned by increases in the level of world trade and by the globalization of investment and finance, generate new complexities for states' foreign policy agendas. The need for international collaborative arrangements or regimes to assist in the management of these complexities is more apparent to states today than ever before. Indeed, we are witnessing a proliferation of international institutions and regimes that facilitate the management of many of the common problems generated by complex interdependencies. In attempting to keep pace with the practice of international relations, students are growing more concerned with the theoretical foundations for and implications of international cooperation and collaboration. This is evident in the central place that the study of international regimes occupies in international relations scholarship.¹

Students of international regimes are generally concerned with the issue of international governance and focus upon the principles and formal and informal rules, practices, procedures, and institutions that regulate international relations. Of concern is identification of the conditions that give rise to international collaboration and systematization of our theoretical and conceptual understanding of cooperation. The concern with understanding international collaboration reflects a dissatisfaction with the dominant paradigm or world view which posits that states exist in a condition of international anarchy. The belief that there are cooperative or societal elements present in international relations that mute the effects of international anarchy suggests that there is a need to re-evaluate assumptions about international relations.

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3. Keohane, "International Institutions."


While the concern with understanding international collaboration is not new, what is novel in the study of international regimes, is the attempt to broaden the conception of international institutions and organizations to include informal as well as formal arrangements and to link the study of such arrangements with the broader theoretical concerns occupying the discipline of international relations. Such concerns relate to the possibilities for and nature of norm governed and cooperative relations in a world that is typically characterized as anarchic, or lacking centralized authority. Notable also, is the reference to other fields of study, such as international law and economics, and the attempt to integrate their insights into the origin and nature of international collaboration. It has been noted that "the literature on regimes has introduced a conception of international institutions that differs markedly from the

6. See Robert O. Keohane, "The Study of International Regimes and the Classical Tradition in International Relations," delivered at the Annual Meeting of the American Political Science Association, 1986 for a discussion of past usage of the term and concept "regime" in international law and international politics. And see K. J. Holsti, "The Necrologists of International Relations," Canadian Journal of Political Science 18 (December 1985), p. 692 for the view that "regimes" is really "a new name to cover an old phenomenon; it used to be called international law and organization".

conception embedded in the orthodox literature on international relations....this conception has already helped to identify constructive opportunities for reintegrating the subfields of international politics, economics, law, and organization."\(^8\) Indeed, progressive analytical shifts in conceptualizing the central problematic of international governance have led to a revival of interest in international law and organization in the context of international regimes.\(^9\) The notion of governance, both implicitly and explicitly, directs attention to authority structures, constituent principles, norms and rules and to institution-building, matters traditionally considered the domain of international law and organization. However, the current concern with authority, rules and institutions does not exhibit what has been referred to as a "sterile preoccupation with legal-formal aspects of international relations" that characterized earlier studies of international law and organization.\(^10\) Rather, many contemporary theorists are exploring more sophisticated and, indeed, more fundamental concerns


9. Kratochwil and Ruggie in "International organization" trace the shifts in analytical focus in conceptualizing the phenomenon of international governance from a focus on formal institutions, to a focus on institutional processes, then to a focus on organizational roles and finally to the present focus on international regimes.

regarding the genesis of normative structures, the
differentiation of authority and rule structures, and the
bases of compliance and obligation. Legal theory has much
to offer in this regard. The integration of insights
afforded by international legal studies can greatly enrich
our conceptual and theoretical understanding of
international regimes.

Collaborative or cooperative arrangements that evidence
rule or norm governed behavior are identified in a number of
issue areas. In the area of international economic
relations, we are most familiar with the regime governing
international trade, and increasing attention is being given
to international monetary relations, international finance,
and investment. This should come as no surprise for, as

11. See for example the works of Kratochwil cited in
Chapter II, notes 13, 14 and John G. Ruggie,
"International regimes, transactions, and change:
embedded liberalism in the postwar economic order,"
International Organization 36 (Spring 1982): 195-229
and Ethan A. Nadelmann, "Global prohibition regimes:
the evolution of norms in international society,"

12. For example see O. Schachter, "Towards a Theory of
International Obligation," Virginia Journal of
International Law 8 (1968): 300-22 for a review of a
number of theories advanced by legal scholars to
explain international cooperation.

13. Robert O. Keohane and John S. Nye, Power and
Interdependence: World Politics in Transition (Boston:
Little, Brown, 1977); Vinod Aggarwal, Liberal
Protectionism: The International Politics of Organized
Textile Trade (Berkeley: University of California
Press, 1985); Robert O. Keohane, After Hegemony:
Cooperation and Discord in The World Political Economy
(Princeton: Princeton University Press, 1984); John G.
Ruggie, "International regimes, transactions, and
change: embedded liberalism in the postwar economic
Oran Young has observed, regimes literature "is closely associated with the ideas of those who have become leaders in the movement to revive the study of international political economy." Furthermore, the now consensual definition of international regimes, to be discussed in Chapter II, is said to have been formulated with reference to the GATT trade regime. This underlines the perceived importance of economic relations and, in particular trade relations to international relations. "Trade is the oldest and most important economic nexus among nations. Indeed, trade along with war has been central to the evolution of international relations. The modern world market economy makes international trade still more important, and developments in the 1980s have had a profound effect on the nature of the international political economy." The post


World War II period has experienced an unprecedented expansion of trade, due in no small part to the regulation of significant barriers to trade under the GATT regime. Strains in the multilateral, liberal regime are, however, evident in the growth of sectoral protectionism, regional trading arrangements, and in the proliferation of trade arrangements not subject to GATT discipline. Students of the trade regime have analyzed the genesis of the regime and identified its normative foundations. Many are attempting to identify sources of weakening or transformation.

While considerable attention has been given to the GATT trade regime, the regime governing private international trade relations has not attracted significant analysis. Some legal scholars and a few economic historians have directed limited attention to this area, but there has been no attempt to analyze the political dimensions of private international trade law. Nor has the private trade law regime been subjected to systematic description and analysis. This is significant, for the regime governing private international trade is the most durable and pervasive regime in the international economy. Indeed, it constitutes the foundation and backbone of the global economy. International commercial transactions provide the

foundation for global economic exchange and their regulation is critical in providing a stable environment for exchange and in facilitating the growth of international trade and commerce. International trade and commerce would not be possible in the absence of generally accepted protections of property and contract. The protection of private property rights and the sanctity of agreements provide the essential preconditions for international economic exchange. These protections have their roots in the tradition of Western jurisprudence and in the practices of commercial actors adopted by Western Europeans to govern commercial relations. The private international trade law regime provides commercial actors with reasonably stable expectations and assurances that their agreements will be honoured. The regime facilitates exchange by providing greater certainty in commercial transactions and by providing mechanisms for the allocation of risks, the determination of liabilities, and the settlement of disputes arising from commercial exchange.

While it is important to understand the durability and pervasiveness of the regime in terms of the facilitation of exchange, it is also important to note that the regime is unique in that it has grown from and been sustained by private commercial actors throughout the world who value both stability and latitude in the conduct of commerce. The regime establishes standards that provide for stable and uniform expectations, but at the same time, leave much room
for merchant autonomy to freely enter into accords and to conduct business with a minimum of external interference. Probably the most notable characteristic of the regime is its basis in commercial custom and practice. While states have intervened at different times to regulate international commercial activities, the regime has derived its strength and stability largely through the self-enforcement actions of merchants. Indeed, with the globalization of economic processes, the principle of merchant autonomy has acquired renewed vigor as merchants seek to strengthen Western liberal capitalist values.

The regulation of private international trade relations provides fertile grounds for regimes analysis. The body of law, custom, and practice that regulate private trading activities is often referred to as transnational commercial law,18 the law merchant (lex mercatoria),19 or simply the law of international trade.20 It is commonly observed that despite the diversity of legal systems in the world, there is a considerable and even surprising degree of uniformity in international commercial law and practice. To quote one


authority, "the law of international trade shows a striking similarity in all national legal systems...transcending the division of the world into planned and free-market economies, developed and underdeveloped economies, and common law and civilian legal systems."\textsuperscript{21} Indeed, international trade terms allocating the risk of loss or damage to goods and clauses included in bills of lading, marine insurance policies, letters of credit, charter parties and arbitration agreements, to cite but a few examples, are generally understood throughout the world and are governed by similar rules and practices.\textsuperscript{22} While care should be taken to avoid overstating the extent of this uniformity of rules and practice, for some areas of trade law exhibit a greater degree of standardization than do others, it is indeed remarkable that uniformity exists to the degree that it does.\textsuperscript{23} It is even more remarkable that there has been considerable continuity over several

\begin{enumerate}
\item For a contrary view that stresses the lack of uniformity, in particular as between common law and civil law jurisdictions, see Rene David, "The International Unification of Private Law," in \textit{International Encyclopedia of Comparative Law II: Legal Systems of the World, Their Comparison and Unification} (1972), chap. 5, p. 8.
\end{enumerate}
centuries in many of the principles governing private trade relations.

Today the private trade law regime may be regarded as a specific regime "nested" in the more diffuse international trade regime. As such, it shares many of the assumptions underlying the GATT trading regime regarding the benefits flowing from trade regulation that reduces impediments or barriers to economic exchange. The private trade law regime focuses upon the reduction of barriers to exchange through the unification and harmonization of different and often uncertain national commercial laws.

A number of intergovernmental organizations are today involved in the unification of international commercial law. They are engaged in the formulation of international conventions, model laws, codes, and statements of commercial practice for the use of parties engaged in international trade. These conventions, laws, and codes may take the form of binding commitments to transact according to prescribed standards and procedures or non-binding instruments for the optional use of the parties. They range from formal international conventions establishing performance obligations, liability and compensation standards, and property rights in transactions concerning the sale, transportation, insurance, and financing of goods to

24. See Aggarwal, Liberal Protectionism for the notion of the nesting of a specific regime in a more diffuse regime.
procedures for the enforcement of agreements and dispute resolution.

However, uniform rule creation at the intergovernmental level has not always been the standard mode for regulating private international trade. Indeed, in the first phase of the development of the regime, the medieval period, merchants themselves exercised significant autonomy in creating uniform rules and in enforcing agreements. This autonomy was exercised within the broad boundaries established by the local authorities of the day who regulated local markets and local trade. However, with a few exceptions, local authorities were not significantly involved in regulating long distance or overseas trade. The establishment of property rights, performance obligations, the allocation of risks, and the enforcement of bargains were largely left to the parties transacting. During this period the merchants constituted a special class and formulated their own system of law and organization to govern their commercial activities. Throughout Europe merchants settled their own disputes in merchant courts that operated outside the jurisdiction of the local authorities and the local systems of law. The law applied was lex mercatoria, the law merchant, which stressed informality, flexibility, equity, good faith, and reciprocity. Merchant courts sat in seaport towns and at fairs and markets throughout Europe, dispensing expeditious and informal justice. The law merchant was distinctive in nature in that
it enforced procedures for rule creation and substantive agreements that were not enforceable in the local common or civil law courts of the day. It was also universal in that it was applied by most seaport and inland towns throughout the European trading world.

It was only later, in the second phase, with the establishment of the states system and the entrenchment of the notion of territorial sovereignty, that governments became involved more significantly in the regulation of trade. Trade relations came to be subject to national regulation, which severely curtailed the autonomy of merchants. This process of nationalizing and localizing trade law lasted well into the nineteenth century and is generally regarded to have fundamentally changed the regime by eroding and undermining its distinctiveness and universality. The standards and procedures governing international commercial relations were subjected to the particularisms of national legal, political, and economic systems which came to regard commercial law in national and territorial terms. However, despite these changes, many fundamental principles of the law merchant survived.

The regime underwent further transformation in the third phase, the twentieth century, and in particular, in the post World War II period. The proliferation of international organizations and private associations engaged in the formulation, unification, and harmonization of trade law and practice is today contributing to a reassertion of
the fundamental principles and a renewal of the regime's distinctiveness and universality. As Schmitthoff suggests, the law of international trade has "reverted to the concept of internationalism and is moving away from the restrictions imposed by national law, towards a more universal and international conception."25

This dissertation undertakes the first systematic description and analysis of the nature and evolution of the private trade law regime. It provides a systematic analytical framework for the regime and evaluates the explanatory capabilities of various theoretical approaches employed in the study of international relations. The regime is traced through three developmental phases, from the first phase of medieval internationalism to the period of state-building and the nationalizing of regime standards in the second phase and, finally, to the third and present phase, which is witnessing a revival of medieval internationalism. The study illustrates that while the normative foundations of the regime have changed over time, there has been remarkable continuity in many of the principles informing the regime. It also shows that the strength of the regime has varied over time. In assessing the explanatory capabilities of different theoretical approaches the study proposes that a synthesis of approaches

is required to understand the nature of the regime and the sources of continuity and change.

The study also shows the contribution that an analysis firmly rooted in both international law and international relations can make to the understanding of international cooperation. Insights afforded by legal theory assist in developing the conceptual foundations for regimes analysis, while the application of international relations theories to a specific area of international law furthers the exploration of the nexus between international politics and international law.

Chapter II provides the conceptual framework for the study and an overview of the private trade law regime. It introduces the concept of international regimes, identifies the key constituent regime issues, and outlines the principles and norms that provide the foundations for the regime. A preliminary assessment of the nature and strength of the regime in the three phases is also provided.

Chapter III reviews various explanations of regime origin, nature, transformation, and strength. This chapter identifies the sort of evidence that will tend to support or undermine the explanatory capabilities of the different theoretical perspectives considered.

Chapters IV through VI present three phases in the evolution of the regime from its inception in the eleventh century up to the present time. The significant
characteristics of and transformations in the regime will be identified and its strength evaluated. These chapters provide the evidence that will form the basis for the evaluation of the theoretical perspectives.

Chapter VII concludes the study with an evaluation of the adequacy of different explanations of regime origin, nature, transformation, and strength. It proposes a synthesis of explanatory approaches.
CHAPTER II

REGIMES ANALYSIS AND THE PRIVATE INTERNATIONAL TRADE LAW REGIME

The conceptual and theoretical insights generated by regimes analysis provide a useful framework for analyzing the nature and evolution of the private international trade law regime. This chapter reviews the conceptual foundations of regimes analysis and provides an overview of the private international trade regime.

A. CONCEPTUAL FOUNDATIONS OF REGIMES ANALYSIS

International regimes have been defined as "sets of implicit or explicit principles, norms, rules, and decision-making procedures around which actors' expectations converge in a given area of international relations." Principles are further defined as "beliefs of fact, causation, and rectitude," norms as "standards of behavior defined in terms of rights and obligations," while rules are "specific prescriptions or proscriptions for action." Decision-making procedures are "the prevailing practices for making and implementing collective choice." Before proceeding to consider the various components of this definition, a few general observations are in order.

The definitional emphasis on convergent expectations embodied in both explicit and implicit regime standards suggests that regimes are "social institutions".

Regimes are social institutions governing the actions of those interested in specifiable activities (or accepted sets of activities). Like all social institutions, they are recognized patterns of behavior or practice around which expectations converge. Accordingly, regimes are social structures; they should not be confused with functions, though the operation of regimes frequently contributes to the fulfillment of certain functions. As with other social institutions, regimes may be more or less formally articulated, and they may or may not be accompanied by explicit organizational arrangements.²

International regimes are thus differentiated from international organizations. While international organizations may be "embedded within international regimes" and "in practice they may seem almost coterminous," they are analytically distinct.³ International regimes may exhibit different degrees of formal explication and institutionalization.⁴ Furthermore, as social institutions,

² Oran R. Young, "Regime dynamics: the rise and fall of international regimes," in Krasner, ed., International Regimes, p. 93. Ernst B. Haas in "Words can hurt you; or, who said what to whom about regimes," in the Krasner volume and Keohane in After Hegemony also emphasize the nature of regimes as social institutions.


⁴ Keohane in International Institutions, p. 3 conceives of institutions as "persistent and connected sets of rules (formal and informal) that prescribe behavioral roles, constrain activity, and shape expectations." He argues that international institutions assume three possible forms: formal organizations, international
regimes are "recognized practices consisting of easily identifiable roles, coupled with collections of rules or conventions governing relations among occupants of these roles." The rules and conventions embody "sets of rights or entitlements" and "sets of behavioral prescriptions."\textsuperscript{5} Regimes thus comprise organizational roles, state practice, and a normative or obligatory element.\textsuperscript{6} They evolve over time in response to changing conventions, practices, and purposes that shape expectations and condition understanding and thus highlight the role of intersubjective meanings and knowledge structures. "The emphasis on convergent expectations as the constitutive basis of regimes gives regimes an inescapable intersubjective quality. It follows that we know regimes by their principled and shared understandings of desirable and acceptable forms of social behavior."\textsuperscript{7}

\textsuperscript{5} Young, "International Regimes," p. 107.
\textsuperscript{6} Kratochwil and Ruggie, "International organization," p. 759.
\textsuperscript{7} Kratochwil and Ruggie, "International organization," p. 764. This matter will be considered at length in Chapters III and VII.
As social institutions, regimes regulate behaviour by establishing standards of conduct. These standards are embodied in a variety of different types of rules. The jurisprudential concept of law as a social or institutional fact is here insightful. It has been observed that "[i]f law exists at all, it exists not on the level of brute creation along with shoes and ships and sealing wax or for that matter cabbages, but rather along with kings and other paid officers of state on the plane of institutional fact."\(^8\) Law may be regarded as an institutional phenomenon in two senses. In a sociological sense, it is institutional "in that it is in various ways made, sustained, enforced, and elaborated by an interacting set of social institutions."\(^9\) The law, in a domestic context, thus refers to the formal institutions constituting the legal system, like courts, the legal profession, and the police, as well as to the rules and norms that regulate these institutions. But the law as an institutional fact also has a philosophical meaning, which refers to some sort of consensus or agreement as to how rules are instituted or created and terminated, as well as to the consequences that flow from their existence.\(^10\)


10. MacCormick refers to these as institutive rules, terminative rules and consequential rules. Joseph Raz in *The Concept of a Legal System: An Introduction to*
H. L. A. Hart's identification of secondary rules is relevant here. Hart makes a useful distinction between primary rules, which grant rights or impose obligations, and secondary rules, which stipulate the manner in which primary rules may be created, modified, extinguished, and recognized. Secondary rules or rules of recognition are the rules instituting, constituting, and governing rules. Rules are binding when they are accepted by society as binding, as evidenced by societal practices and norms, or when they are enacted in conformity with secondary rules that provide for their validity.

A similar distinction, which will be taken up later in the discussion, has been made between regulative rules and constitutive or practice-type rules. The former establish standards governing behaviour in terms of prescriptions or proscriptions. The latter embody standards governing the creation and constitution of rules.

The law as thus conceived can only be understood within the context of shared understandings, societal values, beliefs, and practices. Kratochwil refers to this as "the

the Theory of Legal System, 2nd. ed. (Oxford: Oxford University Press, 1980), p. 176 refers to these rules as investive laws (specifying the way in which rights are acquired), divestive laws (determining the way in which rights can be disposed of) and constitutive laws (specifying the consequences of being a rights holder).


12. See notes 66 and 67 and the accompanying text.
realm of intersubjective rules which are constitutive of social practice, and which an interpretive epistemology has to uncover.\textsuperscript{13} Kratochwil has highlighted the importance of often neglected practice or institution-type rules to our understanding of international regimes.\textsuperscript{14} This type of rule is of particular importance in the conceptualization of the private international trade regime, for this regime is primarily constituted by voluntary and promissory obligations. These obligations derive their meaning and effectiveness from underlying practices. John Rawls, in defining the practice conception of rules, observes the following:

On this view [the practice conception of rules] rules are pictured as defining a practice. Practices are set up for various reasons, but one of them is that in many areas of conduct each person's deciding what to do on utilitarian grounds case by case leads to confusion, and that the attempt to coordinate behavior by trying to foresee how others will act is bound to fail. As an alternative one realizes that what is required is the establishment of a practice.... It is a mark of a practice that being taught how to engage in it involves being instructed in the rules which define it, and that appeal is made to those rules to correct the behavior of those engaged in it. Those engaged in practice recognize the rules as defining it.... Thus it is essential to the notion of a practice that the rules are

\begin{itemize}
  \item \textsuperscript{13} "Regimes, Interpretation and the 'Science' of Politics: A Reappraisal," \textit{Millenium: Journal of International Studies} 17 (1988), p. 277.
  \item \textsuperscript{14} See \textit{Rules, Norms, and Decisions: On the conditions of practical and legal reasoning in international relations and domestic affairs} (New York: Cambridge University Press, 1989).
\end{itemize}
publicly known and understood as definitive; and it is essential also that the rules of practice can be taught and can be acted upon to yield a coherent practice.\textsuperscript{15}

Rawls believes that contractual or voluntary obligations can only be understood in the context of the practices that render promises binding. Promising, it is said, "can be analyzed as a speech act in an intelligible way only if it is observed that particular promissory utterances essentially 'count as' promises only because they are intended to be and are recognized as instances of social 'practice,' or 'institution.' The act presupposes the practice..."\textsuperscript{16} Furthermore, the practice of promising is generated and sustained by secondary rules of recognition. These rules "provide individuals with facilities for realizing their wishes, by conferring legal powers upon them to create, by certain specified procedures and subject to certain conditions, structures of rights and duties within the coercive framework of the law."\textsuperscript{17} Secondary rules draw their ultimate validity from the fact that society regards them and accepts them as valid and, thus, they are ascertainable by reference to societal beliefs, norms, and practices. What distinguishes legal rules from other sorts


\textsuperscript{17} Hart, \textit{The Concept of Law}, p. 27. And see MacCormick, "Voluntary Obligations," p. 61.
of rules is that the former are regarded as binding and obligatory, a consideration we will turn to shortly.

The above definition of international regimes also gives rise to the conceptual distinction between the substantive and procedural dimensions of a regime. Michael Barkun notes that the law is divided between substantive and procedural rules, a division that he observes bears a likeness to Hart's distinction between primary and secondary rules.

The procedural rules or norms create a framework within which a whole array of human actions can be judged, with the subsequent introduction of substantive rules or norms that outline the permissible and impermissible in human behavior. Procedural norms can delegate persons in a society to prescribe conduct by conferring discretionary authority on them. In other words, procedural norms answer the question "Who can legitimately make and enforce the laws." While Hart places primary or substantive rules first, analytically and historically, in the belief that secondary rules come later in the evolution from primitive to advanced legal structures, Barkun inverts the order. The difference is not of immediate concern to this discussion. What is of concern, however, is the distinction between the two dimensions of a legal order. In the context of regimes

analysis we may distinguish between these two dimensions.\textsuperscript{19} The substantive dimension refers to the issues and subject-matter that form the content of the regime and includes the standards and guidelines established by the regime to govern behaviour. The procedural or decision-making dimension refers to the processes and institutions involved in the creation and enforcement of such standards and guidelines. The two dimensions will be further considered when an overview of the private international trade regime is presented.

A few final preliminary comments are in order before the various conceptual components of the definition of international regimes are considered. The issues now to be considered are of first order importance, for how we define each component and conceive of the nature of the relationships between and among the conceptual components depends upon the model of rules and law or authority structures one adopts. Moreover, the criteria to be employed to determine the boundaries or scope of a regime, the factors to be considered in defining the nature or normative content of the regime, and the tests employed to

assess the strength of a regime will all be informed by the underlying model of law employed.

The regime definition suggests that the conceptual components of a regime are arranged hierarchically according to the degree of specificity or generality in which they are formulated. Principles lie at the top of the hierarchy and define the purposes of the regime in the most general terms. Norms constitute more specific injunctions, while rules and decision-making procedures are even more specifically explicated. Kratochwil cautions that "the indiscriminate aggregation of the most disparate phenomena, such as expectations, informal understandings, explicit rules, higher-level norms, decision-making procedures, etc., obscures rather than clarifies the impact on norms in decision-making." Indeed, others have noted the difficulty in differentiating between regime components. "Despite the care with which this complex hierarchy of components is defined, 'principles' (which include not only beliefs of fact and causation, but also of 'rectitude') shade off into norms, 'standards of behavior defined in terms of rights and obligations.' Norms, in turn, are difficult to distinguish from rules, 'specific prescriptions


or proscriptions for action.'" Ambiguity in differentiating between regime components is of considerable significance in determining the processes of regime change. It is commonly asserted that changes in regime rules and decision-making procedures constitute changes within regimes, while changes in principles and norms constitute changes of regimes. Analysis of the processes of regime change is thus rendered problematic when it is difficult to determine whether one is dealing with principles, norms, or rules.

It is submitted that these definitional ambiguities do not pose significant obstacles to analysis. Jurisprudential inquiry into the definition of legal principles, norms, and rules and the identification of legal systems recognizes that an element of ambiguity accompanies even the most developed of legal systems. Dworkin notes that in spite of the problem that legal rules and principles may appear similar in form and function, they are logically distinct. They have different origins and operate differently and, accordingly, they require different tests of validity and pedigree. While we will deal with these differences

22. Haggard and Simmons, "Theories of international regimes," p. 493, notes omitted. And see Keohane, After Hegemony, p. 58.

23. The Krasner volume adopts this position.


25. It should be noted that many legal theorists tend to refer to norms and rules interchangeably. They then differentiate among norms/rules according to their type
shortly, for the moment it is sufficient to note that
difficulties in differentiating between them does not
prevent their logical and analytical distinction. In
addition, Hart, while not in agreement with Dworkin’s
distinction between principles and rules, has dealt at
length with the problem of differentiating between types of
legal standards or rules. Hart argues that while rules must
have a core of settled meaning, "all rules have a penumbra
of uncertainty." 26  "We may call the problems which arise
outside the hard core of settled meaning "the problem of the
penumbra"; they are always with us...." 27  The problem of
the penumbra illustrates the ambiguity inherent in any
system that is not closed or complete. It is a problem that
must be recognized and accommodated through the tolerance of
a degree of ambiguity. Moreover, the degree of ambiguity
tolerable is intimately related to the theory of law or
model of rules one adopts. Strict legal positivists, who
posit that law is the creation of positive legislative acts
and judicial decisions applying those acts, have less
tolerance for ambiguity than do those who adopt less

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restrictive theories of law, more accommodating of custom, practice, and judicial discretion.

Further conceptual ambiguity is generated by problems in determining the scope and boundaries of a regime. The scope of a regime refers to the number of issues and transactions subject to regime discipline.\textsuperscript{28} The boundary of a regime refers to where a regime begins and ends, or alternatively, to the distinction between regime-governed and nonregime-governed behaviour.\textsuperscript{29} It has been noted that the equation of generalized patterns of behaviour with the existence of a regime "runs the risk of conflating regularized patterns of behaviour with rules, and almost certainly overestimates the level of normative consensus in international politics."\textsuperscript{30} Indeed, it is argued that regimes are "examples of cooperative behaviour, and facilitate cooperation, but cooperation can take place in the absence of established regimes."\textsuperscript{31} Keohane's

\textsuperscript{28} Aggarwal in \textit{Liberal Protectionism}, p. 21 defines regime scope as "the range of issues or products regulated by the regime." Haggard and Simmons in \textit{Theories of international regimes}, p. 497 also define regime scope in terms of the range of issues covered by the regime.

\textsuperscript{29} Kratochwil and Ruggie in \textit{International organization,"} p. 763 refer to "boundary conditions" as "Where does one regime end and another begin? What is the threshold between nonregime and regime?"

\textsuperscript{30} Haggard and Simmons, \textit{"Theories of international regimes,"} p. 493.

\textsuperscript{31} \textit{Ibid.}, p. 495.
distinction between harmony and cooperation suggests that some regularities in state action may reflect norm governed behaviour but others may not.\textsuperscript{32} This problem would appear to pose severe limitations to the explanatory capabilities of generalized practices and customs and implicit understandings. However, it is submitted that this statement of the problem relies upon a lack of conceptual clarity as to the underlying model of law and theory of obligation relied upon.

The problem of differentiating between regime and nonregime governed behaviour (i.e., determining the boundaries of a regime) may be said to lie in "the explicitness of commitment required before a regime can be said to exist...."\textsuperscript{33} Reliance upon "implicit regimes," it is said, "begs the question of the extent to which state behaviour is, in fact, rule-governed."\textsuperscript{34} There is thus a tendency in regime analysis to rely upon more explicit regimes and to formulate regime standards in terms of injunctions and constraints, which are more amenable to proof.\textsuperscript{35} Implicit in both tendencies is reliance upon positivistic methods of legal and scientific reasoning and

\textsuperscript{32} After Hegemony, pp. 51-7.

\textsuperscript{33} Haggard and Simmons, "Theories of international regimes," p. 494.

\textsuperscript{34} Ibid.

\textsuperscript{35} See for example Keohane, International Institutions, p. 4 for the limitation of regimes to "explicit regimes." And see the references cited in notes 68-70 below.
upon the command theory of law. Both theoretical underpinnings will be discussed at greater length in Chapter VII. However, for the moment it will suffice to note that both tend to demarcate the boundaries of regimes according to explicitly formulated injunctions, thus omitting standards that have evolved through custom and practice, but that are not explicitly formulated. Furthermore, both tend to ignore standards that operate, not as constraints, but as permissions and entitlements or as secondary rules. These tendencies have implications for the factors to be considered in defining the nature of a regime. The nature of a regime has been defined "by the prominence or weight given to various principles that shape a regime's norms, rules, and decision-making procedures."36 A regime limited by definition to explicit injunctions and prohibitions will exhibit a different nature and normative content than one accommodating less formally articulated standards and a greater variety of rule types.

Clearer conceptual distinctions between different types of regime standards and rules will assist in clarifying the boundaries of a regime and will illustrate the theoretical limitations of command theories of law and of positivistic analysis. It will also assist in understanding the uncertain role that obligation plays in regime analysis. It is generally accepted that regime governed behaviour

involves a 'sense of obligation.' However, the nature and role of this sense of obligation are uncertain. Krasner states that "regime-governed behavior must not be based solely on short-term calculations of interest. Since regimes encompass principles and norms, the utility function that is being maximized must embody some sense of general obligation."\textsuperscript{37} Indeed, Hart shows that the characteristic that distinguishes mere convergent habitual behaviour from behaviour guided by rules is that the latter involves a continuing recognition of its bindingness.\textsuperscript{38} A habit may merely reflect the convergence or identity of behaviour, which Hart argues is insufficient to constitute a rule. Legal rules require the general recognition that they are obligatory. But what generates and sustains the feeling of obligation? Another way of stating the problem is what are the criteria and determinants of regime strength? The measurement of strength "by the degree of compliance with regime injunctions"\textsuperscript{39} errs in limiting regime standards to restraints and prohibitions and implicitly invokes the command theory of law and all of the limitations it admits.

\textsuperscript{37} "Structural causes and regime consequences: regimes as intervening principles," in Krasner, ed., \textit{International Regimes}, p. 3.

\textsuperscript{38} \textit{The Concept of Law}, chap. 4.

\textsuperscript{39} Haggard and Simmons, "Theories of international regimes," p. 494.
The discussion will now turn to the various conceptual components of a regime. In defining regime principles, norms, and rules, the discussion will show that the definitions adopted have implications for determining the boundaries and nature of a regime and for developing an appropriate test of regime strength.

Regime principles, as stated above, are defined in terms of beliefs of fact, causation, and rectitude and are generally regarded as being of higher order than norms, rules, and decision-making procedures. Regime principles have been defined in terms of the "purposes that their members are expected to pursue" and as "general guidelines that concern how states should behave in international issue areas." As MacCormick notes, "legal principles are the meeting point of rules and values." Principles "express the underlying purposes of detailed rules and specific institutions, in the sense that they are seen as rationalising them in terms of consistent coherent and desirable goals." Principles are the foundations from which regime norms, rules, and decision-making procedures are derived. However, principles are cast at a higher level

of generality than are derivative norms and rules and exhibit greater flexibility.

Principles are practically context-free standards that can but need not be invoked in arriving at a decision. (Thus they allow for considerable discretion.) Rules, on the other hand, provide more direct guidance; they specify classes of events to which they apply in an all-or-nothing fashion as long as the empirical circumstances for which the rule was designed prevail. Each rule has its own "scope," usually specified in the rule's preamble. Principles are not only higher-order norms because of their lack of specificity, but also much more flexible [sic].

Dworkin argues that the different properties of principles (greater generality and flexibility) derive from the fact that principles and rules are logically distinct; they operate differently and have different origins.

The difference between legal principles and legal rules is a logical distinction. Both sets of standards point to particular decisions about legal obligation in particular circumstances, but they differ in the character of the instruction they give. Rules are applicable in an all-or-nothing fashion. If the facts a rule stipulates are given, then either the rule is valid, in which case the answer it supplies must be accepted, or it is not, in which case it contributes nothing to the decision.

In contrast, principles are more open-ended and "do not set out legal consequences that follow automatically when the conditions provided are met." Raz echoes the view that


46. Ibid.
principles provide flexibility, while rules provide certainty.

Principles, because they prescribe highly unspecific acts, tend to be more vague and less certain than rules. On the other hand, and for the same reason, they are particularly suitable for incorporating into the law very general goals and values, whereas rules are more apt to reflect more concrete considerations which apply to concrete situations....[rules] are more certain than principles and lend themselves more easily to uniform and predictable application.\(^47\)

Principles thus form the foundation for the creation, interpretation, and alteration of rules and the basis for generating exceptions to rules.

In addition to operating differently, principles have different properties than rules. Dworkin argues that "principles have a dimension that rules do not - the dimension of weight or importance."\(^48\) Principles have counter-instances which can be given different weights. For example, the principle of freedom of contract intersects or conflicts with the principle of consumer protection. "When principles intersect...one who must resolve the conflict has to take into account the relative weight of each."\(^49\) Rules, in contrast do not conflict. If they do, one will constitute an invalid rule or, alternatively, the conflict


\(^{48}\) "Model of Rules," p. 27.

\(^{49}\) *Ibid.*
will produce a dramatic alteration of standards.\textsuperscript{50} Dworkin states that one of the reasons "for drawing the distinction between rules and principles was just to show how rules often represent a kind of compromise amongst competing principles in this way..."\textsuperscript{51}

That principles may conflict and that actors may differ over the priority accorded to divergent principles has been recognized in regimes literature.\textsuperscript{52} Indeed, it is argued that norms embody the standards and practices that emerge from the conflict between actors over the primacy accorded to competing principles.\textsuperscript{53} As Kratochwil notes "we know that effective regimes, such as constitutions, frequently show important discontinuities between specific norms and higher principles, quite aside from the fact that many of the higher principles are expressions of competing values. Liberty and equality can give rise to mutually contradictory prescriptions, and a variety of more special regulations


\textsuperscript{51} Ibid., p. 888.

\textsuperscript{52} For a discussion of the hierarchical arrangement of principles, norms and rules and of the often contradictory nature of principles see Zacher, "Trade gaps," pp. 174- 8.

\textsuperscript{53} Ibid.
might be compatible with the same higher norm or principle."\textsuperscript{54}

A further characteristic that differentiates principles from rules (and norms) is that principles have a different origin and thus require a different test of validity or pedigree. "The origin of...legal principles lies not in a particular decision of some legislature or court, but in a sense of appropriateness developed in the profession and the public over time. Their continued power depends upon a sense of appropriateness being sustained."\textsuperscript{55} Thus we speak of principles as being eroded, while rules are overruled or repealed. Rules are either valid or invalid, while principles are neither, but are regarded as either influential or uninfluential. Principles, unlike rules, are not created by single enactments or judgments, but evolve more like customs.\textsuperscript{56} Indeed, Dworkin cites the law merchant as an example of a collection of ancient legal rules that "were never explicitly created by a legislature or a court. When they made their first appearance in legal opinions and texts, they were treated as already being part of the law because they represented the customary practice of the community, or some specialized part of it, like the business

\textsuperscript{54} Rules, Norms, and Decisions, p. 62. The author here regards principles to be higher order norms, as distinct from more specific rules.

\textsuperscript{55} Dworkin, "The Model of Rules," p. 41.

\textsuperscript{56} Raz in "Legal Principles and the Limits of Law," p. 848 also recognizes the evolutionary nature of principles.
community." Dworkin suggests that legal positivists, who define law as a "system of rules", are unable to account for principles, which have an inherently social, intersubjective, and sometimes customary basis. As such they are not traceable to some positive legislative or judicial act. Moreover, this analysis suggests that it is inappropriate to conceive of principles as being amongst "injunctions at various levels of generality," for principles do not enjoin or command. As Zacher notes "[b]ecause states usually differ on the importance they assign to principles in designing rights and obligations, principles should not be regarded as injunctions that states feel obligated to follow in the same sense that they feel committed to norms, rules, and decision-making procedures. Principles are guidelines that states think should have 'some role' in shaping specific prescriptions and proscriptions."  

Norms, in comparison, are defined as 'standards of behaviour defined in terms of rights and obligations.' Norms exhibit greater specificity than do principles, but are regarded as being "the most general injunctions that constitute the core of a regime," when compared to rules and

decrease-making procedures. Moreover, like Dworkin's rules and unlike principles, norms "are the products of explicit or implicit political bargaining and do not conflict with each other." 60

It should be noted here that the regime definition under discussion differentiates between norms and rules, the latter constituting even more specific prescriptions and proscriptions. However, many legal theorists use norms and rules almost interchangeably. Indeed, von Wright observes that "the field of meaning of 'norm' is not only heterogeneous but also has vague boundaries." 61 In identifying different types of norms, von Wright observes that a hierarchy of norms exists. 'Norms of a higher order' are analogous to principles, as we have here defined them, while many of the lower order norms are comparable to more specifically formulated rules. Kratochwil notes that while he uses "the terms "norms" and "rules" interchangeably," rules and norms differ. 62 He argues that all rules are norms, but not all norms are rules. Some norms (i.e., 'higher order norms') are more like principles, in that they are less specific and more flexible. Kratochwil, thus,

60. Ibid., p. 177.

61. Norm and Action, chap. 1 von Wright differentiates between norms, identifying several types of norms: norms as rules of the game that define or determine a practice; norms as prescriptions; norms as directives; norms as customs or social habit; norms as moral principles; and, norms as ideal rules.

appears to adopt a broader conception of norms, not unlike that of von Wright. Furthermore, Kratochwil echoes Dworkin's conceptualization of the unique character of principles.\textsuperscript{63}

It is submitted that defining norms in a broad, inclusive sense and then differentiating between principle-like norms and rule-like norms lacks sufficient conceptual clarity. We have seen that principles operate in a distinctive manner and have peculiar origins. Thus it is necessary to distinguish between principles and rules. But norms and rules too have distinguishing characteristics and must be differentiated. Norms are standards of behaviour defined in terms of rights and obligations that are widely regarded as legitimate and binding.\textsuperscript{64} Norms may emerge from explicit or implicit political bargaining over competing principles or through customary practice. One does not speak of a norm or practice as being valid or invalid. While norms may change in response to the changing emphasis given to intersecting principles, they derive their validity from the general recognition of their bindingness. Rules, in contrast, are formulated more specifically and absolutely in terms of conditional "if...then" statements. Rules are either valid or invalid; they either apply or do not apply to a given set of facts. Furthermore, rules take different

\textsuperscript{63} See text accompanying notes 48-54 above.

\textsuperscript{64} Keohane, \textit{After Hegemony}, p. 57 and Barkun, \textit{Law Without Sanctions}, p. 63.
forms which exhibit "characteristic differences in the incentives for compliance." Recall for a moment Hart's distinction between primary and secondary rules and Rawl's identification of practice-type rules. We may identify regulative rules, which are typically expressed in terms of imperatives or commands and prohibitions, and institutional rules, which as secondary rules and practice-type rules function as constitutive rules. The former constrain, inhibit, and limit, while the latter facilitate, enable, or empower and permit. Command theories of law may well account for the source of obligation underlying regulative rules, as in the command of a sovereign backed by the threat of sanctions, but they do not account for the binding character of institutional or practice-type rules. It has been noted that "the conception of law as a coercive order needs revision. The efficacy of the law cannot be assessed simply in terms of the compliance or noncompliance with prohibitions.... Actors, in the domestic as well as the international order, are not simply constrained by rules. Rules enable them to act, to pursue goals, to communicate, to share meanings, to criticize claims and justify actions." 67


The above discussion suggests that the test of regime strength should reflect important differences between rule types. It also suggests that it is inaccurate to define regime standards in terms of injunctions, though certainly some rules do function to enjoin or command conduct. Furthermore, the discussion suggests that the identification of the scope or boundaries of a regime must reflect the variable origins of regime standards. Standards that have their origins in explicit bargaining should not be regarded as defining the scope and boundaries of a regime. Standards that have evolved through the customary practices of actors also figure in determining regime scope and boundaries. Furthermore, defining the nature and normative content of the regime should reflect the fact that regime standards originate and operate differently. The discussion will turn now to a closer examination of the test of regime strength.

Various criteria for evaluating the strength of a regime have been identified. Many tend to focus upon the ability of regime injunctions to constrain behaviour. Strength "refers to the stringency with which rules regulate the behavior of countries,"68 "the extent to which the package of injunctions constrains states' behavior,"69 and

68. Aggarwal, Liberal Protectionism, p. 20.
the effectiveness of incentives to comply. In addition, the specificity or clarity with which regime standards are formulated and coherence among regime components are regarded as indicators of regime strength. Strong regimes are those with "clear rules and effective incentives to comply" and will exhibit tight linkage between principles and rules.

In contrast, a weak regime "involves incoherence among the components of the regime or inconsistency between the regime and related behavior." However, the identification of the effectiveness of constraining mechanisms, the clarity and specificity of rules, and coherence of regime components as the criteria of regime strength pose some problems. To begin with, we have already considered the fact that not all rules operate as constraints and prohibitions. Some rules operate as permissions and entitlements, thus performing a facilitative not a prohibitory role. The test of compliance with prohibitions or constraints is not relevant or appropriate for facilitative rules. "Although prohibitions are adequately represented as constraints, rules that empower or enable are not. Thus while enforcement according to the 'cops and robber' model of criminal law may increase compliance with a certain type of prescription, and thus the

70. Keohane, After Hegemony, p. 239.

71. Ibid., pp. 59 and 239.

effectiveness of a certain part of the legal order, it is clearly irrelevant to the compliance patterns of enabling rules. "73 Contractual or promissory obligations cannot be adequately explained by the command theory of law which focuses upon the constraining nature of rules. 74 The performance of contractual obligations stems from trust. "Trust in the system is guaranteed by the intersubjectivity of the rules defining practices, such as promising and contracting." 75 While some regime standards will operate as prohibitions and thus submit to the test of constraint, the efficacy of promissory obligations must be determined according to different criteria. Reference to the proclivity of actors to voluntarily submit their activities to regime discipline, as evidenced by their conduct and practices, is a more appropriate criterion for determining the strength of promissory obligations.

In addition, a related problem arises in identifying clarity and specificity of regime rules as criteria of regime strength. The tendency to equate clear and specific rules with strong regimes may tend to minimize the significance of practices and customs that are less formally explicated, but of considerable influence. 76 This is of

74. See Hart, The Concept of Law, chaps. 2 and 3.
76. Haggard and Simmons, in "Theories of international regimes," p. 495 note that the tendency to focus upon
importance in defining the scope and nature of the regime as well. If the test of strength turns in part upon the clarity and specificity of regime standards, the influence of informal practices will be minimized. Regime scope and nature will thus tend to be limited to areas of positive agreement amongst actors. The tests of the strength or efficacy of positive law and customary law differ. We have already noted the inability of legal positivism to account for the binding nature of customary law. As Dworkin notes, legal positivism is a doctrine for and about rules and positive law, not about standards that have their origins in custom and practice. While the limits of positivist analysis will be further considered in Chapter VII, for the moment it is sufficient to note that while the specificity and clarity with which regime rules are formulated may be regarded as indicators of strength, they should not obscure the value of less formally articulated and more ambiguous standards. Indeed, much of the strength of the law merchant has derived from the assurance of sufficient flexibility for actors to interpret and adapt regime standards to meet their changing needs. Nor should the emphasis upon clarity and explicit injunctions "risks the charge of formalism - a charge which has plagued international law."

77. "The Model of Rules." See also von Wright, Norm and Action for a discussion of the inability of legal positivism to account for the obligatory nature of customary law.
specificity obscure the reality of the 'penumbra of uncertainty' attending every legal system.

The final objection to identifying the coherence of regime components as a criterion of strength touches upon similar considerations. Recall the discussion of the often conflicting nature of regime principles and the nature of rules as embodying the norms emerging as bargains or trade-offs between conflicting principles. Rules will be consistent with some principles but not all principles. Thus, one cannot expect congruence or coherence between all rules and principles. Indeed, Kratochwil notes that "it is the inconsistency and the value opportunism of the legal order that prevent us often from knowing what "the law" is until a court has authoritatively established a link between rules and principles, or between conflicting rules themselves."78 He concludes that the "strength of a regime, therefore, does not seem to result from the logical neatness of relating rules and higher principles to each other, but rather from the deference to authoritative decisions that establishes what "the law" is, or from the acceptance of norm-regulated practices."79

In formulating the appropriate test or criteria of strength, reference must be made to the distinction between

the substantive and procedural dimensions of the regime. With regard to the substantive dimension of a regime, strength may be assessed in terms of the comprehensiveness of the scope of issues and transactions subject to regime discipline. Subject to the considerations just noted, regime strength may also be assessed in terms of the specificity with which rules are formulated and the degree of legitimacy that actors accord to them. A related concern is the extent to which perceptions of legitimacy are generally shared or universal. Strength may also be assessed by the degree of compliance with regime injunctions or adherence to voluntary rules. A strong regime, substantively, will reflect comprehensive coverage of regime issues, though these standards may exhibit varying degrees of formal or specific explication. It will also reflect widespread acceptance and legitimacy of regime standards, as evidenced by general adherence to regime injunctions and uniformity in acceptance of voluntary and enabling rules.

Procedurally, strength may be assessed in terms of the ability of a regime's decision-making authorities to make binding and authoritative decisions. A strong regime, procedurally, will reflect the presence of secondary rules governing the creation, modification, and extinction of regime standards and the general recognition of their legitimacy. These rules will also identify legitimate

80. This discussion draws heavily upon Zacher, "Trade gaps."
agents of law creation. The ability to identify secondary, constitutive rules in the private international trade regime has significant implications for characterizing the regime. It suggests that it is inappropriate to characterize this regime as a primitive legal order, lacking secondary rules which are regarded as present only in advanced legal systems. Moreover, it raises the possibility that this regime is a specie of international law that has developed beyond the primitive level attributed by many to international law. The criteria of strength will be further elaborated after the following overview of the private international trade regime.

Before proceeding, however, it should be noted that regimes analysis also affords important insights into the processes of regime creation and transformation and identifies significant factors influencing regime nature, scope, and strength. A number of explanatory approaches are available. While these approaches have been variously described, this dissertation will focus upon two theoretical approaches that have attracted considerable attention, namely structural realist and functional analyses, and one

which is only recently attracting attention and has been described as a sociological approach. These approaches will be the subject of Chapter III.

We will turn now to consider the substantive and procedural dimensions of the regime in greater detail, beginning with the scope of the regime and then proceeding with a consideration of its nature and strength.

B. OVERVIEW OF THE PRIVATE INTERNATIONAL TRADE LAW REGIME

1. Regime Scope: Constituent Issues

A number of key substantive and procedural issues constitute the core of the regime governing private international trade. While the scope of the transactions covered by the regime has broadened over its three phases, a number of issues have over time provided the regime with a fair degree of coherence. These issues derive from the very nature of exchange involved in commercial transactions relating to contracts for the international sale of goods.

In international trade, the sales contract is the core of an export-import transaction. It is however, always supported by several other related contracts, reflecting the complexity of the transaction and the number of parties involved. Basic among these additional contracts are, first, the contract of carriage by sea or air, under which goods are transported from one country to the other. Secondly, there is the contract of marine or air insurance, by which parties protect themselves from the risks of loss or damage to the goods in transit.²²

To this list of supporting contracts must be added the contracts governing the financing and payment of the transaction.

Commercial sale of goods transactions involving non-simultaneous exchange over time and space give rise to specific concerns relating to the allocation of risks and specification of obligations in contracts of sale, transportation, insurance, and payment and to concerns over the enforcement of contracts and dispute resolution. At issue is the identification and enforcement of the performance obligations and property rights of buyers and sellers and the determination of the nature and scope of their respective liabilities and the liabilities of third party lenders and insurers at various points during the contract of sale. Underlying these issues is the more fundamental concern with the allocation of risks posed by opportunistic behaviour and unforeseen circumstances in transactions involving non-simultaneous exchange.83

These concerns are reflected in the regimes key substantive and procedural issues.84


84. As is the practice with most analyses of private international trade law, this dissertation focuses primarily upon the international contract of sale. The supporting contracts of transport, insurance, and
concern the specific standards governing contracts of sale, transport, insurance, and finance. The key substantive issues relating to the core contract of sale include the regulation of prices and liabilities for defective goods. Relating to the supporting contract of transportation, the key substantive issue concerns the allocation of the costs of transportation. The substantive issue relating to the contract of insurance concerns the allocation of risks of loss or damage to goods in transport, while the regulation of financing and credit arrangements is the key issue relating to the contract of payment. As will become evident, many of these issues are interrelated and overlap.

**Procedural issues** concern the identification of the appropriate agents and processes for creating and enforcing rules governing the various components of an international sales transaction and governing the resolution of disputes arising from the transaction. The key procedural issues include the locus of regulation, including rule creation and enforcement; the methodology of rule creation, including the sources of law and coordinative strategies; and, the processes and institutions governing dispute settlement.

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finance are considered only insofar as they contribute to the main sales contract and facilitate the sales transaction. Accordingly, the analysis of the supporting issue areas, each arguably a dissertation unto itself, will not be as detailed as the analysis of the central or main issue area.
Turning first to the key substantive issues, these issues concern standards governing merchants and third party lenders, insurers, and transporters in the creation of enforceable bargains that allocate risks in contracting through the specification of performance obligations and liabilities and by establishing property rights in the goods.

The first substantive issue is that of price regulation and relates to the standards to be applied to the determination of prices in commercial sales agreements. The different standards applied to price-setting reflect a tension between the regime principle that views commercial exchange in terms of equitable purposes and that which views exchange in terms of facilitative purposes.

This tension between different views of the nature and purpose of the exchange relationship is also evident in the second substantive issue concerning the nature and scope of merchant liability for defective goods. Whether vendors should be held to standards of strict or limited liability for defective goods reflects a tension between the equitable and facilitative functions of exchange. These standards governing liability for defective goods have changed over the history of the regime, reflecting a different weighting of regime principles.

The third substantive issue, which concerns the allocation of the costs of transportation, relates to standards imposed upon or voluntarily adopted by merchants
to regulated their respective liabilities for transportation costs. Throughout the history of the law merchant, merchants have regulated transport costs through uniform customary practices establishing clear liability rules.

The fourth substantive issue concerns the availability of standards and insurance practices regulating the allocation of loss or damage to goods while in transit. Merchants have utilized the practice of insuring against losses, throughout the course of the evolution of the trade regime, relying upon uniform standards that exhibit considerable consistency over time.

The fifth issue relates to the regulation of financial and credit arrangements and concerns the standards and practices regulating payment arrangements and the ability of merchants to charge interest on commercial loans. From the earliest days of the regime, merchants devised uniform mechanisms for financing sales transactions and these mechanisms today form the foundations of modern exchange. In addition, the prohibition of usury, present in the early days of the regime, was not uniformly enforced and over time gave way to a more permissive attitude.

Turning next to the first procedural issue, the locus of regulation refers to the identification of the legitimate agent(s) for rule creation and enforcement. At issue here is whether the determination of the content and formal requirements of contracts and their enforcement should be the domain of merchants, local and state authorities, or
international organizations. As will be discussed in the next section, regime norms regarding the locus of regulation have changed markedly over the three phases, reflecting the predominance of different principles. The nature and extent of government regulation of the formation and content of commercial transactions and of the processes of enforcement and dispute resolution have changed over time, as too has the role of international organizations.

The second procedural issue concerns the **methodology of rule creation** and relates to the generally accepted methods for creating regime standards and binding rules. This issue comprises two closely related sets of considerations. The first may be referred to as the **sources of law** and refers to the origin of regime standards. The issue is whether legitimate regime standards derive from customary law and practice or from positive law in the form of national laws and international treaties and conventions. The legitimacy accorded to the different sources of law has changed throughout the history of the regime, reflecting a change in the weight given to regime principles. The second set of considerations may be referred to as the **coordinative strategies** adopted by regime actors in the development of regime standards.

Actors have adopted four distinct strategies to coordinate commercial exchange which, in turn, reflect the dominant or accepted sources of the day. The first strategy places emphasis on the development of uniform merchant
practice and was common in the early phase of the regime, reflecting the widespread legitimacy of merchant custom as a source of law. The second strategy involves reliance upon national systems of conflicts of law which regulate transactions containing a foreign element. This strategy dominated the second phase of the regime and reflected the predominance of the principle of state intervention and reliance upon national positive law as a source of law. The third strategy involves the unification of national conflicts of laws rules, while the fourth strategy involves a more extensive and difficult process of unifying substantive rules of national commercial law by international conventions or model laws. The latter strategy, relies on positive international law as a primary source of law, though in some instances it is customary law that forms the basis for unification efforts. The emphasis given to different coordinative strategies has also changed over the development of the regime, again reflecting different weighting of regime principles.

The final procedural issue concerns the processes and institutions governing dispute settlement. This refers to the generally accepted means for resolving commercial disputes. Recourse to private means of dispute resolution, like private arbitration, may be distinguished from the resolution of disputes in national courts under national

85. See generally David, "The International Unification of Private Law."
legal systems. This too is an issue that has been subject to changing norms over the course of the regime's evolution.

We will now turn to consider the nature and normative foundations of the regime by reviewing the principles and norms that inform the substantive and procedural dimensions of the regime.

2. Regime Nature: Relevant Principles

The nature of the regime governing commercial relations is determined by the normative structure or orientation of the procedural and substantive dimensions. The regime's normative structure is in turn determined by the principles accorded primacy by regime norms and rules. The weight given to regime principles has often changed over the course of the development of the regime and a number of principles have competed for primacy. The principles are listed below in Figure 1 and then described. The reader is directed to Appendix A for a summary description of the regime principles.

FIGURE 1

REGIME PRINCIPLES

Principles Relating to the Purposes of the Regime:
- Facilitation of Exchange
- Political Autonomy
- Equity

Principles Relating to the Substantive and Procedural Dimensions:
- Market Allocation
- Merchant Autonomy
The facilitation of exchange principle provides that the purpose of regulating commercial transactions is to facilitate the expansion of commercial exchange by providing a permissive regulatory framework which enhances the efficiency of commercial transactions. This may be achieved through the reduction of the costs of doing business (i.e., information costs, transaction costs, and enforcement costs) and the uncertainties that attend nonsimultaneous exchange (i.e., protecting expectations by controlling opportunistic behaviour and unexpected risks). Certainty and costs go to the very heart of commercial exchange. The ability for commercial actors to be reasonably sure of their performance obligations, property rights, and liabilities at different points in a transaction and under different national legal systems is central to the exchange relationship. In addition, the ability to enforce agreements without the imposition of unnecessary constraints on commercial flexibility is a central concern. All national legal systems recognize these concerns in one way or another. However, the emphasis placed by the private international trade law regime on the facilitation of efficient exchange has changed over the course of its development. The value placed upon the facilitation of exchange has at times been
subordinated to the value that local and national authorities placed on the principle that commercial regulation should enhance the political autonomy of states by promoting the achievement of national or local goals and policy concerns. In addition, at times the facilitation principle has given way to the equity principle. Though the equity principle has been subject to different formulations, it identifies the main purpose of commercial regulation as the promotion of fairness and equality in exchange. Some formulations go further to endow the regulation of the exchange relationship with a redistributional function.

The facilitation principle is closely related to the market allocation principle and the principles of merchant autonomy and freedom of contract. The market allocation principle provides that the expansion of commerce can best be achieved by allowing market forces to determine the most efficient allocation of resources. Market forces, as opposed to considerations of equity, should determine the creation, substantive content, and enforcement of commercial agreements. Prices, earnings, liabilities, dispute settlement, and the like should be left to merchants to determine in the context of market conditions.

The principle of merchant autonomy provides that merchants are the legitimate agents for creating binding promissory obligations and should be free to conduct business by entering into contracts creating legal obligations and to enforce those obligations without
external interference. Autonomy in its broadest sense extends to determining the substantive content of agreements, in addition to the procedures governing creation, interpretation, evidentiary requirements, and enforcement. While the principle of freedom of contract is related to the principle of merchant autonomy, in that it embodies the right of merchants to freely enter into exchange relations, it is inspired by free market principles which appeared a considerable time after the formulation of the principle of merchant autonomy. The modern formulation of freedom of contract provides that the most efficient allocation of resources is achieved by according broad scope for merchants to determine the nature of their contractual obligations. Merchants should be free to create contractual obligations which will be enforced by the law, subject only to certain limited exceptions. While the principles of merchant autonomy and freedom of contract are today considered to be closely related as reflecting liberal, free market values, it is important to note that the former principle took on this character later with the development of capitalism and the advent of liberal values.

In contrast, the state or local intervention principle, identifies local or state authorities as legitimate agents of rule creation and vests such authorities with the power to determine the content of agreements and the procedures and conditions governing their creation, interpretation, and enforcement. Such interventions may embody equity concerns,
concerns of moral rectitude, or matters of public policy, and reflect the belief that reliance on market mechanisms may not produce outcomes consistent with national policy goals. Similarly, the international intervention principle provides that the facilitation of exchange and satisfaction of equity concerns in commercial transactions requires the intervention of international bodies. International organizations are thus regarded as legitimate agents for creating and unifying commercial law.

The principle of the sanctity of contracts or pacta sunt servanda provides that promissory obligations freely entered into by competent parties are enforceable in national courts and in private arbitrations, subject to national public policy limitations.

The informality principle provides that the most efficient allocation of resources is achieved through avoiding the imposition of formalities on the creation and enforcement of commercial agreements. It also recognizes the value of ensuring sufficient flexibility for merchants to devise the means for adapting to changing circumstances and commercial needs and thus is related to the principles of merchant autonomy and freedom of contract.

Finally, the arbitration principle provides that commercial expectations are best protected through the process of arbitration, which allows the parties considerable independence and flexibility in dispute settlement. The principle stipulates that merchants submit
their disputes to international arbitration under the law chosen by the parties and requires state authorities to recognize and to enforce arbitral decisions. The adjudication principle, in contrast, identifies national courts operating under national legal systems and formal laws of procedure as the appropriate venue for dispute resolution and enforcement.

Certain principles have at times taken precedence over others, affecting the scope, nature, and strength of the regime. For example, the free market principle of freedom of contract and the principles of merchant autonomy and the sanctity of contracts today, with some exceptions, constitute the normative foundations of the regime. So too do the facilitation of exchange and market allocation principles. In addition, elements of the informality principle are today present. However, this has not always been the case. Market interventions by domestic and international authorities setting limits to the substantive content of agreements and prescribing procedures for the creation of binding obligations have been made on equitable, moral, and public policy grounds.

Shifts in the priority attached to regime principles reflect changing standards of legitimacy concerning the normative foundations of the regime. We will now consider the variable weight given to these principles in light of the norms regulating the substantive and procedural
dimensions of the regime. Figure 2 provides a summary of
the normative structure of the regime. The remainder of the
chapter outlines the normative structure and is intended to
provide the reader with a guide to subsequent chapters that
deal with the subject-matter in greater detail.

[Figure 2 about here]

See pp. 62 i–vi.

3. Normative Structure of the Regime: Substantive Dimension

Prices. The standards regulating prices and earnings
have varied depending upon the nature of the sales
transaction. During the first phase, the norm for
international transactions was generally price-setting by
the agreement of the parties to a sales contract
(contractual prices). However, for domestic transactions
the norm was for prices, and ultimately earnings, to be
fixed by local market authorities. In keeping with the
equity principle, the principle of local intervention, and
the political autonomy principle, local political and
religious authorities fixed prices for local and retail
transactions utilizing the standard of the ‘just price’.
Local and retail transactions were unenforceable if they did
not conform to fixed prices, and in cases where prices were
not fixed, there had to be equivalent value exchanged.
Similar discipline did not generally extend to foreign and
Figure 2
NORMATIVE STRUCTURE

Substantive Dimension

Prices

Phase I: Norm of *contractual prices* for international (foreign and wholesale) transactions. Reflects dominance of the following principles: merchant autonomy and the facilitation of exchange.

- Norm of *just prices* for domestic (local and retail) transactions: Prices fixed by local authorities utilizing the standard of a "just price." Reflects dominance of the following principles: equity, local intervention, and enhancing political autonomy through the achievement of local goals.

Phase II: Norm of *contractual and market prices* for domestic and international transactions. Prices fixed generally by contract or by market conditions. Reflects dominance of the following principles: facilitation of exchange, market allocation, merchant autonomy, and freedom of contract.

Phase III: Norm of *contractual and market prices* for international transactions. Prices in international transactions fixed generally by contract and by market conditions. Attempts to revive notion of "just price" in international transactions generally unsuccessful. Reflects the dominance of the following principles: facilitation of exchange, market allocation, merchant autonomy, freedom of contract, sanctity of contract, and international intervention.

Variable norms governing prices in different states for domestic transactions.

Liability for Defective Goods

Phase I: Norm of *limited liability* for international transactions. Reflects the dominance of the following principle: law merchant standards of equity.

- Norm of *strict liability* for domestic transactions. Vendors held to standards of strict liability for defective goods. Reflects the dominance of the following principles: canonical notions of equity, local intervention, and enhancing political autonomy through the achievement of local goals.
Phase II: Norm of limited liability for domestic and international transactions. Vendors' liability for defective goods limited in most jurisdictions, but some variation in liability standards. Reflects the dominance of the following principles: facilitation of exchange, freedom of contract, merchant autonomy, and market allocation.

Phase III: Norm of limited liability for international transactions. Vendors' liability for defects still limited, but greater time now given for purchasers to inspect. Reflects the dominance of the following principles: As in Phase II except for moderate influence of the equity principle and authoritative international intervention in the extension of inspection time.

Norm of strict liability for domestic transactions in some states. Reflects the dominance of the following principles: political autonomy, equity, and state intervention.

Allocation of Transport Costs and Liabilities

Phase I: Norms of the adoption of uniform merchant standards and limited liabilities. Standards determined by contract with reference to commercial custom. Liability contingent on fault. Reflects the dominance of the following principles: facilitation of exchange, merchant autonomy, and law merchant notions of equity.

Phase II: Norms of uniform merchant standards and limited liability persist, but some differences arise with development of national standards. Considerable freedom for merchants to regulate transport liabilities and obligations. Reflects continued, but weakened dominance of the following principles: facilitation of exchange and merchant autonomy. Increasing strength of principles of state intervention and political autonomy.

Phase III: Norm of uniform international standards, but variable state standards persist. Expansion of international usage of voluntary, non-binding statements of commercial custom and proliferation of international conventions and model laws governing new modes of transportation. Reflects the dominance of the following principles: facilitation of exchange, market allocation, merchant autonomy, and freedom of contract. Continuing influence of principles of state intervention and political autonomy is evident.
Insurance

Phase I: Norm of uniform merchant standards apportioning risk and limiting liabilities. Merchant customs regulated insurance. Reflects the dominance of the following principles: merchant autonomy, and the facilitation of exchange.

Phase II: Norm of similar state standards, although some variation in state standards appear. States regulate insurance, though many incorporate commercial customs into national laws and private insurance companies continue to develop customary standards. Reflects the dominance of the following principles: state intervention and political autonomy.

Phase III: Norm of some uniform international standards. Private actors engage in codification of custom but not in a comprehensive way. There are little or no intergovernmental regulatory efforts. Reflects the dominance of the following principle: merchant autonomy.

Financing and Credit:

Phase I: Norm of uniform merchant standards. Merchants devise uniform procedures and documents for financing transactions. The norm of charging interest on international financial transactions. Reflects the dominance of the following principles: facilitation of exchange, merchant autonomy, law merchant standards of equity, and market allocation.

Norm of the prohibition of usury for domestic transactions is weak. Local authorities prohibit lending at a charge, but methods of evading prohibition proliferate. Reflects the influence of the following principles: canonical notions of equity, enhancing political autonomy through the achievement of local goals, and local intervention.

Phase II: Norms of uniform standards and interest charges practiced by most states for international and domestic transactions. While states establish national payment procedures, many incorporate merchant custom. Some national differences emerge. Interest charges are permitted by most states. Reflects the dominance of the following principles: state intervention and enhancing political autonomy through the achievement of national goals. But state controls also emphasize the following principles: facilitation of exchange, merchant autonomy, and freedom of contract.
Phase III: Norm of uniform international standards. Proliferation of international financial and credit arrangements through international legislation and commercial custom. Interest charges permitted in most states. Reflects the dominance of the following principles: facilitation of exchange, merchant autonomy, freedom of contract, and international intervention.

Procedural Dimension

Locus of Regulation

Phase I: Norm of merchant control of international transactions. Reflects the dominance of the following principles: merchant autonomy, facilitation of exchange, and informality.

Norm of local control of domestic transactions. Reflects the dominance of the following principles: local intervention, enhancement of political autonomy through the achievement of local goals, and canonical notions of equity.

Phase II: Norm of state control of domestic and international transactions. States control formalities for creating and enforcing agreements, reflecting the dominance of the principles of state intervention, political autonomy, and formality. However, merchants retain significant control as states adopt principles of merchant autonomy, freedom of contract, and the facilitation of exchange.

Phase III: Norm of international control appears. Intergovernmental organizations engage in the unification of international commercial law. Reflects the dominance of the following principles: international intervention and the facilitation of exchange. State controls persist in significant areas, reflecting the continuing influence of the state intervention and political autonomy principles, but this norm is weakening. Merchant control is being strengthened through the creation of a predominantly permissive international regime, emphasizing merchant autonomy and informality.

Methodology of Rule Creation:

Sources of Law:

Phase I: Norm was the identification of merchant custom as the primary source of law governing international transactions, although local authorities did impose
legislative restrictions on local trade. Reflected the dominance of the following principles: facilitation of exchange, merchant autonomy, informality, sanctity of agreements, and arbitration. Some influence of the local intervention principle.

Phase II: Norm was the identification of positive national law as the primary source of law governing international commercial transactions. Reflected the dominance of the following principles: state intervention, enhancing political autonomy through the creation of national commercial legal systems, and formality.

Phase III: Norm is the identification of positive international law and national law as main sources of law. Revival of commercial custom as a source. Reflects the dominance of the following principles: facilitation of exchange, international intervention, merchant autonomy, and informality. Continuing influence of the state intervention and political autonomy principles is evident.

Coordinative Strategies

Phase I: Norm is the coordination of international commercial relations through uniform merchant practice. Reflects the dominance of the following principles: facilitation of exchange, merchant autonomy, and informality.

Phase II: Norm is the coordination of international commercial relations through national conflicts of laws systems. States regulate international commerce through nationally-based conflicts of law. Very limited attempts later in period to harmonize conflicts of laws rules. Reflects the dominance of the following principles: state intervention and political autonomy.

Phase III: Norm is the coordination of international commercial transactions through the unification of substantive rules of national law. States harmonize national laws and participate in international organizations engaged in the unification of commercial law utilizing international conventions and model laws. There has been a revival of uniform commercial custom and practice as a coordinative strategy, while national conflicts of law systems are still relied upon. The priority given to unification of substantive laws reflects the dominance of the following principles: facilitation of exchange and international intervention. The strengthening of uniform custom as a strategy reflects the growing importance of merchant autonomy and informality, while the declining
importance of unifying conflicts laws reflects the decreasing influence of the political autonomy and state intervention principles.

Dispute Resolution

**Phase I:** Norm was merchant dispute settlement and enforcement. Merchant control of dispute resolution and enforcement in private merchant courts/arbitrations and under merchant law. Reflects the dominance of the following principles: merchant autonomy, arbitration, and informality.

**Phase II:** Norm was national adjudication. State control of dispute settlement and enforcement in national courts under national legal systems. Merchant dispute settlement persists in some states. Reflects the dominance of the following principles: state intervention, political autonomy, formality, and adjudication.

**Phase III:** Norm is international arbitration. The revival of international arbitration with the assistance of international and national authorities reflects the growing influence of the following principles: informality, merchant autonomy, state intervention, and international intervention.
whole trade where merchants determined prices through contractual agreement.

During the second and third phases, the norm for local and retail trade was brought into line with that for wholesale and foreign trade as contractual prices became the norm. This reflected the growing influence of the principles of merchant autonomy, freedom of contract, and the facilitation of exchange. In deference to the principles of freedom of contract and the facilitation of exchange, common law courts adopted rules that precluded judicial evaluation of the equivalence of exchange and the prudence of bargains. In cases of underspecification of prices, reference was made to the current market price. While states have intervened to establish some statutory guidelines relating to fairness in contracting and the law has developed protections for incompetent and weaker parties, reflecting encroachments on market allocation by the equity and state intervention principles, these are considered exceptional derogations from the dominant free market principles. Contractual and market prices continue to dominate commercial transactions. While certain states have attempted to revive the notion of just prices, the regime continues to reflect the dominance of market oriented principles and the emphasis on the facilitation of exchange.

The degree of price specificity required in order to render a contract enforceable has changed over time. In the first phase the issue of price specificity did not arise in
most local transactions, for prices were determined by the local authorities. In instances where prices were not fixed, recourse was made to the "common estimation" of the value of the transaction. Price specificity became more of a concern in the second phase, with the advent of liberal, free market principles. The courts began to adopt the practice of adopting current market prices to render contracts enforceable in instances of underspecification. This reflected the dominance of the market allocation principle. In addition, it reflected the value placed upon the sanctity of contracts, for courts held that it was their duty to uphold agreements and give effect to the reasonable intentions of the parties. In instances where the parties made inadequate provision for price, this involved the judicial implication that they intended to contract at the 'fair market price', being the current market price. Price specificity has taken on greater significance in the third phase. Many states, in particular less developed and Eastern European states, believe that the enforcement of contracts in which prices are underspecified or left open works against them. They are asserting the need for international intervention to provide more rigorous standards for price determination and have made modest advances in this area.

*Liability for Defective Goods.* This issue concerns the extent to which merchants should be responsible for damages
arising from defective goods. As in the case of price regulation, different liability standards applied to foreign and domestic transactions. Under the law merchant, international transactions were subject to standards of limited liability. In contrast, merchants in domestic transactions were held to standards of strict liability and could avail of few defences.

During the second phase, the advent of free market principles served to dilute the scope of liability for defective goods. States came to limit liability, bringing state practice into greater accord with the law merchant. The norm was limited liability for defects in both domestic and international transactions. National differences, however, began to emerge in the strength of this norm. At the height of laissez-faire thinking, merchants were held liable for a very narrow class of defects. For common law jurisdictions, unlike civil law jurisdictions, the rule of caveat emptor, buyer beware, and rules establishing inspection obligations for purchasers, narrowed the scope of sellers' liability for defects. In addition, rules regulating the recovery of damages to only losses that were reasonably foreseeable served to further limit the liability of sellers.

During the third phase, attempts to formulate comprehensive international standards in this area have been unsuccessful. States have been unwilling to submit the issue to significant international regulation, arguing that
important domestic public policy issues are concerned. As a result, international conventions dealing with international sale of goods have left significant aspects of the liability issue for states to regulate according to national law. Insofar as international standards apply to some aspects of the liability issue, the norm continues to be limited liability for international sales transactions. There has been some expansion of merchant liability for defective goods under different systems of national law in the form of consumer protection, reflecting the principles of state intervention, political autonomy, and equity.

Allocation of Transportation Costs and Liabilities. The standards governing the allocation of transportation costs and liabilities between buyers, sellers and transporters exhibit considerable uniformity throughout the development of the regime. During the first phase, the norm was the adoption of uniform merchant practices allocating costs and limiting liabilities under transportation agreements. This norm reflects the dominance of the principles of merchant autonomy and the facilitation of exchange.

During the second phase, merchants devised uniform rules, which today are called 'terms of trade,' that became a part of merchant custom and practice and were enforceable in merchant courts. Later in the second phase, the norm shifted to state regulation of transport terms, reflecting
the growing influence of the principle of state intervention and resulting in the appearance of national distinctions. However, many states incorporated the terms of trade from merchant law and custom into domestic sales law, creating a permissive regulatory structure that left considerable scope for merchants to choose the applicable terms. Thus liability for loss and damage during the course of the transaction continued to be governed by the contract of sale and transport, reflecting the continuing influence of the principles of merchant autonomy, freedom of contract, and the facilitation of exchange.

During the third phase, uniformity weakened in some areas. However, terms of trade have been codified by international organizations into non-binding rules for the optional use parties. Though legally non-binding these terms are used widely and are regarded as evidence of customary international law. The codification of merchant custom by international actors reflects the growing importance of the principle of international intervention, but of a permissive and not a prohibitory nature. In addition, advances in transportation and documentation have generated new uniform rules and customs.

Insurance. Standards regulating liability of buyers, sellers, transporters, and insurers for loss of goods during transit also exhibit considerable uniformity over time and have their origins in merchant custom and practice. During
the first phase, merchants devised methods for apportioning risk between buyers, sellers and insurers, and limiting liabilities. These standards were used widely and were ultimately codified into insurance codes and enforced by merchant courts. The norm was the adoption of uniform standards allocating transport risks according to commercial custom, reflecting the dominance of the principles of merchant autonomy and the facilitation of exchange.

During the second phase, the principle of state intervention dominated, and the norm was state established standards for transport insurance, which somewhat weakened uniformity. However, as many states adopted national insurance laws that incorporated merchant custom and the leading multinational insurance companies adopted similar practices, considerable uniformity in standards was preserved.

During the third phase, technological developments in trade, transportation, and finance have generated new insurance concerns. It is significant, however, that international efforts to codify insurance law and practice and to develop rules governing insurance standards in a number of new areas have not occurred. Insofar as internationally accepted standards characterize the modern regime, they are predominantly customary in nature.

*Financing and Credit.* This issue concerns the standards and practices regulating payment arrangements and
the ability of merchants to charge interest on commercial loans. During the first phase, the norm was for merchants to utilize uniform payment and credit documents and procedures to facilitate sales contracts. These documents and procedures evolved out of commercial custom and ancient law. The principle of merchant autonomy was evident in the broad range of choice of the documents and procedures that were to govern the sales transaction. However, at the same time the principle of local intervention and canonical notions of equity were evident in the general prohibition of usury. The prohibition of usury derived from ecclesiastical law, but was also reflected in the disdain that political authorities had for the merchant class. Merchants and lenders, however, were ingenious in devising payment methods and procedures that embodied interest charges, but were less transparent than outright charges on loans. In spite of the prohibition of usury, various forms of exchange were devised that extended credit at a charge. These documents were enforceable only under the law merchant and in merchant courts. The simultaneous prohibition of interest by the local authorities and the legitimacy of interest charges under the law merchant evidences the conflict between the principles of local intervention and merchant autonomy. It also reflects the tension between the equity principle and the facilitation of exchange principle. The norm was the prohibition of interest charges by local authorities, but the acceptance of such charges under the law merchant.
The growing acceptability of the merchant class and the practice of lending for profit in the second phase brought an end in most systems to the prohibition of usury. This reflected the growing ascendance of the principles of the facilitation of exchange, merchant autonomy, and market allocation, evident in the widespread acceptance of interest charges.

The third phase has witnessed a technological revolution in the financial instruments available for exchange. Today, in addition to the methods and procedures inherited from the law merchant, there has been a proliferation of new methods and procedures available to regulate payment relations. The principles of merchant autonomy, freedom of contract, and the facilitation of exchange continue to prevail, as evidenced by the general legitimacy of interest charges and merchant choice in the payment and financing documents and procedures adopted.

4. Normative Structure: Procedural Dimension

*Locus of Regulation.* With regard to identification of the legitimate agent(s) for rule creation and enforcement, the principle of merchant autonomy has competed with the principles of local, state, and international intervention. As stated above, the principle of merchant autonomy provides that merchants should be free to regulate commercial transactions by entering into contracts creating legal
obligations, determining the substantive content of such agreements, and enforcing those obligations without external interference. In contrast, the principles of local, state, and international intervention provide that local, state, and/or international authorities should intervene to regulate the creation, content and enforcement of commercial agreements.

During the first phase, a dual system of commercial regulation existed. Merchants exercised great autonomy in regulating wholesale and foreign trade and the procedures for creating and enforcing binding obligations. Few formal requirements were imposed upon the formation of agreements, reflecting the operation of the informality principle, and merchants were autonomous in the enforcement of agreements, reflecting the principle of merchant autonomy. The norm was to accord broad latitude to merchants to establish the formal requirements for creating binding obligations and to devise appropriate enforcement procedures. The specific rules regulating the formation, interpretation, and proof of contracts reflected the value attached to informal and expeditious procedures. However, significant intervention by local authorities was accepted with regard to the regulation of local and retail transactions and local markets. These authorities regulated when and where markets could be held and created rules governing market offences aimed at local supply management. They also intervened in the substantive content of sales contracts by regulating
prices and establishing strict liability standards for
defective goods. Local intervention into payment and
financing arrangements was evident in the prohibition of
usury. Thus, the norm during the first phase of the regime
was merchant control of wholesale and foreign trade, but
local control of domestic trade and the local market
environment for exchange.

During the second phase, the dualistic system of
regulation disappeared and the norm became the acceptance of
greater state control of commercial relations. States
created rules that imposed significant procedural and formal
requirements on the creation, interpretation, proof, and
enforcement of contracts. The principle of merchant
autonomy gave way to interventions by local and state
authorities as states replaced merchants as the legitimate
agents of law creation and enforcement. The creation,
interpretation and enforcement of binding agreements were
subject to increasing formality, reflecting the erosion of
support for the informality principle. Rule creation and
enforcement became the prerogatives of the state. However,
at the same time the norm was greater merchant control of
the substantive content of all commercial agreements as
price regulation receded, liability for defective goods was
limited and the prohibition of usury removed.

In the third phase, changing standards of legitimacy
have had a profound impact upon the locus of regulation as
international organizations and associations have come to
share legitimacy as agents of law creation and enforcement. Today a variety of international organizations participate in determining the conditions that have to be met in order to create binding obligations, in many cases dispensing with many formal requirements and suggesting a return to the procedural informality of the early law merchant. In addition, states, recognizing the value in collaborating to achieve common standards governing commercial relations, have taken on the responsibility of representing commercial actors in international forums where international codes, conventions, and model laws are formulated. While this might appear to be a reflection of further erosion of the primacy accorded to the principle of merchant autonomy, for states now dominate the process, in fact there has been a reassertion of the principle by states. States, in collaboration with commercial actors, are participating in the effort to remove procedural and formal obstacles to the creation and enforcement of agreements. In some cases this involves replacing national legal formalities with internationally agreed upon formalities. These rules governing the formation, content and enforcement of agreements impose far fewer formal or procedural requirements, leaving greater scope for merchants to regulate their affairs. The norm today is acceptance of a mixture of merchant, state, and international control.
Methodology of Rule Creation. This issue concerns the identification of legitimate sources of regime standards and the chosen means or method for rule creation. The principles that characterize the issue of methodology of rule creation are those of merchant autonomy, local or state intervention, international intervention, and informality. With regard to the legitimate sources of law, reliance upon commercial custom and usage reflects the priority attached to the principles of merchant autonomy and informality. In contrast, reliance upon positive acts of law creation by local, state, or international authorities reflects the priority attached to the principles of intervention.

During the first phase, the norm was widespread acceptance of merchant custom as a source of law. Indeed, many merchant practices were only recognized by and enforceable in separate merchant courts. The acceptance of merchant custom as a source of law also reflected the importance attached to the merchant autonomy principle, the informality principle, and the facilitation of exchange, for the law merchant accepted informal procedures, unacceptable in the local common and civil law courts, and stressed the need for the expeditious settlement of disputes.

During the second phase, the norm shifted to recognize positive national law as the legitimate source of commercial regulation. This reflected the predominance of the principles of state intervention and the enhancement of political autonomy through the achievement of national
goals. The second period thus witnessed significant encroachments upon the principles of merchant autonomy, informality, and the facilitation of exchange.

During the third phase, the norm is widespread acceptance of both customary and positive law as sources of the law. While positive national law and international conventions today are generally regarded as the primary sources of the law, there has been a revival of emphasis on commercial custom. The third period, thus, exhibits the simultaneous influence of the principles of state intervention, international intervention, and merchant autonomy. In addition, the revival of merchant custom reflects growing influence of the informality principle and the facilitation of exchange.

With regard to the dominant coordinative strategies, reliance upon uniformity in merchant practices, which was the norm adopted by commercial actors to coordinate their relations in the first phase, reflected the general legitimacy accorded commercial custom as a source of law. The norm of uniform practice thus reflects the predominant influence of merchant autonomy, informality, and the facilitation of exchange.

During the second phase, the norm was to regulate international commercial relations according to national conflicts of law principles which sought to localize transactions with a foreign element in a particular system of national law. This norm reflected the overwhelming
influence of the principles of state intervention and political autonomy, as international transactions were forced to submit to national legal principles and standards. Acceptance of the unification of national conflicts of law rules as a coordinative strategy appeared late in the second phase. This strategy also reflects the predominance of the principles of state intervention and political autonomy, for only conflict rules and not substantive rules of commercial law are rendered uniform.

In contrast, the unification of substantive rules of law became more the norm in the third phase. This strategy can involve relinquishing significant national control to international authorities for the formulation of standards of general application and thus reflects the operation of the principle of intervention by international authorities. It should be noted, however, that states ultimately enforce agreed upon standards in their national legal systems and thus retain significant control over implementation and interpretation.

The third phase exhibits reliance upon all of the coordinative strategies. The unification of national conflicts of laws rules, the unification of substantive national commercial laws, and the reliance upon commercial custom all figure as legitimate coordinative strategies, although commercial actors and states often differ in the emphasis placed on the different approaches. However, the
unification of substantive commercial laws has become the dominant coordinative strategy.

Dispute Settlement. The final procedural issue concerning the processes and institutions for dispute resolution have already been touched upon in the discussions of the locus of regulation and of the nature and extent of state intervention. Here the issue is identification of legitimate means for dispute settlement. The conflict is between the adjudication principle, which favours dispute resolution in national courts with national judges applying the law of the forum, and the arbitration principle, which embodies a preference for private arbitrations where parties are free to choose the applicable law and to designate arbitrators. The identification of adjudication or arbitration as the appropriate means for dispute resolution also reflects the conflict between principles of merchant autonomy and state or international intervention.

In the first phase, the norm was the acceptance of dispute resolution and enforcement by merchants. The law merchant was enforced by merchant courts that operated more like private arbitrations in dispute settlement. These courts were independent of the local common and civil law courts of the day and adopted informal procedures and enforced bargains that were unenforceable in the local courts. The dispute settlement system achieved a high degree of efficacy through the practices of notaries who
travelled with merchants from port to port and market to
market, recording agreements and keeping accounts. In-Formality of procedures for creating, proving, and
enforcing commercial agreements and self-enforcement actions
of merchants imposing the sanctions of market exclusion,
bankruptcy, and loss of reputation characterize dispute
settlement in the first phase.

During the second phase, support for the arbitration
principle weakened as states either abolished merchant
courts or incorporated them into national legal systems. The
norm became the acceptance of state offices for dispute
settlement and enforcement. While private arbitrations
still took place, effective enforcement lay in the hands of
the state.

In the third phase, both the arbitration and the
adjudication principles are influential. However, while
merchants continue to settle their disputes by national
adjudication, they are increasingly turning to arbitration.
International arbitration is becoming the norm. Fur-thermore, states are participating in the reassertion of
the arbitration principle. They are adopting international
conventions governing international arbitration and devising
national procedures for enforcing the decisions of
international arbitrations. Merchant autonomy in dispute
settlement is thus being asserted and assisted by states and
being codified by national legal systems, producing a
mixture of merchant, state, and international regulation.
The return to international arbitration as the chosen method of dispute resolution also reflects the increasing importance attached to the informality principle and to the facilitation of exchange. International arbitrations are generally not subject to the strict procedural formalities required by national courts of law and are regarded as dispensing a more expeditious and less costly form of dispute resolution.

Having reviewed the structure and normative content of the private international trade regime it is now appropriate to return to the discussion of regime strength.

5. Regime Strength

It was noted earlier that while regime strength depends upon a number of criteria, care must be taken to develop criteria and tests of strength that reflect the specific nature of the private trade law regime. The above overview of the substantive and procedural dimensions of the regime shows the important role that merchant custom and permissive and facilitative standards and rules play the regulation of international trade relations. While the regime does consist of some injunctions and mandatory rules, and the mandatory content of the regime has changed over time, a great deal of international commercial law is comprised of model codes and rules designed for the optional use of parties in the creation and enforcement of binding
obligations. Moreover, the obligatory basis of promises or contractual obligations derives not from external sources, but from the free will of the contracting parties. It has also been noted that tests of regime strength are intimately connected to the model of rules or rule structure one explicitly or implicitly adopts. The tests of strength appropriate to directives, prohibitions, and injunctions derive from the command theory of law, which directs attention to the extent to which regime injunctions of a mandatory nature actually constrain the behaviour of actors and actually limit recourse to actions that parties would normally undertake in the absence of regime injunctions. Of relevance are the comprehensiveness and legitimacy of regime injunctions and the level of compliance. However, the facilitative, voluntary, and suppletive nature of promissory obligations requires a different test of strength. This test entails the evaluation of the extent to which parties avail themselves of the optional codes and model laws and the uniformity and universality of such practices. Accordingly, with regard to assessing the strength of the substantive dimension of the regime, the criteria employed will be the comprehensiveness of the scope of issues and transactions covered by the regime and the legitimacy and support that actors accord to them. While the specificity and clarity with which regime rules are formulated will be indicators of strength, it is also important to note that regime standards have derived a great deal of support from
the fact that they permit sufficient flexibility. Commercial actors have always recognized the value of ensuring that their rights and obligations are stated with sufficient specificity to minimize the risks of misunderstandings. Yet at the same time they value retaining certain flexibility in order to adjust and adapt to changing circumstances. Indeed, one of the virtues of commercial custom is its ability to adapt to changing circumstances as the need arises.

A strong substantive regime will thus exhibit comprehensive coverage of regime issues and widespread legitimacy accorded to regimes standards, as evidenced by near universality of reliance upon or deference to such standards

Procedurally, strength will be assessed by identifying the presence of secondary rules identifying legitimate agent(s) of law creation and providing mechanisms for creating, modifying, and extinguishing uniform rules. This will involve evaluating the ability of decision-making authorities to make and enforce binding and authoritative decisions and to promulgate widely adopted rules.

A strong regime procedurally will exhibit general perceptions regarding the legitimacy of rule-making authorities, whether governmental or non-governmental, in the creation and enforcement of rules of international application. It will also exhibit strong support for
methods of law creation that are capable of generating standards, rules, and decisions of broad or near universal appeal and application. The identification of legitimate agent(s) capable of generating uniform laws, widely accepted customary law, the acceptance of unification as the methodology for rule creation, and broad acceptance of international arbitration as the means for dispute settlement will thus indicate procedural strength.

While subsequent chapters will assess the strength of the regime in greater detail, Figure 3 provides a preliminary indication of the strength of the procedural and substantive dimensions.

**FIGURE 3**

**REGIME STRENGTH**

**Substantive Dimension**

<table>
<thead>
<tr>
<th></th>
<th>Phase I</th>
<th>Phase II</th>
<th>Phase III</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prices:</td>
<td>moderately strong</td>
<td>stronger</td>
<td>strong</td>
</tr>
<tr>
<td>Defective Goods:</td>
<td>moderately strong</td>
<td>stronger</td>
<td>weak</td>
</tr>
<tr>
<td>Transport:</td>
<td>strong</td>
<td>weaker</td>
<td>moderately strong</td>
</tr>
<tr>
<td>Insurance:</td>
<td>strong</td>
<td>weaker</td>
<td>weak</td>
</tr>
<tr>
<td>Finance/Credit:</td>
<td>strong</td>
<td>weaker</td>
<td>strong</td>
</tr>
</tbody>
</table>

**Procedural Dimension**

<table>
<thead>
<tr>
<th></th>
<th>Phase I</th>
<th>Phase II</th>
<th>Phase III</th>
</tr>
</thead>
<tbody>
<tr>
<td>Locus:</td>
<td>strong</td>
<td>very weak</td>
<td>strong</td>
</tr>
</tbody>
</table>
Methodology: strong very weak strong
Dispute Resoln: strong weak strong

We will turn now to consider various explanations of the origin, evolution, scope, nature, and strength of the regime.
CHAPTER III

THEORETICAL PERSPECTIVES ON INTERNATIONAL REGIMES

A variety of approaches are available for explaining the conditions that give rise to collaboration or norm governed activity in a world that is typically characterized as anarchic.\(^1\) This dissertation utilizes three broad approaches to regimes analysis: structural realist, functional, and sociological.\(^2\) While these are not the only perspectives on international cooperation, they have attracted considerable scholarly attention.\(^3\) In addition,

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1. Haggard and Simmons in "Theories of international regimes" identify four approaches: structural, game-theoretic, functional, and cognitive. However, this classification is problematic for the approaches often overlap. Structural analysis often draws upon game-theory or is combined with functional analysis, as in the works of Kenneth A. Oye, "Explaining Cooperation under Anarchy: Hypotheses and Strategies," World Politics \(38\) (October 1985): 1-24; Keohane, After Hegemony and Aggarwal, Liberal Protectionism.

2. Keohane in "International Institutions," p. 381 identifies two broad approaches to regime analysis. One is the rationalistic approach, comprised of realist or structural realist and functional theories of regimes, which are essentially power or interest based theories. The other is the reflective or sociological approach which stresses "the role of impersonal social forces as well as the impact of cultural practices, norms and values that are not derived from the calculations of interests." (references omitted).

3. This dissertation does not consider Marxist or neo-Marxist approaches, which stress the themes of exploitation and dependency and fall outside the mainstream approach to international relations. For analysis of the capitalist world system see Immanuel Wallerstein, The Capitalist World Economy (Cambridge, Mass.: Cambridge University Press, 1979). For dependency theory, see Andre Gunder Frank, Capitalism and Underdevelopment in Latin America (New York: Monthly Review Press, 1967) and Theotonio Dos Santos,
there is some overlap among them. However, they do identify different factors as significant in regime creation and transformation and in the determination of regime nature, scope, and strength. This chapter will describe each approach and identify the sort of evidence that will tend to support or undermine their explanatory capabilities. It will lay the foundation for an evaluation of the most useful explanation of the origin and evolution of the private international trade law regime. As subsequent chapters show, the regime has passed through three phases, from a phase of medieval internationalism, through a phase involving the nationalization of regime standards, to the present revival of internationalism. During these phases the nature of the regime has changed as different principles have been accorded primacy in the norms and rules governing the substantive and procedural dimensions of the regime. So too have the scope and strength of the regime varied over time. The approaches will later be assessed in terms of their relative abilities to explain the origin of the regime and sources of continuity and change.

The following discussion will proceed to describe structural realist, functional, and sociological approaches in turn. Their key assumptions and hypotheses on cooperation will be highlighted and the type of evidence

that will tend to support or undermine their explanatory capabilities will be identified.

A. Structural Realism

In spite of the diversity amongst those who may be said to adopt a structural realist perspective, it is possible to identify certain core elements or assumptions that inform structural realism. In general terms, structural realists are very pessimistic regarding the potential for cooperation among states and they stress the transitory nature of cooperative arrangements that do emerge. States are regarded as the major units of analysis and as unitary, egoistic, utility-maximizing actors. States regard security as the preeminent interest and are bound only by commitments they have accepted or agreed to. Furthermore, structural analysis emphasizes the all-important role of system structure in conditioning the actions of states and

4. Kenneth Waltz, Theory of International Politics (Reading, Mass.: Addison-Wesley, 1979) is commonly cited as a classic example of structural realist analysis. Also often referred to as "structural realists" or as neorealists are Keohane and Nye, Power and Interdependence; Stephen D. Krasner, Structural Conflict: The Third World Against Global Liberalism (Berkeley: University of California Press, 1985); Aggarwal, Liberal Protectionism; Keohane, After Hegemony; Robert Gilpin, War and Change in World Politics (New York: Cambridge University Press, 1981).

in determining the conditions under which states are likely to enter into collaborative arrangements. For Waltz, state interests are determined by states' overriding concern for security in an anarchic system and by the changing distribution of power among states. While Waltz does not deny that the purposes of states may vary, he regards the influence of system structure to be determinative. Structural anarchy places a premium on security and survival and dictates that states will eschew relationships that pose potential threats to their political autonomy. As Waltz states, "[i]n an unorganized realm each unit's incentive is

6. Ashley in "The Poverty of Neorealism" identifies the following five elements of structuralism: the rejection of evolutionary and speculative thought; regarding conduct and practices as the product of deeper objective structural forces; a commitment to a systemic point of view; the presupposition of the predominance of structure over practice and the whole over the parts; and, a view of change that accentuates the dependence of change upon structural conditions. Ashley argues that these five elements inform the neorealist structuralism of Waltz, Keohane, Gilpin and others and translate into the neorealist commitment to statism, utilitarianism, and positivism.

7. In Theory of International Politics, Waltz defines system structure as consisting of three components. The first is the principle according to which the system is ordered. He identifies the system as anarchic, ordered on the principle of self-help. The second component is the differentiation of units and the specification of their function. He regards states to be functionally undifferentiated in that all states pursue similar goals (i.e., security and survival) in a self-help system. The third component is the degree of concentration or diffusion of power capabilities within the system. According to Waltz, the third component provides the only source of variation in system structure and, hence, in state actions.

8. Theory of International Politics, p. 91.
to put itself in a position to be able to take care of itself since no one else can be counted on to do so. The international imperative is 'take care of yourself'.

Thus the dominant image or world view is international anarchy or the absence of centralized authority or formal management structures. Structural realist explanations attribute regime origin, development, nature, and strength to the distribution of power in the international system. Regimes are thus temporary and transitory as they "reflect the prevailing patterns of interest and power...and they change as these patterns change."

Stephen Krasner identifies three approaches to international regimes. Two approaches, the conventional and modified structural approaches, adopt structural realist assumptions, "which posit an international system of functionally symmetrical, power-maximizing states acting in an anarchic environment" and are of immediate concern to this discussion. The third approach, the Grotian approach, departs from structural assumptions in significant ways, and is of less concern at the moment. Grotians regard regimes

10. See Holsti, *The Dividing Discipline*.
12. "Structural causes."
to be pervasive in international relations and evident wherever patterned behavior can be identified.\textsuperscript{14}

The conventional structural view regards regimes "as useless if not misleading." States as rational, egoistic actors "function in a system or environment that is defined by their own interests, power, and interaction. These orientations are resistant to the contention that principles, norms, rules, and decision-making procedures have a significant impact on outcomes and behavior."\textsuperscript{15}

Conventional structuralists, like Waltz, deny that regimes significantly influence state behavior because states simply will not submit to legal or normative constraints on their actions.\textsuperscript{16} The fear that binding oneself to a course of conduct that could ultimately compromise security and survival as an autonomous political unit by rendering a state vulnerable or weaker in relation to other states works against the development of mutual interests in cooperating. Thus states will avoid relationships and arrangements that render them dependent on others and that raise the possibility that others will experience relative gains. As

\textsuperscript{14} Donald J. Puchala and Raymond F. Hopkins, "International regimes: lessons from inductive analysis" and Oran R. Young, "Regime dynamics: the rise and fall of international regimes," both in the Krasner volume, are said by Krasner to exemplify this approach.

\textsuperscript{15} \textit{Ibid.}, p. 6. See Susan Strange, "Cave! hic dragones: a critique of regime analysis," in this volume for the view that regimes are merely epiphenomenal and obscure the real influence of underlying power relations.

Waltz states, "[b]ecause states are in a self-help system, they try to avoid becoming dependent on others for goods and services" and should try to reduce their dependency if they are dependent on others.\textsuperscript{17} Arthur Stein notes that to realists, states "cannot tolerate intrusions on their independence or their prerogatives. They must not allow themselves to become dependent on others."\textsuperscript{18} Stein provides the following summary of the realist view on cooperation:

Cooperation is rare, because states act autonomously and self-help is the rule. Since realists hold that states cooperate only to deal with a common threat, they see cooperation, when manifest, as temporary or inconsequential and ultimately explained by conflict.

In this vision international institutions are not particularly relevant. States do not cede any authority to them, and they are powerless to shape state behavior.

Cooperation is unusual, fleeting, and temporary. International institutions do not exist or are irrelevant.\textsuperscript{19}

Zacher and Matthew identify six barriers to cooperation under neorealist logic: the autonomy barrier (states resist encroachments on their political autonomy), the common interest barrier (states share only modest common interests), the relative gains barrier (cooperation is likely to benefit some states more than others),\textsuperscript{20} the


\textsuperscript{19} Ibid., pp. 6-7.

\textsuperscript{20} See Grieco, "Anarchy and the limits of cooperation," for further exploration of the relative gains obstacle.
institutional barrier (institutions for negotiating and enforcing agreements are inadequate), the security-dilemma barrier (in security matters it is difficult to differentiate between defensive and offensive capabilities), and the defection-cost barrier (the costs of noncompliance in security matters are high).²¹

Structural realists, however, differ in the degree to which such obstacles preclude cooperation and the development of influential regimes. The modified structural view shares similar assumptions, but attributes more importance to regimes, albeit, "only under fairly restrictive conditions."²² States will enter into collaborative, norm governed relations when it is in their interests to do so. Such interests can arise in response to problems of coordination and situations in which self-interested and individualistic behavior lead to undesirable or sub-optimal outcomes, like prisoners' dilemma situations, collective goods problems, and the tragedy of the commons.²³


For many structural realists cooperation in the development of regimes will only occur in the presence of a hegemonic state capable of creating and enforcing regime standards. Hegemonic stability theory identifies the presence of a hegemonic distribution of power as necessary for regime creation, maintenance, and strength. This theory is said to offer "the most parsimonious and widely employed explanation of regime dynamics; it links regime creation and maintenance to a dominant power's existence and the weakening of regimes to a waning hegemon." While different versions or strands of the theory may be identified, proponents draw upon analytical insights provided by the literature on public or collective goods.


25. Haggard and Simmons, Theories of international regimes," p. 500.

26. Important differences are apparent in the hypothesized nature of hegemonic leadership as benevolent or coercive, in the goals pursued by the hegemon, and in the nature of the goods supplied by the hegemon. Kindleberger contemplates a benevolent or benign hegemon supplying public goods of benefit to all states. Gilpin and Krasner, in contrast, recognize that hegemony may be coercive, that the hegemonic state will be motivated by self-interest and that the goods supplied will not necessarily provide symmetrical benefits.

Baldly stated, the premise is that in a formally anarchic system, lacking hegemonic leadership, public goods, like economic or political stability or an open trading system, are underprovided as a result of the free rider phenomenon. By definition, public goods are characterized by jointness of supply and nonexcludability. Jointness of supply "requires that different states be able simultaneously to consume the same produced unit of the good," in that consumption by one does not reduce the amount available for others. 28 Nonexcludability concerns the inability of states to exclude or prevent others from enjoying the public good. 29 Kindleberger argues that small and medium-sized states lack incentives to contribute to the provision of the public good of economic stability and will be tempted to

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free ride, letting others provide the good.\footnote{30} In the absence of a strong leader capable of providing public goods, such goods will go underproduced. For "the world economy to be stable, it needs a stabilizer, some country that would undertake to provide a market for distress goods, a steady if not countercyclical flow of capital, and a rediscount mechanism for providing liquidity when the monetary system is frozen in panic," as well as the management of exchange rates and the coordination of domestic monetary policies.\footnote{31} While other versions of the theory accept the public goods premises, they also highlight the ability of a hegemon to structure and shape the regime to its own ends.\footnote{32} This suggests that the nature of a regime will reflect the preferences and interests of the hegemonic power.\footnote{33} It also suggests that a regime will change in response to changes in the capabilities and preferences of the hegemon.


\footnote{31}{\textit{Ibid.}, p. 247. And see Kindleberger, \textit{The World in Depression}.}

\footnote{32}{Stephen Krasner in "State Power and the Structure of International Trade," argues that a hegemon will structure the trading system so as to maximize its national goals. Gilpin in \textit{U. S. Power and the Multinational Corporation} also emphasizes the notion of hegemonic self-interest.}

\footnote{33}{Zacher, "Trade gaps," p. 194.}
Other structural realists adopt the view that a hegemonic state is not necessarily required in order to enable cooperation and have explored the possibility that a coalition or group of states with similar interests can sustain a regime in the face of hegemonic decline. Keohane contends that in the absence of hegemony "the common interests of the leading capitalist states, bolstered by the effects of existing international regimes (mostly created during a period of American hegemony), are strong enough to make sustained cooperation possible, though not inevitable."\(^{34}\) Zacher has found support for the hypothesis that "a strong regime is likely when there is a coalition of (or mutuality of interests among) the most powerful group of states involved in an issue-area."\(^{35}\)

Structural realism gives rise to the following hypotheses regarding regime origin, evolution, nature, and strength:

A.1. Important international regimes only develop if they are imposed or created by the actions of a hegemonic state or a group of powerful states who share similar interests.

A.2. The nature and scope of a regime reflect the interests and preferences of the hegemonic state or the coalition of powerful states.

A.3. Regimes based on mutual interests and consent do not develop in issue-areas because:
   a) states oppose serious incursions on their political autonomy (autonomy barrier);

\(^{34}\) After Hegemony, p. 43.

\(^{35}\) "Trade gaps," pp. 193, 198.
b) states fear that other states will gain more (relative gains barrier); and,
c) there are no international institutions to facilitate the acquisition of information, the negotiation of accords and the monitoring of compliance (institutional barrier).

A.4. A regime changes in response to changes in the capabilities and preferences of the hegemon or of the coalition of powerful states. A decline in the capabilities of the hegemon or of the coalition of powerful states is accompanied by a decline in the strength of the regime.

A.5. Important international regimes are transitory and temporary since hegemonic states and coalitions always disappear.

In order to establish the explanatory power of structural realism it will be necessary to show that the regime was imposed or created by the actions of a hegemonic power or a group of powerful, like-minded states. The nature of the regime and changes in its normative foundations and strength should also reflect changes in the interests and power of the hegemon or of the coalition of states. Evidence that the hegemon or the more powerful states used sanctions or employed incentives in order to get the less powerful to comply will provide an indication of the efficacy of the approach. In addition, one would expect to find that states resisted the development of regime standards in areas concerning military security, relative economic power, and economic vulnerability and in areas lacking institutional safeguards. Issues that touch too closely upon the security interests of states, that encroach upon their political autonomy, or that relate to "the
central terms of competition" and that lack adequate international institutions for monitoring compliance are unlikely to be subject to regime discipline. Furthermore, the regime should show signs of weakening when the hegemonic or coalition states decline in power or when there is an erosion of the consensus amongst coalition states. Finally, one would expect to find that states and not private actors were responsible for the development of the regime.

Evidence that regime standards evolved in the absence of a hegemonic state or a coalition of like-minded states or changed in response to factors that do not relate to alterations in the distribution of capabilities will tend to undermine the explanatory power of structural realism. Thus, evidence that private, non-state actors were responsible for the development of the regime will work against a structural realist explanation. Evidence that domestic political considerations, ideology, or increasing economic interdependencies influenced the nature, scope, and strength of the regime will also undermine the efficacy of this approach. Finally, evidence that consensual regime standards developed and exhibited considerable longevity in important areas affecting the political autonomy, military security, relative economic power, and economic vulnerability of states and in areas lacking international

36. Ibid., p. 193.
institutions will deal a severe blow to structural analysis. The key indicators are summarized below:

1. The imposition or creation of the regime by a hegemonic or coalition of states and not its creation as a result of a consensus among states (or private actors).

2. Regime norms and scope reflect the interests and preferences of the hegemonic or coalition states and not those of weaker states.

3. The regime is transitory and changes only in response to changes in the capabilities and preferences of the hegemonic or coalition states.

We will turn now to consider the functional approach to regimes analysis.

B. Functionalism

As in the case of structural realism, there is considerable diversity amongst those who adopt a functionalist approach to cooperation. In general, functional analysis is more optimistic regarding the prospects for cooperation among states, for it posits that states are willing to compromise political autonomy in order to achieve other values. While functionalist logic informed post-War regional integration theory and interdependence

theory of the 1970s, a contemporary formulation of functionalism has been referred to as "neoliberal institutionalism." As Joseph Grieco notes, this most recent derivation is distinctive:

What is distinctive about this newest liberal institutionalism is its claim that it accepts a number of core realist propositions, including apparently, the realist argument that anarchy impedes the achievement of international cooperation. However, the core liberal arguments - that realism overemphasizes conflict and underestimates the capacities of international institutions to promote cooperation - remain firmly intact. The new liberal institutionalists basically argue that even if realists are correct in believing that anarchy constrains the willingness of states to cooperate, states nevertheless can work together and can do so especially with the assistance of international institutions.

Central to this approach is the belief that regimes develop under certain conditions that give rise to mutual interests in and joint benefits from cooperation. Drawing upon insights from interdependence theory, it is believed


40. See Zacher, "Toward a Theory of International Regimes" and Zacher and Matthew, "Liberal International Theory: Common Threads, Divergent Strands" for exploration of the theoretical bases for common interests in cooperation.
that such conditions typically involve growing economic interdependencies and consequential management problems. As Richard Cooper states, "[t]he growing interdependence of the world economy creates pressures for common policies, and hence for procedures whereby countries discuss and coordinate actions that hitherto were regarded as being of domestic concern exclusively." 41 Keohane observes that economic interdependencies generate conflict as states seek to shift the costs of adjustment to others. "If discord is to be limited, and severe conflict avoided, governments' policies must be adjusted to one another, that is, cooperation is necessary." 42

Most functional theories of international regimes explain the origin and operation of regimes in terms of their effects. As Keohane notes:

> In general, functional explanations account for causes in terms of their effects. That is, 'the character of what is explained is determined by its effect on what explains it.' ... Functional explanations in social theory, like functional explanations of international regimes...are generally post hoc in nature. We observe such institutions and then rationalize their existence. Rational-choice theory, as applied to social institutions, assumes that institutions can be accounted for by examining the incentives facing the actors who created and maintain them. Institutions exist because they could have reasonably been expected to increase the welfare of their creators. 43


42. *After Hegemony*, p. 243.

43. *After Hegemony*, p. 80 (references omitted).
As Haggard and Simmons observe, "functionalist theorizing suggests that some generalized functions are underprovided, given conditions of anarchy or market failure." Indeed, functional analysis adopts the assumption of structural anarchy, but identifies certain conditions under which collaborative arrangements will produce joint gains for states and thus provide incentives for states to cooperate in the creation and enforcement of regime standards. Drawing upon economic theories of market failures and imperfections, information and transaction costs, game theory and public goods theory, functional analysis identifies situations in which unilateral state action will not produce the outcomes desired. The reliance on market analogies and the assumption that coordinated action (to address market failures, to reduce transaction costs, and to supply undersupplied public goods) produces joint gains for all states are characteristic of functional analysis. Keohane posits that in an anarchic and self-help system certain problems arise concerning legal liability and property rights, uncertainty, and transaction costs. "Without consciously designed institutions, these problems will thwart attempts to cooperate in world politics even when actors' interests are complementary."

44. "Theories of international regimes," p. 507.
45. See Keohane, After Hegemony, chap. 6.
Thus international regimes are useful to governments. Far from being threats to governments...they permit governments to attain objectives that would otherwise be unattainable. They do so in part by facilitating intergovernmental agreements. Regimes facilitate agreements by raising the anticipated costs of violating others' property rights, by altering transaction costs through the clustering of issues, and by providing reliable information to members. Regimes are relatively efficient institutions, compared with the alternative of having a myriad of unrelated agreements, since their principles, rules, and institutions create linkages among issues that give actors incentives to reach mutually beneficial agreements.\textsuperscript{47}

Zacher notes that neoclassical economic theory regards "uncertainty of costs and commercial opportunities, high transaction costs, impediments to factor mobility (e.g., tariffs), collusive arrangements, and natural monopolies" as market imperfections that reduce efficiency and gains from exchange.\textsuperscript{48} He identifies three forms of market failure that economic regulation seeks to address: the production of externalities affecting third parties; the uncontrolled exploitation of common property resources; and, the undersupply of public goods.\textsuperscript{49} The assumption is that the regulation of such imperfections and failures will increase efficiencies, producing greater overall economic welfare.

744- 53 Keohane refers to this as the "contractual approach."

47. Ibid., p. 97.


49. Ibid.
The assumption that international regimes regulating market imperfections and failures will produce greater overall welfare and thus generate the foundation for joint gains and mutual benefits from cooperation is critical to the functional approach. Keohane observes that "actors must have some mutual interests; that is, they must potentially gain from their cooperation. In the absence of mutual interests, the neoliberal perspective on international cooperation would be as irrelevant as a neoclassical theory of international trade in a world without potential gains from trade."\textsuperscript{50} Indeed, Zacher argues that "[c]ommon interests are probably more important to the politics of collaboration than has been conveyed by most of the literature, which implicitly stresses structural impediments, conflicting interests, and the power of opposed coalitions."\textsuperscript{51}

For neoliberal institutionalists, international organizations play a central role in facilitating the attainment of common goals. International organizations provide an institutional framework for the identification, articulation, and achievement of common interests. As Zacher and Matthew note:

There are a number of theses in the institutionalist approach. First, institutions (basically multilateral organizations and regulatory regimes) improve

\textsuperscript{50} International Institutions, p. 2.

\textsuperscript{51} "Toward a Theory of International Regimes," p. 154.
the quality of information about international issues and thereby assist states in understanding [the] bases for accord. Second, they reduce the transaction costs of agreements through convening multilateral meetings and providing normative frameworks within which agreements can be negotiated. Third, they facilitate agreements by making it easier to negotiate tradeoffs among issue areas. Fourth, they facilitate the enforcement of accords by promoting the transparency of states' policies, increasing the importance of states' reputation, and legitimizing sanctions against transgressors. Fifth, they create vested interests in their own norms and rules — in part because of political inertia. Finally, they not only change conceptions of instrumental self-interest (how to promote existing goals) but can alter the priority states attach to base values.52

International organizations, thus, are regarded as important influences in facilitating the development of regime standards. They also influence the strength of a regime by assigning property rights and creating vested interests in perpetuating regime norms and rules.53

Functional analysis gives rise to the following hypotheses regarding regime origin, evolution, nature, and strength:

B.1. Important international regimes develop in areas where there are opportunities for joint gains (especially from the correction of market failures) because:
   a) states are willing to sacrifice some political/legal autonomy to realize other values, like economic welfare;


b) relative gains problems seldom threaten future security and welfare; and,
c) international organizations facilitate the conclusion and monitoring of agreements.

B.2. Regimes develop and strengthen with increases in economic interdependence because the possibility of realizing gains from correcting market failures increases.

B.3. There is reasonable continuity in the normative structure and strength of the regime despite major changes in the distribution of capabilities among states.

In order to establish the basis for a functional explanation, one would expect to find regime norms and rules developing in areas where states have identified mutual interest in and shared benefits from collaborating. Evidence that states have traded off political autonomy to attain other values, like economic welfare, in the belief that all states gain as a result, will tend to support a functional explanation. Indications that the regime enhances overall welfare by correcting market failures will provide significant support. Admittedly, it is difficult to offer an objective assessment of the benefits and efficiencies generated by the trade regime in that it is impossible to know what the commercial world would look like in the absence of the regime. However, the belief of commercial actors that regime standards produce overall benefits by facilitating exchange by providing greater efficiencies in transacting, as evidenced by their support for the regime, should provide some proof of the efficacy of functional explanations.
In addition, one would expect the regime to develop with increases in the volume of trade and changes in the nature of trade. The scope of the regime should expand as commercial transactions proliferate and as technological advances create new commercial transactions and functional needs.

One would also expect to find evidence that international organizations have been influential in the development of the regime. The existence of institutional arrangements providing information, reducing transaction costs, and monitoring compliance should accompany the development of regime standards.

Finally, one would expect reasonable continuity in the normative foundations and strength of the regime over a long period of time, in spite of changes in the underlying power structure. As Zacker notes, "good evidence of common interests in a regime would be found if its basic features did not change significantly over time despite changes in alliances and the distribution of power." 54 Such commonalty of need not reflect the symmetrical distribution of benefits as long as all parties received some benefit. 55 Inversely, issues that do not give rise to common interests or any mutuality of benefits would not be expected to be subject to regime discipline. Evidence that regime standards have

54. Ibid., p. 155.
55. The issue of symmetry of benefits is taken up in Chapter VII.
changed or that the regime has weakened, in spite of the continuity of commercial needs, will tend to undermine the explanatory power of the approach. The approach will also be undermined by a finding that regime standards have not been developed in areas clearly exhibiting market failures and common interests or inversely, that the standards reflect only the interests of the dominant state or states.

These indicators are summarized below:

1. Strong regimes based on consensus exist in important issue areas.

2(a). The regime corrects market failures and benefits all participants.
(b). States and commercial actors support the regime in the belief that it generates overall increases in economic welfare by correcting market failures.

3. The regime covers all areas in which market failures exist.

4. The regime grew in scope and in strength as international commerce developed both quantitatively and qualitatively.

5. The regime exhibits considerable longevity and continuity in regime norms and strength over time, despite significant changes in underlying power relations.

6. International institutions perform valuable roles in providing information, reducing transaction costs and monitoring compliance.

Consideration will now turn to the third explanatory approach.

C. Sociological Approach
The sociological perspective emphasizes the impact that shared ideological, normative, and epistemological structures have on generating cooperative arrangements. This approach has been variously described as the "reflective approach" or the "sociological perspective," cognitive theories," and an "interpretive epistemology". Keohane observes that "the sociological approach has recently been in some disarray, at least in international relations: its adherents have neither the coherence nor the self-confidence of the rationalists." Others note that this approach refers to "quite a disparate group of approaches." The incoherence of the approach may well be explained by the fact that it has emerged more as a reaction to perceived inadequacies of structural realist and functional explanations, and not as an attempt to create a fully articulated theory of international collaboration. Indeed, it has been observed that this approach "explore[s] what structural, game-theoretic, and functional approaches

56. Keohane, "International Institutions."

57. Haggard and Simmons, "Theories of international regimes."


60. Haggard and Simmons, "Theories of international regimes," p. 509, note 66.
However, its proponents do share certain beliefs that enable their treatment as a rather loose group.

Proponents of what shall here be referred to as the sociological approach share the belief that there are significant limitations to the positivist, rationalist, and utilitarian premises of structural and functional analysis. As Keohane notes, "they all emphasize the importance of historical and textual interpretation and the limitations of scientific models in studying world politics." They emphasize that social institutions are often not the product of conscious choice and design, but evolve out of historically conditioned beliefs, habits, and practices. Ernst Haas emphasizes the important role that human learning and understanding play in the evolution of institutions, adopting an orientation that he refers to as "evolutionary epistemology."

This stand suggests that the study of regimes is more than the study of international collaboration as a matter of politics, though it certainly includes the political dimension. The study of regimes is a way of understanding the interactions of homo politicus with nature and with culture. It rests on the supposition that our collective understanding of our political choices increasingly depends on how we think about nature and about culture. The study of regimes illustrates the range of past and

61. Ibid.

62. The limitations that these premises pose for structural and functional explanations are further explored in Chapter VII.

future choices about international collaboration in a context of changing self-understanding. The politics of collaboration are seen as evolving alongside the evolution of consciousness itself, though not necessarily as an expression of biological evolution. 64

He notes how the changing normative foundations of the Law of the Sea, from the norm of maximum open access to the high seas to the treatment of the high seas as common property and subject to limitations on access, reflect an evolutionary change in consensual thought regarding appropriate uses of the high seas.

Kratochwil and Ruggie make the persuasive argument that the study of international regimes has been conducted according to a positivistic epistemology, an orientation that is inconsistent with the intersubjective ontology of international regimes.

International regimes are commonly defined as social institutions around which expectations converge in international issue-areas. The emphasis on convergent expectations as the constitutive basis for regimes gives regimes an inescapable intersubjective quality. It follows that we know regimes by their principled and shared understandings of desirable and acceptable forms of social behavior. Hence the ontology of regimes rests upon a strong element of intersubjectivity.

Now, consider the fact that the prevailing epistemological position in regime analysis is almost entirely positivistic in orientation. Before it does anything else, positivism posits a radical separation of subject and object. It then focuses on the 'objective' forces that move actors in their

64. "Words can hurt you; or, who said what to whom about regimes," in Krasner, ed., International Regimes, p. 24.
social interactions. Finally, intersubjective meaning, where considered at all, is inferred from behavior. Here, then, we have the most debilitating problem of all: epistemology fundamentally contradicts ontology! 65

We have touched on this problem before in terms of the inability of positivist methodology and rationalist and utilitarian premises to generate an explanation of the origin and binding nature of customary law. Legal positivism emphasizes and, indeed, defines law in terms of rules enacted by positive acts of will. Customary law, however, cannot be traced to some positive act of will, as evidenced in statutory enactments, but has evolved over time in the context of regularized practices that have come to be vested with an obligatory force. The assumption that states enter into collaborative arrangements on the basis of rational calculations of the costs and benefits are thus said to be of limited assistance in understanding collaborative arrangements that have evolved over time through customary practices and historical, social, and interpretive processes that do not submit easily to positivist analysis. Central to this criticism is the belief that there is an irreconcilable difference between social arrangements deriving from evolutionary processes and those deriving from rational or conscious choice and design. 66

Indeed, Ashley argues that structuralism, with


66. For the view that the two approaches are irreconcilable see F. A. Hayek, Law, Legislation and Liberty: Rules
its emphasis upon utilitarian, rational, and positivist discourse, evolved as a reaction to and rejection of evolutionary and speculative thought. Structural analysis thus neglects the role that human learning, knowledge, and self-reflection have played in the evolution of institutions.

Far from expanding discourse, this so-called structuralism encloses it by equating structure with external relations among powerful entities as they would have themselves be known. Far from penetrating the surface of appearances, this so-called structuralism’s fixed categories freeze the given order, reducing the history and future of social evolution to an expression of those interests which can be mediated by the vectoring of power among competing states-as-actors. Far from presenting a structuralism that envisions political learning on a transnational scale, neorealism presents a structure in which political learning is reduced to the consequence of instrumental coaction among dumb, unreflective, technical-rational unities that are barraged and buffeted by technological and economic changes they are powerless to control.

Ruggie has shown that international regimes reflect more than the underlying distribution of power, for they also embody the values, beliefs, and social purposes of the participants. He argues that "[w]hatever its institutional manifestations, political authority represents a fusion of

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68. Ibid., p. 260 (references omitted).
power with legitimate social purpose." He shows that different historical periods reflect structures of authority that embody distinctive ideological dispositions regarding the ways in which the political authorities defined their social purposes. Ruggie thus challenges the structural realist assumption of the primacy of system structure in the determination of state actions. He suggests that the dominant ideology embodied in the social purposes pursued by states are also determinative of state action. This raises the possibility that state actions are not only the product of the underlying power structure, but are also determined by domestic political considerations, including national ideology and opinion. Furthermore, it raises the possibility that dominant value structures, beliefs, and consensual knowledge are important determinants of regime nature and strength.

Ruggie also takes issue with the assumption that the structure of the system has not been affected by the functional differentiation of the units comprising the system. He argues that the shift in authority structures from the medieval to the modern structure reflects significant differences in the "principles on the basis of which the constituent units are separated from one another." These principles defined the scope, nature, and


purposes of legitimate authority. In the medieval period, the absence of a concept of sovereignty, a system of segmental and overlapping rule, and the lack of a distinction between the public and private domains gave rise to an authority structure that differs profoundly from the modern structure premised on a clear notion of sovereignty, well defined and distinct territories, and the notion of private property. He argues that changing concepts of legitimacy as to the nature and purposes of political authorities have asserted significant influence on the determination of state actions.

The belief that transnational values form the foundation for international cooperation also informs the work of those who posit the existence of an "international society." The Grotian or neo-Grotian strain of regimes analysis emphasizes the existence of a normative consensus regarding the fundamental values and purposes of states. Hedley Bull, for example, posits that international society is premised upon a consensus regarding the elementary goals of providing security against violence, enforcing promises, and protecting private property. While I have elsewhere argued that there are significant tensions in Bull's position regarding the potential for normative solidarity among states, the significant point here is that this approach premises cooperation on the existence of an

71. The Anarchical Society, pp. 4-5.
international society capable of generating a normative consensus.72 For Martin Wight, international society is premised upon 'an international consciousness, a world-wide community sentiment' regarding the moral virtue of Western values of constitutionalism and moderation.

International society, then, on this view, can be properly described only in historical and sociological depth. It is the habitual intercourse of independent communities, beginning in the Christendom of Western Europe and gradually extending throughout the world. It is manifest in the diplomatic system; in the conscious maintenance of the balance of power to preserve the independence of the member communities; in the regular operations of international law, whose binding force is accepted over a wide though politically unimportant range of subjects; in economic, social and technical interdependence and the functional international institutions established latterly to regulate it. All these presuppose an international consciousness, a world-wide community sentiment.73

Furthermore, some proponents of the neo-Grotian approach highlight that transnational values and knowledge structures are transmitted through a variety of agencies -- including states, private actors, and international organizations. For Young, states are the essential actors in the creation and transmission of regime standards;


however, they often act through the agency of private, non-state actors:

In formal terms, the members of international regimes are always sovereign states, though the parties carrying out the actions governed by international regimes are often private entities (for example, fishing companies, banks or private airlines).\(^7^4\)

Puchala and Hopkins identify elites as the practical actors in regime formation: "nation-states are the prime official members of most international regimes, although international, transnational, and sometimes subnational organizations may practically and legitimately participate."\(^7^5\)

The sociological approach does not provide a theory of collaboration. Nor does it, as Keohane notes, give rise to a clear research program.\(^7^6\) However, it does give rise to the following hypotheses on regimes:

C.1. International regimes develop when there are crucial transnational consensuses on ideology, values, and knowledge about international relations, and will weaken as the consensuses weaken.

C.2. The normative structure of a regime reflects consensuses regarding the desirability of the regime, its purposes, and the procedures for implementing it.

C.3. A variety of governmental and non-governmental actors are involved in the establishment and articulation of regime norms.

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Admittedly, it is difficult to identify the autonomous influence of values, knowledge, or ideology, especially when there is a congruence between ideology and structural position. Haggard and Simmons conclude that if "structural theories are weak on cognitive variables, most cognitive theories cannot describe clearly how power and ideas interact." However, subject to this caveat, evidence that the knowledge, ideology, and the values or social purposes of states have had an impact on the determination of regime norms, scope, and strength and contribute to explaining regime change will suggest that this approach is a useful supplement to structural and functional analysis. Reference to the nature and content of the principles accorded primacy in regime norms will assist in identifying the underlying purposes of the actors. In addition, the level of support for and acceptance of regime standards will provide indirect evidence of the purposes pursued by the actors. Evidence that changes in the dominant or accepted ideology, values, and knowledge have produced changes in the normative orientation of the regime will tend to support its explanatory capability. In contrast, evidence that the regime or sub-issue areas of the regime have not changed in response to ideological shifts or to changes in consensual values and knowledge will suggest that other influences are at work. Furthermore, a finding that the normative

structure of the regime does not reflect ideological, normative, or epistemological consensuses, but rather reflects the ideology etc. of a particular state or group of states will undermine the explanatory capability of this approach.

The following provides a summary of the relevant indicators:

1. The existence of a transnational consensus regarding the purposes of commercial regulation and the procedures for implementing regime norms and rules.

2. The embodiment of the transnational consensus and not the values and ideology of any particular state or group of states in regime principles, norms and rules.

3. Regime norms embodying the transnational consensus are strong; those that do not are weak.

4. A change in the normative structure of the regime is accompanied by a change in the transnational consensus.

5. Private actors participate in the development, articulation, and implementation of the transnational consensus.

Attention will now turn to the first phase in the development of the regime.
CHAPTER IV

PHASE I: THE MEDIEVAL LAW MERCHANT, 11th to 16th Centuries.

The law merchant has been described as "a venerable old lady who has twice disappeared from the face of the earth and twice been resuscitated."\(^1\) Goldman here refers to the disappearance of the Roman *jus gentium*, occasioned by the breakup of the Roman world and the disintegration of international economic relations in the Middle Ages and its reappearance in eleventh century Europe with the rebirth of international commerce. The second disappearance is said to have occurred in the seventeenth century when nation states localized and nationalized commercial law, resulting in a period of hibernation that lasted until the reappearance of a modern *lex mercatoria* in the twentieth century. Legal theorists generally agree that the law merchant has progressed through three phases in its evolution, although few would agree that it ever 'disappeared from the face of the earth.' Rather, most regard the evolution of the regime through the first phase of medieval internationalism in the eleventh to sixteenth centuries, the second phase of nationalization and localization in the seventeenth to nineteenth centuries, and the third phase of modern internationalism in the twentieth century as evidence of a

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continuous, albeit rather uneven, existence of merchant law and practice.2

This chapter will review the significant characteristics of the regime in the medieval phase and identify the factors that influenced the nature and strength of the regime. However, before proceeding to consider the substantive and procedural dimensions of the regime, it will provide some information on the historical context of medieval trade and commerce. The discussion will thus turn to the nature of commercial relations in the medieval period.

A. Medieval Jus Commune and Jus Gentium

Europe in the eleventh and twelfth centuries experienced a commercial revival associated with the opening of trade markets in the East and with the economic and political changes brought by the rise in Europe of cities and towns as autonomous political units.3 The Islamic


3. For discussion of these developments see Henri Pirenne, Economic and Social History of Medieval Europe (Kegan Paul: London, 1937); R. Lopez, The Commercial
invasions beginning in the seventh century interrupted merchant commerce and coupled with the advent of feudalism in the ninth century, which occasioned the disappearance of towns and most merchant activity, reduced most of Europe to a 'purely agricultural state'. Pirenne observes that "from every point of view, Western Europe, from the ninth century onwards, appears in the light of an essentially rural society, in which exchange and the movement of goods had sunk to the lowest possible ebb. The merchant class had disappeared. A man's condition was now determined by his relation to the land...." Pockets of commerce persisted, however, as Venice, Amalphi, Naples and other Italian cities continued to trade with Byzantium, and the Scandinavian countries engaged in trade in the North and Baltic Seas. As Clough notes:

Although trade over long distances existed in the Adriatic and in the North and Baltic Seas during the first half of the Middle Ages, most of Western Europe's economy was moribund, based as it was on a rigid land tenure system and upon production for immediate consumption. By the end of the eleventh century, however, there were many signs of economic growth and in the twelfth and thirteenth centuries a revival took place which was to break the older rigidities and greatly extend the range of commercial

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opportunities. Many forces, such as the growth in population, the rise of towns, greater industrial production, and more extensive trade, initiated this change.\textsuperscript{6}

While he suggests that to "attribute to any one of them the ultimate cause of what took place is to raise the problem of whether the hen, the egg, or the rooster came first to the poultry kingdom," he identifies the commercial expansion in northern Italy and in the Low Countries as of particular significance.\textsuperscript{7} The Crusades freed up the Mediterranean for trade, facilitating the commercial growth of the Italian cities. Venetian and Genoese traders brought goods to the port of Bruges, regarded as the 'Venice of the North', which along with other North and Baltic Sea ports, was experiencing a growth in trade.\textsuperscript{8}

It was in the Italian cities and northern port and market towns that the law merchant has its origins. As these trading communities grew and as commerce expanded, merchants created a system of law to govern their commercial activities. This system of law drew initially upon ancient Greek maritime customs, the Roman law of sales, debt, and general civil obligations, as well as the Roman \textit{jus gentium}. Then and for some time to come maritime and commercial law, together, formed the foundation of the law merchant. In a

\textsuperscript{6} The Economic Development of Western Civilization, p. 77.

\textsuperscript{7} Ibid., pp. 77, 81.

\textsuperscript{8} Ibid., pp. 80-2.
seventeenth century treatise on the law merchant, Gerard de Malynes observed the interrelatedness of maritime and commercial law: "Even as the roundness of the globe of the world is composed of the earth and waters; so the body of the *Lex Mercatoria* is made and framed of the Merchant Customs and the sea laws, which are involved together as the seas and the earth." 9

Merchants in ports drew upon the Sea Law of Rhodes, which was received and transmitted to Western Europe by the Greeks and Romans. 10 In the eleventh century the Italian republic of Amalphi produced a collection of maritime laws called the Amalphian Table, which was adopted by all the Italian cities, 11 while the seaport towns of the Atlantic and North Sea and England adopted a collection of maritime judgments of the Court of Oleron on the French coast. 12

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10. There is some disagreement as to the dating and origins of the Sea Law of Rhodes. Most historians date it from 300 B.C., although some date it from 900 B.C. See Robert D. Benedict, "The Historical Position of the Rhodian Law," *Yale Law Journal* 18 (1909): 223-42. And see Bewes, *The Romance of the Law Merchant*, chap. 6 for the view that the Rhodian Sea law is probably not confined to Greek sources but likely derives from more ancient civilizations.


These laws and customs spread to other commercial centres in Europe as patterns of trade changed creating new centres of commercial activity.\textsuperscript{13} In the fourteenth century the Baltic ports adopted the Laws of Wisby, thought to be modelled on the Laws of Oleron,\textsuperscript{14} while the Consulato del Mare of Barcelona, consisting of a compilation of the customs of the sea applied in the Consular Courts of Barcelona and based upon the customs of the Italian cities, gained wide currency in the ports of the Mediterranean.\textsuperscript{15}

Simultaneously, inland towns were developing a body of law to regulate overland trade in the markets and fairs of Europe. In Germany, England, and northern France the law merchant developed in the context of the fair, while in Italy and in southern France it developed in the context of the city-state.\textsuperscript{16} In England, in the thirteenth century the fair of St. Ives was regarded by English and foreign

\textsuperscript{13} For discussion of the impact of the shift in commercial power from the Mediterranean to the Atlantic see Shepard B. Clough and Charles W. Cole, \textit{Economic History of Europe} revised ed. (Boston: D. C. Heath & Co., 1946), chap. 5.


\textsuperscript{15} \textit{Ibid}.

merchants as "one of the most important in England." On the Continent, the fairs and courts of Champagne "had a universal importance" from the twelfth to the fourteenth centuries, while the fair of Lyon became a major commercial centre in the fifteenth and sixteenth centuries. In Italy, courts held in the commercial cities of Venice, Florence, Genoa, and Pisa were responsible for significant advances in the development of law merchant. The fair courts developed somewhat later in Germany in the fifteenth, sixteenth and seventeenth centuries. The law governing sales and market transactions drew upon a number of sources, most notably Roman and German sales laws, which were modified by merchant custom, and to a lesser extent, canon law. Fairs came to play an important role in facilitating the growth of commerce by providing security and safe conduct for merchants, while the fair courts contributed to the universalization of merchant law and custom.

20. Ibid., p. 178.
accompanied merchants to the fairs and represented them in fair courts. As Bewes notes the "merchants carried their law, as it were, in the same consignment as their goods, and both law and goods remained in the places where they traded and became part of the general stock of the country."23 While more will be said shortly of the special role played by merchant courts held in the fairs, cities, and ports of Europe, Sanborn underlines their significance in the following observation:

The privileges and the internal organization of the fairs constituted a very complete and ingenious system, the starting point in the evolution of the special law of the fairs, and all the more important because of the close commercial relations of the fairs with all that part of Europe from Flanders and England to Italy. The fair courts exercised a great influence upon the development of the modern Continental courts of commerce, for they were the first special courts, just as the peace of the fairs was the true precursor of the modern peace of commerce.24

Merchants came to be accorded a special status in medieval society, as the law merchant emerged as a distinct and autonomous body of law regulating the activities of merchants who were granted significant immunities from local laws and regulations.25 The law merchant was regarded as


the *jus commune* or common law of the medieval period. As Berman and Kaufman observe:

The law merchant governed a special class of people (merchants) in special places (fairs, markets, and seaports). It was distinct from local, feudal, royal, and ecclesiastical law. Its special characteristics were that 1) it was transnational; 2) its principal source was mercantile customs; 3) it was administered not by professional judges but by merchants themselves; 4) its procedures were speedy and informal; and 5) it stressed equity, in the medieval sense of fairness, as an overriding principle.

While local variations in the law merchant have been identified, universality in the fundamental principles applied to commercial relations throughout the European trading world have resulted in its characterization as medieval *jus commune* or common law and *jus gentium* or the law of nations. Indeed, in an authoritative essay on the law merchant the author concludes that the "international nature of the sources from which it drew its rules and of the persons over whom it exercised jurisdiction, combined with the universality of its guiding principles, fairly entitle the Law Merchant to be called 'the private international law of the Middle Ages'."


28. Mitchell, *An Essay on the Early History of the Law Merchant*, p. 21. The author here quotes Justice Maitland to the effect that the law merchant is the 'private international law' of the middle ages. See also Frederick Pollock and Frederick W. Maitland,
When we turn to consider the substantive and procedural dimensions of the regime we will see that the medieval law merchant embodied principles that emphasized the facilitative nature of exchange and the need for expeditious, informal, and flexible standards and procedures. It granted significant autonomy to merchants through the independent status accorded merchants and merchant custom. However, there were also other, at times incompatible, influences at work. Ecclesiastical law played a part in the development of commercial law in the medieval period. Canon law contributed to a tension between the principle that provides that the purpose of commercial regulation is to facilitate the expansion of commerce and the principle that identifies the purpose of commercial regulation as the promotion of fairness and equality in exchange. The law merchant adopted the Roman notion of equity, which contrasts with religious conceptualizations of

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equity that attribute distributional purposes to the exchange relationship. In Roman law the principle of deciding cases *ex aequo et bono*, by what is equal and good, contemplated the use of equity as a "discretionary corrective" to be applied in specific cases so as to avoid the rigours and potential injustices of formal laws. The law merchant adopted this conception of equity:

...the courts of commerce were to proceed according to equity and to examine the truth of the fact itself, without regard to the formal legal rules of evidence and proof. There is nothing more characteristic of the medieval law of commerce than its spirit of equity, its desire for true justice, and its abhorrence of legal technicalities. To express this we again find certain phrases that are commonly used, or their equivalents: *ex aequo et bono*, *sola veritate rei inspecta*, *sola facti veritate inspecta*, etc. This principle of substantial equity runs all through the *lex mercatoria* in every place at every period.

Thus the merchant courts were to tailor justice to the specific facts of each case, employing standards established

30. This definition of equity came to form the foundation of the common law Court of Equity (or Chancery) and for Anglo-American and civil law notions of equity under international law. For the former see Thomas E. Scrutton, "Roman Law Influence in Chancery, Church Courts, Admiralty, and the Law Merchant," in *Selected Essays in Anglo-American Legal History*, vol. I (Boston: Little Brown & Co., 1907), pp. 208-47. For the latter see M. W. Janis, "The Ambiguity of Equity in International Law," *Brooklyn Journal of International Law* 9 (Winter 1983): 7-34. The reference to equity as a discretionary corrective is taken from Janis.

by merchant custom and practice. However, canon law presented a different conception of equity. This conception regarded equity as a form of distributive justice, which "does not suggest flexible correction of strict rules of law, whether intra, praeter, or contra legem, but rather suggests a norm correcting existing distributions of wealth." The canonical view of equity was more consistent with the medieval view of society and stood in stark contrast with the view of equity evolving under the law merchant. Medieval ecclesiastics adopted a paternalistic attitude toward commercial relations that was reflective of an organic view of society combined with a general suspicion of material wealth.

Medieval society was conceived by its members to be an organic whole. Within it were two principal spheres of influence: the Church and the State. Because of the overriding concept of unity, the Spiritual and Temporal orders were seen as two sides or two aspects of the single Christian Commonwealth. Mutual cooperation between the two was encouraged, with a view towards achieving a full and harmonious life for medieval man.


It has been noted that the "medieval thinker had a functional idea of society." Each individual as a member of this organic whole belonged to a class and possessed a particular function in society. The accumulation of wealth in the attempt to change one's place in society was held in distrust.

It was therefore wrong for a man to try to earn more than was necessary to keep him comfortably in the station of life to which he was born.... The Middle Ages distrusted wealth.... Of the ways of making money, that of the merchant or trader was to the Middle Ages particularly dangerous and suspect.... To the strictest view, any profits from pure trade were wrong. 

Medieval canon law regulated commerce with a view to protecting consumers and the general public from unscrupulous trade practices. "Matters of trade were, by and large, immediate and intra-personal, and therefore, the application of personal morality to personal activity was fairly easy." Trade was regarded as an "instrument of social purpose" whereby merchants were required to conform to standards of Christian morality. Thus, canon law provided the source for the principle of *pacta sunt servanda*, or the binding force of promises, which were not enforceable under Roman civil law or the common law of the

period. This principle was ultimately adopted by the law merchant.

Merchants were required to make confession and to seek absolution before death, which often required making restitution for commercial offences. Excommunication was used by the Church as a means of enforcing the payment of debts and penalizing prohibited practices. It was not until the seventeenth century and later that there was a "secular literature of economic analysis which could compete with, substitute for, or influence the economic content of Scholastic moral theology." However, as we shall see there was a dualism in the Church's attitude towards

39. Bare promises were not enforceable under either the common law or the civil law. The law merchant drew upon the ecclesiastical practice of enforcing promises not under seal. See E. Allan Farnsworth, "The Past of Promise: An Historical Introduction to Contract," Columbia Law Review 69 (1969), pp. 588-99. In the following passage taken from A. W. B. Simpson, A History of the Common Law of Contract (Oxford: Clarenden Press, 1975), p. 4 Glanvil, writing in the twelfth century, explains his limited treatment of private agreements on the grounds that the royal court did not deal with such agreements: "We deal briefly with the foregoing contracts which are based on the consent of private persons because...it is not the custom of the court of the lord king to protect private agreements, nor does it even concern itself with such contracts as can be considered to be like private agreements."


41. Ibid., p. 46 Viner defines the term "scholastic" to cover all Catholic moral theologians and canonists who wrote in the tradition of the Church from the late Middle Ages to the end of the sixteenth century.
material wealth, evident in the tolerance of certain commercial practices, but the prohibition of others. This produced a somewhat uneven application of religious sanctions on commercial practices.\textsuperscript{42}

While the Church thus challenged merchant autonomy in many respects, other challenges came from controls imposed by local authorities. Local authorities regulated markets to ensure adequate supplies and to collect revenues from merchants who were granted the right to trade in markets and fairs. Thus it can be said that the

...dominant note of the period was authority. The social organization was a hierarchy of controls: the individual, if such there was, owed allegiance to priest and bishop of Holy Church, to lord and Baron of Feudal Order, to gild and town of a rising Third Estate. The foundations of obedience, which underlay all human activity, were established by churchmen. The world was a great penitential wherein man was fitted for the Kingdom of Heaven; the human being, conceived in iniquity and born in sin, was a depraved person; he must be kept free from the world, the flesh, and the devil; his plans, his actions, and even his thoughts were to be supervised by his betters, - to the great end of the salvation of his mortal soul. The spirit of the age, at least in ideal, imposed a religious purpose upon all human conduct.\textsuperscript{43}

\textsuperscript{42} Gilchrist in \textit{The Church and Economic Activity in the Middle Ages}, chap. 4 identifies this dualism in the Churches permissive attitude towards private property and slavery but its condemnation of avarice and the singling out of trade for condemnation. He shows how this dualism came to be reflected in dual standards applied to various commercial activities.

Amidst this authority structure the law merchant took shape, borrowing in some cases from canon law, as regards the principle of the sanctity of agreements, and, in other cases, evading or circumventing restrictions imposed by religious and local authorities. We will turn now to consider how these various influences and developments were manifested in the substantive and procedural dimensions of the regime.

1. Substantive Dimension

(a) Prices. During the medieval period the norm for foreign and wholesale transactions was the establishment of prices by agreement of the parties (i.e., contractual prices). In contrast, prices in local and retail transactions were fixed by local authorities using the canonical standard of the 'just price.' However, the 'just price' requirement did have some application to international transactions when foreign merchants traded in local fairs and markets subject to price controls. Furthermore, the issue of just prices for international transactions arose later in the development of the regime. Thus, it is important to consider the foundations of the requirement in some detail.

The norm of just prices reflected the priority given to the equity principle and to the principles of local intervention and the enhancement of political autonomy. "The essence of the medieval scheme of economic ethics had been its insistence on equity in bargaining - a contract is
fair, St. Thomas had said, when both parties gained from it equally." The monopolistic raising of prices through the manipulation of supplies, sales at prices that did not reflect equivalent value in exchange, and the taking of excessive profits were regarded as unjust. Maylnes formulated equity in prices in the following way:

> Every man knoweth, that in the Buying and Selling of Commodities there is an estimation and price demanded and agreed upon between both parties, according to a certain equality in the value of things, permuted by a true reason grounded upon the commodious use of things. So that equality is nothing else but a mutual voluntary estimation of things made in good order and true, wherein Inequality is not admitted or known.  

For many commodities prices were fixed by local authorities who considered market conditions, the level of necessary supplies, and the labour and costs of the producer. As Gilchrist notes, "[a]rtificially fixed prices, brought about by base business methods, such as monopoly or price agreement, forestalling, regrating, and engrossing, were considered unjust." Local authorities thus intervened to prevent price manipulation by requiring that all sales take place in open markets (market overt) and by limiting the activities of middlemen through enforcing the market

44. Tawney, Religion and the Rise of Capitalism, p. 152.
47. The Church and Economic Activity in the Middle Ages, p. 61.
offences or rules against regrating, engrossing, and forestalling.

*Forestalling* meant buying up goods before they got to the market, going out to intercept and purchase them on their way into town, or buying grain or produce in the country from the peasants who would normally have brought it into town. *Engrossing* meant trying to corner the market. In the middle ages supplies were limited, transportation was slow and difficult, and famine was usually imminent. By buying up large quantities of goods it was fairly easy to raise the price to the detriment of fellow gildsmen and the townsfolk. *Regrating* was buying to sell again at a profit. It represented the tendency for a middleman to come between the producer and the consumer and was frowned on especially when it was speculative or was done in connection with foodstuffs.... The prohibition of these practices was designed to protect the consumer as well as the members of the gild. Since it had a monopoly of the local trade, the gild was forced both by policy and by teachings of the Church to try to prevent the use of that monopoly to exploit the public.48

Merchant guilds, granted legitimate monopolies by local authorities, assisted in the enforcement of market regulations to minimize outside competition.49


49. See Pirenne, *Economic and Social History of Medieval Europe*, chap. 6 for a discussion of the origin and nature of merchant craft guilds. He argues that guilds performed a public function of consumer protection by enforcing the rules against members. The guilds also provided members with protected markets and were a source of revenue for local authorities who exacted payment in return for the monopoly rights granted to the guild. See also Clough, *The Economic Development of Western Civilization*, pp. 99-103.
When the local authorities did not intervene to set prices, prices were established by the *communis estimatio*, or common estimation of the vendors. The individual was to be "guided by a consideration of 'what he must charge in order to maintain his position, and nourish himself suitably in it, and by a reasonable estimate of expenditure and labour'."\(^{50}\) Tawney notes that the formal theory of the just price went through some modification as fourteenth and fifteenth century theologians explored the foundation of the rule of 'common estimation' and developed distinctions between different types or grades of prices, generating significant exceptions.\(^{51}\) As we shall see in the discussion of price regulation in the second phase of the law merchant, by the seventeenth and eighteenth centuries the number of permitted exceptions to the requirement of just prices contributed to significant erosion of the norm.

In assessing the strength of the norms governing prices in the medieval phase of the law merchant, it is thus necessary to distinguish between the regulation of

\(^{50}\) Clough and Cole, *Economic History of Europe*, p. 40.

\(^{51}\) He notes that in the fourteenth century some emphasized the subjective nature of common estimation and that its essence should be utility. They drew the conclusion that a fair price was "most likely to be reached under freedom of contract, since the mere fact that a bargain had been struck showed that both parties were satisfied." While he acknowledges that this view "contained the seeds of an intellectual revolution," he also notes that it was not the characteristic doctrine of the time. *Ibid.*
international transactions and domestic transactions. The norm for international transactions (foreign and wholesale trade) was contractual prices, while domestic transactions (local and retail trade) were subject to the just price requirement. As a general rule, foreign and wholesale trade were not subject to the just price requirement and merchants engaging in such trade were not subject to prosecution for committing market offences.\textsuperscript{52} There was, however, some weakness in the norm of contractual prices, for foreign merchants engaging in trade in markets and fairs subject to price controls were subject to discipline, unless they were granted an exemption. Furthermore, the law merchant notion of equity imposed some limits to prices that did not substantially reflect the value of the goods exchanged, although the standards were not as exacting as those established by canon law.\textsuperscript{53} Moreover, as Clough argues market and price regulations reflected class distinctions.

Since the city fathers were exclusively consumers of foodstuffs, they wanted adequate and steady supplies at reasonable, if not low prices. To achieve their ends they forced on both peasants and retail food merchants all kinds of restrictive rules and those people had to submit to them because they depended on cities for markets....no such strict rules

\textsuperscript{52} For examples of the enforcement of market offences in the thirteenth and fourteenth centuries see Selden Society, \textit{Leet Jurisdiction in Norwich}, William Hudson, ed. (London: B. Quaritch, 1892).

\textsuperscript{53} For examples of law merchant standards of fairness in prices see the cases recorded in Selden Society, \textit{Leet Jurisdiction}. 
were applied to the wholesale business in foods in long-distance trade, for some of the rich merchants were engaged in this activity and they did not want to do anything to curb their opportunities for making a profit.\(^5^4\)

Clough notes that a "kind of a 'deal'" was struck between the local authorities and individual local and retail trades whereby the latter would be granted a monopoly of business in return for enforcing the canonical requirement of a just price and market offences.\(^5^5\) The rules were strictly enforced against local retailers and "had considerable efficacy in maintaining honesty, quality, and fair prices."\(^5^6\) Ecclesiastical authorities imposed the sanctions of excommunication and refusal of a Christian burial, while the local market and guild courts imposed fines, suspensions, and the sanction of market exclusion. However, those trading wholesale and in long distance trade were not subject to the same discipline. Pirenne, as well, observes that import trade and large scale commerce largely escaped these restrictions. The regulations were designed for the municipal market and could not be enforced against "the wholesale merchant, who unloaded on the town quays the cargo of several ships laden with rye, cheese, or casks of


56. In a review of the case law dealing with market offences, Thompson in "The Moral Economy of the English Crowd in the Eighteenth Century," p. 96, note 64 observes that it was predominantly local petty traders who were subject to discipline.
Indeed, such merchants were forced to work through the very middlemen or brokers prohibited by the market restrictions. Furthermore, local political authorities were unwilling to impose constraints upon foreign and wholesale merchants as they provided a lucrative source of foreign exchange and revenues in the form of customs duties and taxes. The norm of contractual prices was thus moderately strong for international transactions. Local authorities were either unable or unwilling to impose the local norm of just prices on foreign and wholesale trade in any comprehensive manner.

(b) Liability for Defective Goods. During the medieval phase of the regime, as in the case of prices, different standards governed liability for defective goods in international and in domestic transactions. The law merchant imposed a standard of limited liability. Drawing upon the Roman law of warranty and reflecting law merchant standards of equity in contracting, vendors were not liable for patent defects and liability for latent defects was limited. However, for domestic transactions, vendors were held to standards of strict liability and could avail of few

57. Economic and Social History of Europe, pp. 176-7.
58. Ibid.
defences. Regulations imposing quality controls formed a "buyer's code," imposing "exacting standards" on the seller. As in the case of the just price standard, the standards governing liability for defective goods reflected canon law and the paternalistic and collectivist nature of medieval commercial regulation.

In medieval society the regulation of trade and commerce was characterized by a strong preference for the rights of the consumer. Extensive regulation sought to insure that all products were the result of good workmanship and proper measure, and that they were sold at a fair price. The community at large was also given preference.

As Hamilton notes, in the "prevailing legal theory it was not so much the buyer who was injured as the commune." Acquinas had taught that a seller sins and a sale is void if goods are sold containing a defect in kind, quantity, or quality of which the vendor has knowledge. Furthermore, the vendor must compensate the purchaser for losses sustained by defects of which the vendor had no knowledge. Medieval society adopted this standard of strict liability for defective goods. The vendor was accountable through

63. Ibid., p. 1138.
annulment of the contract, compensation of the buyer, or a reduction in the purchase price.

Local authorities intervened to establish quality control standards. Weights and measures were standardized. For many foodstuffs and manufactured goods specific rules regulated material content, production methods, and measurement. These regulations were enforced through a variety of means. Local authorities sent inspectors around to ensure that artisans and merchants conformed to the rules. In England, the Court of Leek or view of the frankpledge was held twice a year at which time the conduct of merchants and tradesmen (e.g., bakers, butchers, tailors, goldsmiths, weavers, etc.) was reviewed. Attendees were expected to report upon the activities of others and records were kept of complaints regarding breaches of content, quality, measurement, and production standards. Merchant guilds assisted in the enforcement of quality controls through the punishment or exclusion of members who breached the rules. "Artisans who broke the rules were severely punished by fines and suspensions; in the case of repeated infractions, they might be subjected to the ignominy of having their shoddy goods exposed before their

64. See Hamilton, "The Ancient Maxim Caveat Emptor" for a very extensive review of the sorts of quality controls placed upon foodstuffs and manufactured goods.

65. Hamilton, ibid., p. 1144 notes that the Court of Leet performed a preventive and not a remedial function for there were no provisions for suits by aggrieved consumers.
shops for all to see. Still worse, the artisan might be read out of his guild and hence prevented from practicing his trade."

In the fairs and markets the rule of market overt and the rule requiring "frontage," the open display of wares, contributed to detection of nonconforming goods.

The discipline imposed on the artisan naturally aimed at ensuring the irreproachable quality of manufactured products. In this sense it was exercised to the advantage of the consumer. The rigid regulation of the towns made scamped workmanship as impossible, or, at least, as difficult and as dangerous, in industry as was the adulteration in food. The severity of the punishments inflicted for fraud or even for mere carelessness is astonishing. The artisan was not only subject to the constant control of municipal overseers, who had the right to enter his workshop by day or night, but also to that of the public, under whose eyes he was ordered to work at his window.

As in the case of the just price requirement, quality controls were enforced primarily against those engaged in production for the local, retail trade. Those producing for wholesale and export trade were not subject to the same degree of discipline. Guild discipline, the inspection procedures of municipal authorities, and the controls exerted by direct and public exchange in the fairs and markets could not extend to cover those working in the countryside for export or those working in towns for the wholesale trade. These workers "formed a class apart among

67. Pirenne, Economic and Social History of Europe, p. 186.
the other artisans and bore a pretty close resemblance to the modern proletariat." 68 While some were organized into associations, these associations did not exercise the control exercised by the guild system. 69 They worked for merchants for the export or wholesale market and were thus not subject to the controls exerted by direct exchange with consumers in the fairs and markets. Nor did the quality control standards have the same impact on foreign merchants engaged in import trade. Foreign merchants were prohibited from engaging in retail trade and trading with strangers. "During their stay they were to lodge with a 'host' appointed by the town or gild magistrates, and the host was held responsible for the behaviour of his guests and expected to see that they did not infringe the rights of the citizen by retail trade or by dealing with other strangers". 70 Mitchell notes that while the rule of 'going to host' fell into disuse in England in the fifteenth century, it continued to be enforced on the Continent. Foreign merchants thus operated through agents or brokers, who in turn would arrange sales to the local retail merchants, rendering direct accountability of the producer to the consumer virtually impossible. While, as noted

68. Ibid., p. 189.


above, the law merchant did impose liability on the seller for defective goods, the discipline imposed by the merchant courts was not as extensive or demanding as that imposed by local political, religious, and guild authorities. As a result the norm of limited liability for defective goods was moderately strong for international transactions. Local and retail trade, in contrast, was subject to standards of strict liability.

(c) Allocation of Transportation Costs and Liabilities. The norm governing the allocation of costs and liabilities in the transport of goods during the medieval phase was the adoption of uniform standards allocating costs and limiting liabilities. The norm reflected the operation of the principles of merchant autonomy and the facilitation of exchange, as well as law merchant notions of equity. At this time ocean transportation was the main means for transporting goods over long distances and, thus, it is in the maritime laws that early standards evolved. Sanborn's review of the general principles of medieval maritime law discloses that while there were a variety options open to parties for allocating the costs and risks or liabilities of transportation, there was remarkable uniformity in law and practice. This he attributes to the similarity of problems arising out of seaborne trade. All parties faced the need to determine who pays for what and who is liable for loss or damage occurring at various points in the transport of
goods. The manner in which costs and liabilities were allocated between the parties depended very much on the contractual arrangements adopted. Many of these arrangements concern matters that go beyond the allocation of costs and liabilities, involving matters of finance and insurance. As early as the thirteenth century bills of lading, transferring to the holder a title to the document and the goods and having the character of negotiable instruments, were in use.71 There were numerous ways of determining the freight to be paid and the time at which payment was due under a bill of lading. A merchant could hire a ship by the month or for the entire voyage for a fixed price or at a price reflecting a percentage of the value of the goods. In cases where merchants formed charter-parties, there were a variety of options as to the times at which freight was payable and the proportions owed by the charter-party members. In most cases some proportion of freight was payable at the beginning of the voyage with the balance payable upon completion. The various obligations and risks of the parties concerning unloading, delivery, loss upon jettison of the goods, shipwreck or collision, or breach of contract by the merchant relating to late loading or of the shipowner for late departure depended very much on the specific terms of the agreement. The medieval commenda and societas, though forms of maritime

loans and partnerships in use from the tenth century, contained specific rules allocating the costs and risks of transportation.\textsuperscript{72} The same applied to the bottomry contract, which functioned as a mortgage on a ship given by the shipowner to a financier to pay for the costs of the voyage (the shipowner pledging the keel or bottom of the ship as security for repayment of the loan).\textsuperscript{73} In cases where the agreement was silent as to the respective rights and obligations of the parties, the custom of the port applied.\textsuperscript{74}

While we see that there was considerable diversity in the options open to the parties to a maritime voyage for allocating costs and liabilities, the adoption of uniform guidelines establishing the broad parameters of liability assisted in the development of uniformity. These parameters in turn reflected the belief that merchants and shipowners would not engage in maritime trade in the absence of clear rules governing and limiting liability.\textsuperscript{75} The rule of limited liability thus came to characterize medieval


\textsuperscript{73} Ibid., pp. 103–5.

\textsuperscript{74} Ibid., p. 100.

\textsuperscript{75} Grotius in the seventeenth century endorsed the rule of limited liability on the grounds of public policy, arguing that it encouraged shipping. In contrast, unlimited liability was regarded as injurious to the interests of trade. Ibid., p. 121.
maritime law, reflecting the principle of the facilitation of exchange and law merchant notions of equity. As a general rule, liability for loss was contingent upon fault. A shipowner was liable for loss or damage to goods due, for example, to bad caulking, unless he could show that the damage was due to a storm or some other cause relieving him of responsibility. While liability was generally contingent upon fault, different standards governed the manner in which damages were apportioned between the parties. Whereas some of the earlier laws adopted the rule of unlimited liability, later codes came to limit liability and established rules governing the division of loss between the parties. Losses or costs occasioned by the common good, as in jettison of the goods for the ships safety or the borrowing of money by the ship's master to pay for necessaries, gave rise to the duty of all to contribute to payment of the loss and costs. This rule came to be known as contribution to the general average, which will be considered as a means by which parties limited their liabilities in the subsequent discussion of insurance. These rules provided a general framework for the regulation of transport costs and liabilities embodied in medieval sea laws, to which we will now turn.

Mention of the early sea laws and their genesis has already been made. The Sea Law of Rhodes had its origins in

76. Ibid., pp. 108–22.
ancient and local customs. Sanborn notes that it is the first collection of maritime laws of the late Roman Empire and it "was apparently compiled from earlier materials, was not to any great extent original, and it treats chiefly loss at sea and commercial risk."\(^77\) It is divided into three parts containing chapters stating the rules governing a variety of risks and obligations. The rules of relevance to this discussion include the right and results of jettison (Part III, chap. 9); the responsibility for ship or cargo where one of the parties is to blame (Part III, chap. 10); the obligation of two shipowners and two cargo owners to contribute (Part III, chap. 21); the duty of contribution to loss of ship and cargo (Part III, chaps. 26-44); the liability of the merchant for damage to the ship during loading, while at sea, and after it has been unloaded (Part III, chaps. 27-33); liability upon collision and the proportions by which contribution is made to the loss of a ship (Part III, chaps. 36, 37, 40, 41); the duty to contribute where the mast is cut away or broken (Part III, chap. 35); liability for damage to cargo (Part III, chaps. 38 and 39) and the rights and responsibilities governing salvage (Part III, chaps. 45-7).\(^78\)

Sanborn observes that the Sea Law of Rhodes was "not a bad code for its day, and it was certainly in use in the

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south of Italy for six or seven hundred years" and had a great influence on the content of Italian sea laws. Most notably, the sea laws of Trani, the Amalphi Code, and the decisions from the court of Pisa adopted rules from the Rhodian Sea law, as modified by commercial custom. Pisa, in particular, is noted as the source of a variety of transport documents, including bills of lading, charter-parties, contracts of affreightment, commenda (partnerships), and bottomry contracts. These contractual arrangements were universalized through the office of Consuls who travelled with merchants arbitrating and adjudicating maritime disputes.

Many of the rules embodied in the Sea Law of Rhodes were adopted in the later Laws or Rolls of Oleron in almost identical form. The Laws of Oleron contain a number of articles dealing with a broad range of topics including the prohibition of the ship's master from selling the ship (art. 1); the master's liability for the ships value upon shipwreck when he leaves port without the mariners' consent

79. Ibid., p. 37.

80. The Italian sea laws contained in the Ordinances of Trani and the laws of Amalphi, Venice, Pisa and Genoa will not be considered in any detail. For discussion of these and other Italian sea laws see ibid., pp. 45-60.

81. Ibid., pp. 59-60.

82. This is particularly so regarding the rules regulating contribution to the general average, to be discussed below under insurance.
and the master’s duty upon shipwreck (arts. 2, 3); the requirement that freight be paid at the end of the voyage and pro rated payment obligations upon shipwreck (art. 4); the right of the master to jettison the cargo and the obligation of the cargo owners to contribute to loss of cargo (art. 8); the obligation of cargo to contribute to costs when it is necessary for the master to cut the ship’s mast (art. 9); the duty of master and crew to safely discharge the cargo (art. 10); the liability of master and crew for not trimming the sail properly (art. 11); the merchant’s responsibility for paying for towage (art. 13); the master’s liability for loss of the ship if he wrongfully discharges a crewmember and does not hire another of equal skill (art. 14); equal division of damages payable for loss to ships and cargo when two ships collide at anchor (art. 15); the obligation of demurrage whereby a merchant must load a ship in a timely manner or pay damages to the master and crew (art. 22); the right of the master to sell part of the cargo at the market price of the port of destination if he is in a foreign port without money and necessities (art. 23).

In addition to these laws, the customs of the maritime court at Oleron gained wide currency. Together these rules

83. Sanborn notes that there are a number of versions of the Sea laws of Oleron and bases his analysis on the version found in the Black Book of English Admiralty.
were adopted by England, the ports of the Mediterranean, the Baltic, and the North Sea.\textsuperscript{84}

Further derivations of the Laws of Oleron are found in the Sea Laws of Wisby, thought to date from the thirteenth or fourteenth centuries.\textsuperscript{85} These laws contain rules regulating the expiration of the contract of hire (art. 7); prohibiting the sale of a hired ship (art. 10); requiring contribution to the costs of overly long or additional voyages (art. 11); requiring the contribution of cargo to damages arising from the necessary cutting of the mast (art. 12); providing for the right of the master to sell cables, cordage and cargo for provisions and the rights and obligations when the master is forced to enter into a bottomry contract to finance the voyage (arts. 13, 35, 45); defining the liability of the master for damages arising upon setting sail without the permission of the mariners (art. 14); providing for the right of the master to jettison goods for the general safety of the ship and the obligation of cargo to contribute (arts. 20–1, 38–40); defining the liability of the master for losses to wine resulting from improperly laden vessels (art. 23); providing for the equal division of damages between ships upon collision when there is no fault of the master of

\textsuperscript{84} \textit{Ibid.}, pp. 74–5.
\textsuperscript{85} \textit{Ibid.}, p. 76.

either ship (arts. 26, 50, 70) and for pro rata assessment of damage to cargo (art. 67); requiring payment by the merchant of the costs of voyages delayed more than two weeks at the merchants instance (art. 34); identifying the obligation of the master to exercise care in preserving the cargo upon mooring and providing for liability for losses upon breach of the obligation (art. 36); defining the duty of mariners to care for the cargo (arts. 47-9); defining the obligation to pay the master within eight to fifteen days of conclusion of the voyage (art. 52); specifying the rights and obligations of merchant and master when it is necessary to put into another port (art. 53); defining the obligation of master and merchant when a ship runs aground (art. 55); defining the master's right to retain the goods until payment by the merchant if the master questions the honesty or ability of the merchant to pay (arts. 57-8); and, providing for the master's obligation to reimburse the merchant for goods sold to provision the ship should the ship be lost (art. 68).  

The third famous code is the Customs of the Sea of Barcelona. Sanborn observes that the code was not established or promulgated by public authorities. Nor are its provisions "couched in imperative terms; usages are

stated, explained, or commented upon." It is thought to have been first printed in the Catalan dialect in the fifteenth century, but to date from the fourteenth century.

The Customs of the Sea became known... in the chief maritime ports of the Mediterranean. They were introduced first into Valencia, then into the Island of Majorca, then into Sicily, then into Rousillon, all of which countries were under the scepter of the King of Aragon, before any version of them was printed at Barcelona. Within half a century after they were printed in the Book of the Consulate of the Sea at Barcelona they were translated into the language of Castile and of Italy. They were further translated into French before the conclusion of the sixteenth century, into Latin sometime in the seventeenth century, into Dutch at the beginning of the eighteenth century, and into German in the course of the same century. 88

These Customs govern a number of matters, including for example the influence of force majeure on liability; the rules governing shipwreck and jettison; the documents, conditions, and liabilities of affreightment contracts; obligations regarding the loading, storage, and unloading of goods; partnership responsibilities; liabilities in marine accidents and the mutual obligations of masters, loaders, and passengers.

These laws reflect considerable uniformity in the manner by which the costs and risks of transportation were

87. Ibid., pp. 82-3.

allocated between and among the parties to maritime adventures. The widespread adoption by merchants and merchant courts of the standards embodied in the sea laws suggest that the norms of allocating costs and limiting liabilities were of considerable efficacy and strength. Furthermore, the diversity of the contractual arrangements available to parties evidences the value given to the principle of merchant autonomy. While merchants had a broad range of contractual options, there was a clear recognition of the need for rules governing and limiting liabilities. These rules facilitated commercial exchange by reducing transaction costs, establishing property rights, and providing greater certainty of the rights and obligations of parties to maritime adventures. The development of standard transportation agreements lowered costs by obviating the need to negotiate a contract each time a merchant shipped goods. Furthermore, the establishment of uniform standards, clear property rights, and entitlements reduced the uncertainty facing parties as to the rules that would apply should disputes arise.

(d) Insurance. Similar conditions prevailed in the medieval regulation of insurance. Merchants devised uniform means of apportioning risk through limiting their liabilities. The norm of apportioning risks developed through merchant custom and practice to facilitate exchange by providing greater certainty and security for merchants. The various means
devised to apportion risk were enforceable only in merchant courts and under the law merchant and, thus, reflected the operation of the principle of merchant autonomy.

Insurance, if defined narrowly as "a contract by which one party (the insurer) undertakes to indemnify another (the insured) against loss, in consideration of a premium," appeared only in the fourteenth century. However, if defined more broadly to include "any kind of conventional arrangement by which one or more persons assume the risk of perils to which others are exposed," then the practice of insurance goes back much earlier. In the medieval period the practice of insurance first developed in the context of maritime transportation. It developed from maritime loans of bottomry (loans secured by the ship), and respondentia (loans secured by the cargo) and the rule of contribution to the general average. These maritime loans, in addition to raising capital, functioned to disperse risks amongst lenders, merchants, and shipowners. They contained


91. Sanborn in Origins of Early English Maritime and Commercial law, p. 19 traces the practice of maritime insurance to the early days of Christianity and caravan insurance and the insurance of beasts and ships to the fourth century A.D. in the Babylonian Talmud. See also ibid.

provisions spreading the risks of loss of cargo or ship amongst the parties. The rule of contribution to the general average originated in Roman law in terms of the sharing of responsibility for losses occasioned by needs of common safety.\textsuperscript{93} The medieval sea laws varied this rule so that it became a means for

\textit{...mutual insurance of each other by ship and cargo. If the ship is wrecked, dismasted, or loses her tackling, is run into, burnt or attacked by pirates; if the cargo is lost, wetted or plundered, and if no one is to blame for the loss, the Sea Law lays down in many places that ship and cargo, so far as saved, are to contribute to ship and cargo so far as lost. The common safety resulting from a deliberate sacrifice is not considered, for it is only necessary, in order to have contribution, that there shall have been a loss without the owner's negligence and without the responsibility of any other person in the maritime adventure. The result follows that, by participation in the voyage, one mutually insures, and is insured by, the ship and the property of the other shippers.}\textsuperscript{94}

Sea loans embodying the rule of contribution to the general average were widely used in the Italian cities in the thirteenth and fourteenth centuries. Vance, upon reviewing records of merchants and financiers from the period, concludes that "as early as 1318 the custom of making insurances upon goods subject to peril of transportation on

\textsuperscript{93} But note that Vance in "The Early History of Insurance Law," p. 100 note 1 cites evidence that the rule of contribution to the general average was in use in ancient Greece.

sea or land had become a customary incident of traffic."\textsuperscript{95} The earliest known insurance policy was made in Genoa in 1347, while a policy issued by a Genoese underwriter is recorded in Bruges in 1370.\textsuperscript{96} In the fifteenth century, Barcelona passed ordinances regulating marine insurance.\textsuperscript{97} These regulations were translated into several languages and "exercised a considerable influence upon the law of insurance by giving precision to the usages and promoting uniformity in the laws of the chief countries of Europe."\textsuperscript{98} Italian merchants carried their practices of insurance to ports and cities throughout Europe and to England in the fourteenth and fifteenth centuries. Mitchell stresses that these practices were not the 'creation of the legislature,' but the product of merchant custom. Furthermore, during the first phase, they were only recognized under the law merchant and in merchant courts, reflecting the merchant autonomy principle. Insofar as legislation regulating insurance existed, it functioned to articulate existing usages and customs.\textsuperscript{99} Vance too stresses the customary basis of insurance law:

\begin{footnotesize}
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\item \textsuperscript{95} "The Early History of Insurance Law," p. 105.
\item \textsuperscript{96} \textit{Ibid.}, p. 106.
\item \textsuperscript{97} \textit{Ibid}.
\item \textsuperscript{98} See Mitchell, "An Essay on the Early History of the Law Merchant," pp. 153-5 for the content of these regulations.
\item \textsuperscript{99} \textit{Ibid.}, pp. 141, 155.
\end{itemize}
\end{footnotesize}
The usages of insurance...readily took on the same character that had already been impressed upon other customs of traders engaged in international mercantile pursuits. The usages governing older forms of commerce, especially maritime usages, had found expression in collections of regulations and ordinances of great antiquity, that came to possess the greatest authority throughout Europe rather by their general acceptance than by the force of authoritative enactment.  

By the sixteenth century insurance was well established, as is evident in the various treatises on the subject published by Europeans.  

Insurance was introduced into England by the Italians and the first record of an insurance transaction dates from 1545 in the Court of Admiralty. As we shall see in the next chapter, as the medieval period of the law merchant drew to a close, state intervention into the regulation and adjudication of insurance matters occurred. However, as Mitchell notes, "the clauses of the early contracts remain the basis of the modern law of insurance of the civilized world...The modern law of insurance is more complicated and far more precise than the law and custom of the 14th or 15th centuries, but the development from old to new has been slow and natural, and the old and the new alike have the same underlying general principles." These principles reflected the belief that merchants should be accorded autonomy in the conduct of


commercial affairs, and that commercial exchange is facilitated by providing for greater certainty as to the allocation of risks and liabilities in the exchange relationship. The widespread usage of sea loans and the general adoption of the rule of contribution to the general average suggest that medieval insurance laws were of considerable strength and efficacy.

(e) Financing and Credit. During the medieval phase of the law merchant the norm was for merchants to utilize uniform payment and credit documents and procedures to facilitate sales contracts. Merchants had a broad range of choice as to the contractual arrangements adopted to finance sales transactions, which reflected the operation of the merchant autonomy principle. The principle was also reflected in the fact that these arrangements were only recognized under the law merchant and in merchant courts. It was only later, in the second phase, that common and civil law systems came to recognize and enforce such agreements.

A variety of arrangements were developed to facilitate commercial exchange and, in some cases, to circumvent restrictions on exchange posed by the general prohibition of usury. In other cases, the arrangements were regarded as permissible exceptions to the general prohibition. We will deal with each, in turn, after a brief discussion of the general prohibition of usury.
The medieval attitude towards the charging of interest had similar origins as the just price rule and the rule of strict liability for defective goods. A negative attitude toward the taking of profits, a general distaste for men of commerce, and a desire to protect the consumer characterized ecclesiastical attitudes towards usury. Gilchrist notes that the prohibition of usury "can be seen as a genuine attempt, somewhat misplaced when applied by rigorists to all profits of commercial enterprise, to protect consumer credit in an age when there were few opportunities to save for emergencies provoked by illness, disease, fire, war, alien seizure of one's goods or property, all of which deprived the peasant or the artisan of his means of livelihood and forced him into the hands of the money-lender or pawnbrokers." Others too have identified the purpose of the prohibition in the protection of the consumer: "[i]ts object was simple and direct - to prevent the well-to-do money-lender from exploiting the necessities of the peasant or the craftsman; its categories, which were quite appropriate to that type of transaction, were those of personal morality." The idea that fair or just exchange should represent rough equivalence in value, and that the taking of profit in the form of interest constituted the sin

103. See generally, Gilchrist, The Church and Economic Activity in the Middle Ages, chap. 4.

104. Ibid., pp. 63-4.

of avarice, characterized the attitude of early medieval theologians. The general prohibition of interest charges of the twelfth and thirteenth centuries thus reflected the influence of the canonical version of the equity principle. This principle emphasized fairness and equality in exchange and that commercial exchange should exercise a distributive function in society.

However, in spite of the general prohibition of interest, the charging of interest was in fact practiced in many places. Indeed, "lending at interest continued quite openly in such cities as Venice and Toulouse, and the municipal or state authorities, e. g., in the Low Countries, usually licensed or protected the public usurers."¹⁰⁶ The prohibition was generally enforced against local and small lenders and pawn-brokers and did not extend in any significant way to the activities of the great merchants engaged in wholesale or foreign trade.¹⁰⁷

The distinction between pawnbroking, which is disreputable, and high finance, which is eminently honorable, was as familiar in the Age of Faith as in the twentieth century; and no reasonable judgment of the medieval denunciation of usury is possible, unless it is remembered that whole ranges of financial business escaped from it almost altogether. It was rarely applied to the large-scale transactions of kings, feudal magnates,

¹⁰⁶. Gilchrist, The Church and Economic Activity in the Middle Ages, pp. 64- 5.

¹⁰⁷. The canonists "could not get at occult usurers, which included the great merchants, and their profits, for they claimed, and on paper proved, that they took no interest," ibid., p. 48.
bishops and abbots.... It was even more rarely applied to the Papacy itself; Popes regularly employed the international banking-houses of the day, with singular indifference, as was frequently complained, to the morality of their business methods.... As a rule, in spite of some qualms, the international money-market escaped from it; in the fourteenth century Italy was full of banking-houses doing foreign exchange business in every commercial center from Constantinople to London, and in the great fairs, such as those of Champagne, a special period was regularly set aside for the negotiation of loans and the settlement of debts.108

Merchants were ingenious in devising methods to evade the prohibition. A variety of documents were conceived to facilitate commercial exchange, functioning in part, as a means of concealing interest charges. Bills of exchange, were used as early as the twelfth century and achieved wide currency by the fourteenth century.109 A bill of exchange constituted both an acknowledgement by a purchaser of receipt of goods from a vendor at a set sum and a promise that the purchaser would pay the vendor for the goods in a certain amount, at a particular place, in the future. The payment of interest on the loan was concealed in the difference between the value of the goods and the sum payable at the future date.110 Bills of exchange were probably the most important financial instrument of the


period and have their origins in merchant custom.\textsuperscript{111} According to Malynes the "nature of a Bill of Exchange is so noble and excelling all other dealings between merchants, that the proceedings therein are extraordinary and singular, and not subject to any prescription by law or otherwise; but merely subsisting of a revered custom, used and solemnized concerning the same."\textsuperscript{112} In addition to providing a mechanism for evading the prohibition of usury, their importance can be attributed to the flexible and efficient system of credit they made possible. The system

...enabled a merchant by drawing, accepting, buying, or selling bills of exchange to have his funds where he wanted them, when he wanted them, with little risk. It was common to fix sums in the bill so that interest was paid to the person who granted any credit. The widespread use of the bill of exchange made clearing possible from the thirteenth century on. It was done largely at the fairs of Champagne at first and then successively at those of Geneva, Lyons, and Besacon. Clearing is the process by which the debts of various merchants are set off against each other and cancelled, without the actual transfer of money.... Practiced on a large scale...clearing permitted big transactions at the fairs with only relatively small cash transfers.\textsuperscript{113}

\textsuperscript{111} Edward Jenks, in "The Early History of Negotiable Instruments," in Selected Essays in Anglo-American Legal History, pp. 50-71 dates bills of exchange from the fourteenth century. However, Bewes in The Romance of the Law Merchant, chap. 4, argues that they can be traced to the Arabs in the eighth century who passed them on to the Italian traders who followed the Crusades.

\textsuperscript{112} Lex Mercatoria, vol. 1, p. 269.

\textsuperscript{113} Clough and Cole, Economic History of Europe, pp. 78-9.
The fair letter or lettre de foire, the early precursor of the letter of credit which developed at the fairs in the twelfth and thirteenth centuries, also provided a mechanism for concealing interest charges. Merchants short of cash would arrange to purchase the goods on credit, payment (including an interest charge) to be made upon resale at the end of the fair or at the next fair.\textsuperscript{114} Letters of credit came to function much like bills of exchange, enabling the clearing of debts without the direct exchange of money, and thus facilitating commercial transactions. In time, money-lenders became involved in the extension of credit or in the guarantee of the credit worthiness of the purchaser.\textsuperscript{115}

The sea loans, discussed above, also provided means for the avoidance of the prohibition of usury. Loans to build or repair a ship or to finance a voyage regularly contained hidden interest charges.\textsuperscript{116}

\textsuperscript{114} Ibid., p. 79. For a discussion of the history of letters of credit see E. P. Ellinger, \textit{Documentary Letters of Credit: A Comparative Study} (Singapore: University of Singapore Press, 1970), chap. 2. Ellinger argues that letters of credit were not in general usage on the Continent prior to the fourteenth century and in England prior to the seventeenth century. However, others date their usage from the twelfth and thirteenth centuries in the practices at the great fairs of Europe, in particular at those of Champagne, and in the commercial transactions of the English crown. See \textit{ibid.}, p. 79 and Sanborn, \textit{Origins of the Early English Maritime and Commercial Law}, pp. 347-8.


Other arrangements adopted by merchants were considered to be exceptions to the prohibition of usury. The prohibition of taking interest was formulated in the twelfth and thirteenth centuries in terms of a general prohibition of all forms of commercial profit. In time, however, as ecclesiastical authorities lost the battle against profit-making, they began to develop exceptions to the general prohibition. "Gradually the very word usury took on its modern meaning of excessive charges for loans, while interest or some other pleasing word was used for moderate charges."\textsuperscript{117} Profits on goods purchased for personal use or consumption that later had to be sold (forced sales) and profits on the sale of goods that embodied the labour of craftsmen or the investment of time and money came to be regarded as acceptable.\textsuperscript{118} Thus, the taking of profits of a partnership were permitted, provided that the lender assumed the partner's risk.\textsuperscript{119} Rent-charges on the produce from land were acceptable, as too was interest on the late payment on a loan.\textsuperscript{120} In some cases local authorities intervened to enable the taking of interest. The general

\textsuperscript{117} Clough and Cole, \textit{Economic History of Europe}, p. 82.

\textsuperscript{118} See Gilchrist, \textit{The Church and Economic Activity in the Middle Ages}, pp. 53-6.


\textsuperscript{120} See Gilchrist, \textit{The Church and Economic Activity in the Middle Ages}, pp. 67-70 for a more comprehensive list of the types of transactions that were regarded as exceptions to the prohibition of usury.
prohibition was suspended in order to enable the clearing of accounts during the fairs of Champagne, while in Genoa the authorities prohibited the attempt to use the prohibition as a means for invalidating insurance contracts. 121

The Reformation was to have a significant influence on the church's attitude towards commerce, contributing further to the development of distinctions between permissible and impermissible profit and charges. 122 Toward the close of the medieval phase, though some ecclesiastical restrictions remained, the charging of interest was widely practiced in the world of international finance. Petty, local pawnbrokers were subject to the prohibition, but it was generally inapplicable to larger transactions involving foreign or wholesale trade. As regards the latter, the arrangements developed by merchants to facilitate the payment and financing of sales transactions in the great fairs and commercial ports avoided or were exempted from the church's prohibition. These arrangements were utilized with a high degree of uniformity. They were enforced under the law merchant in merchant courts with considerable success, leading Mitchell to conclude that the impact of the prohibition of usury has been "greatly exaggerated" and did


122. See generally, Viner, Religious Thought and Economic Society.
not significantly impede the development of an autonomous law merchant.\textsuperscript{123}

Thus we see conflicts between the equity principle and the principle of the facilitation of exchange and between local ecclesiastical intervention and merchant autonomy resolved in different ways for local finance and for international finance. In the former, local ecclesiastical regulations enforced the prohibition of usury. In the latter, the norm was merchant autonomy, albeit sometimes assisted by local political authorities, and the uniform practice of interest charges. With regard to the regulation of international trade, it would appear that there was little strength to the prohibition. Indeed, the very weakness of the prohibition is evident in the strength of the norm of adopting uniform credit and payment documents and procedures embodying interest charges.

Attention will now turn to the procedural dimension of the regime during the medieval phase.

2. Procedural Dimension

(a) Locus of Regulation. With regard to the identification of the legitimate agents of law creation and enforcement, a dualistic system of regulation applied to commerce. Merchants generally controlled foreign and wholesale trade,

particularly with reference to the procedures for creating and enforcing agreements. While local political and religious authorities exercised significant control over local and retail trade, regulating the substantive content of agreements and local markets, they were unable or unwilling to discipline merchants engaged in foreign and wholesale trade.

The norm of merchant control of wholesale and foreign trade reflects the priority given to the principle of merchant autonomy. This principle provides that merchants should be free to regulate commercial transactions by entering into contracts creating legal obligations, determining the substantive content of such agreements and enforcing those obligations without external interference. During the first phase, merchants engaged in foreign and wholesale trade operated as an autonomous class. Foreign merchants were accorded special status and were often exempted from the application of local laws and taxes. Procedures regulating the formation and enforcement of commercial agreements were governed by the law merchant, which operated outside the jurisdiction of the local authorities, as an autonomous and distinctive body of law. The law merchant stressed informality in the procedures to create and enforce transactions and recognized transactions that were not recognized by the local systems of civil and common law. The informality principle is evident in the absence of formal procedural constraints on the conditions
necessary to create or vary binding obligations. Unlike under the local legal systems, property in goods could pass without delivery and oral evidence was sufficient to vary written agreements and to create partnership agreements. Unlike under the common law, bare promises, not supported by consideration or under seal, were regarded by the law merchant as sufficient to create binding obligations. With regard to the enforcement of agreements, the law merchant provided informal rules of evidence and proof. The parties to agreements were regarded as competent and compellable witnesses, journal and ledger accounts were admissible into evidence, and the rules regulating the service of documents were relaxed. Indeed, as we shall see when we later consider the law merchant courts, local authorities at times intervened to exempt the law merchant courts from local procedural requirements in the interest of facilitating speedy dispute resolution. The law merchant also recognized transactions that were not recognized by the local systems of law. Bills of exchange, letters of credit, insurance contracts, charterparties, sea loans, bills of

124. See Bewes, Romance of the Law Merchant, Part I.


126. Ibid., pp. 242- 3.


lading, the assignment of debts, and a variety of partnership arrangements were recognized and enforced only under the law merchant.129

While local and retail merchants could avail of the procedural informality and the distinctive transactions afforded by the law merchant when litigating in merchant courts, they were also subject to significant local controls that did not extend to their counterparts engaged in wholesale and foreign trade. We saw earlier that local political and religious authorities intervened to regulate the substantive terms of local and retail sales agreements. Canonical notions of equity and the principles of local intervention and the enhancement of political autonomy prevailed in the regulation of prices, quality controls, and interest charges. As Pirenne observes, the "liberty of the individual was ruthlessly curtailed and the sale of foodstuffs subjected to a regulation almost despotic and inquisitorial."130 Rules regulating the market offences of regrating, forestalling, and engrossing were enforced against local and retail merchants, significantly controlling the local market environment for exchange. As was noted before, however, these offences simply could not be enforced against wholesale and foreign merchants who were


forced to work through the agency of middlemen, often outside or prior to the operation of the markets and fairs. Furthermore, in England, merchants were granted exemptions from municipal regulations.

In 1303 the Carta Mercatoria gave to certain foreign merchants, in return for certain customs duties, exemption from certain municipal dues, freedom to deal wholesale in all cities and towns, power to export their merchandize, and liberty to dwell where they pleased. They were promised speedy justice "secundum legem mercatoriam" from the officials "feriarum, civitatum, burgorum, et villarum mercatoriamrum;" and any misdoings of these officials were to be punished.\textsuperscript{131}

Local market intervention, however, extended beyond the enforcement of market offences, prices, quality controls, and interest charges in a manner touching upon all merchants selling in the markets and fairs. This intervention is generally regarded as reflecting the first hint of the significant control that states were to come to exert over commercial activities.\textsuperscript{132} Local authorities regulated where, when, and what could be sold, in some cases to whom, as well as the administration of markets, in the grant of a right to convene a market or fair. The right to convene a fair could be acquired by prescriptive right or by prerogative grant. The right or grant generally included "the right of police and justice...which had the effect of

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  \item[132.] Pirenne, Economic and Social History of Medieval Europe, chap. 6, part II.
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facilitating the enforcement of summary justice and the law of the market, apart from the ordinary King's jurisdiction and the common law."133 While we will consider the jurisdictional right granted to set up fair courts and tribunals later under the issue of Dispute Settlement, the grant of a fair specified when the fair could be held, the location, and the goods that could be sold. Local authorities granted merchants safe-conduct during the fair. In England for some time nationals were forbidden from engaging in export trade, while foreign merchants were granted special rights.134 Merchants, unless granted an exemption, thus had to operate within the broad parameters established by the local authorities.

Furthermore, with regard to foreign and wholesale trade, the norm of merchant control was not absolute, but was also exercised within the broad parameters established by local authorities. The staples system developed in England and on the Continent in the fourteenth century as a means of regulating wholesale and foreign trade by concentrating commercial exchange in specific towns. Certain towns were designated markets for particular goods. Brodhurst notes that the staple system, by centralizing commercial exchange, functioned to facilitate the collection of royal customs, to ensure the quality of goods

exported,\textsuperscript{135} to replenish the gold supply,\textsuperscript{136} and to attract foreign trade by providing legal machinery for the recovery of debts.\textsuperscript{137} The staples system reflected the sorts of policy concerns that were, during the second phase of the law merchant, to provide the foundations of national, mercantilist regulation.\textsuperscript{138}

The strength of the norm governing the identification of legitimate agents capable of creating and enforcing standards of broad application thus varied according to the nature of the transaction. For foreign and wholesale transactions merchants were generally quite successful in creating and enforcing uniform standards, evidencing the strength of the norm of merchant control. However, while local authorities did not regulate prices, quality, and interest charges or enforce market offences with much success for wholesale and foreign transactions, merchants engaging in such trade still had to conform to the discipline of the staples system, unless they were granted exemptions, as was often the case. There was thus some weakness in the norm of merchant control when foreign and

\textsuperscript{135} In England, for example, legislation was enacted limiting the sale of wool to fifteen staple towns and regulating the weighing of wool.

\textsuperscript{136} English merchants trading at Calais were required to take payment in precious metals.


\textsuperscript{138} See generally Pirenne, \textit{History of Medieval Europe}, chap. 6 and \textit{ibid.}
wholesale trade were subject to local regulations. Further weakness is evident in the regulation of local and retail trade. Here the norm of merchant control was very weak as local authorities regulated the substantive content of agreements regarding prices, product liability, and interest charges and the market environment for exchange through the strict enforcement of market offences.

(b) Methodology of Rule Creation. With regard to the sources of law, the norm during the first phase was the widespread acceptance of commercial custom as a source of commercial law. While local political and religious authorities enacted legislation regulating local transactions, the legislation did not limit international transactions in any significant way.

We have seen that many transactions were universalized through merchant custom and usage and, indeed, were only enforceable under the law merchant and in merchant courts. We have noted that the various sea laws governing transport costs and liabilities have their origin in commercial practice.139 Bills of lading, charterparties, and partnership agreements, though in some instances of ancient origin, were modified by and gained their currency and efficacy through commercial custom. So too, the principles

139. See also Thomas L. Mears, "The History of the Admiralty Jurisdiction," in Selected Essays in Anglo-American Legal History, pp. 312-64 for a discussion of the customary basis of maritime law.
governing insurance and the range of instruments available to finance transactions were developed and legitimized by merchant custom. The rule of contribution to the general average, the various sea loans utilized, letters of credit, and bills of exchange were widely used and regarded as part of the custom of commerce. Insofar as commercial codes or statutes addressed such transactions, they generally provided authoritative statements of commercial custom:

...by far the largest element in the body of the maritime law was either created or modified by custom. Such was the case with the law merchant, which was also mostly customary law....in the Middle Ages the words 'custom' and 'statute' are used quite interchangeably. The very word 'statute' may mislead us considerably in the sense in which it was used, say six centuries ago, because many statutes then were just as much a compilation of existing customs as a modern statute may be a compilation of existing caselaw. And so, although when one examines a statute it may seem to be a new and sweeping code passed by a city or a gild, one is much more likely to find that it has been built up almost entirely upon a basis of custom and borrowed bodily from some other place.

Custom is ... the ruling principle and the originating force of the law merchant; 140

While local authorities did intervene to enact legislation regulating the local market environment and canon law regulated significant aspects of local and retail trade, the law governing international transactions was predominantly custom-based. Thus the norm identifying custom as a source

of law was strong for international transactions, but weak for largely domestic transactions.

Reliance upon commercial custom and usage reflects the priority attached to the principles of the facilitation of exchange, informality, and merchant autonomy. Indeed, the facilitative nature of flexible and informal standards are stressed as dominant characteristics of the medieval law merchant. 141 Today, customary law is generally regarded as providing greater flexibility and adaptability than legislation 142 and, as Schmitthoff notes, it is intimately related to the principle of merchant autonomy.

The essential difference between the two sources of the law of international trade is that international legislation applies, in the last resort, by virtue of the authority of the national sovereign but international custom is founded on the autonomy of the wills of the parties who adopt it as the regime applicable to the individual transactions at hand. 143

Considerable efficiencies are said to flow from custom-based commercial regulation, both in terms of facilitating exchange and in terms of unifying commercial law. 144

141. See generally Trakman, The Law Merchant.


distinguishing characteristic of the medieval phase was the ability of merchants to generate, modify, and extinguish legal standards in response to qualitative and quantitative commercial developments through changes in commercial custom. Medieval merchants, however, were not acting in response to any conscious preference for customary law over statutory law, as the distinction between the two had not yet clearly emerged. Furthermore, they did not have liberal and neo-liberal theory to instruct them on transaction cost economics and the efficiencies of customary law\textsuperscript{145}. However, the development of customary standards did reflect a consensus amongst merchants regarding the need for commercial regulation. Moreover, these standards reflected a consensus regarding the value of facilitating exchange by creating informal and permissive rule structures that enabled the expeditious conclusion of agreements and settlement of disputes.

With regard to the dominant coordinative strategy, the norm was the reliance upon uniformity in merchant practice to regulate international commercial relations. This was

consistent with the identification of merchant custom as the primary source of law. Insofar as merchants or local authorities utilized codes and legislation to harmonize or unify commercial laws, as noted above, they generally adopted, or restated merchant custom and practice. The issue of the appropriate coordinative strategy did not really arise in this phase for, as David notes, unification only really became a concern later upon the disappearance of the medieval *jus commune*.

However, the development by merchants of uniform commercial practices governing the sale, transportation, financing, and insurance of goods evidences the value that they placed on regularizing and standardizing commercial relations. Commercial practices changed and developed to reduce the transaction costs of exchange as commercial relations expanded. Moreover, in spite of the proliferation of transportation, financial, and insurance arrangements, commercial practices embodied standards that emphasized the need to avoid formalities and that encouraged the expeditious conclusion of commercial agreements. However, it has been noted that "[t]he benefits of all these developments...could only be enjoyed as long as merchants obeyed the Law Merchant. Moreover, since disputes arise even among honest merchants, there needed to be a

146. David in "The International Unification of Private Law" notes that there was really no "movement" for unification of private law prior to the nineteenth century.
system for hearing and settling these disputes."\textsuperscript{147} These "feats of coordination" were achieved through the development of a private enforcement system,\textsuperscript{148} to which we will now turn.

\textit{Dispute Settlement}

During the medieval phase, the norm was the settlement of disputes by private adjudication. Merchants developed a system of private adjudication and enforcement which reflected the priority attached to the merchant autonomy principle, the informality principle, and the arbitration principle.\textsuperscript{149}

Merchants developed a variety of courts for the settlement of their disputes and these courts achieved a high degree of independence from the local courts and the local legal systems. Indeed, they operated more like modern arbitration tribunals than like courts of law. As Schmitthoff notes "these commercial courts were unique; they

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\textsuperscript{147} Milgrom, et. al., "The Role of Institutions in the Revival of Trade," p. 3
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\textsuperscript{148} Ibid.
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were in the nature of modern conciliation and arbitration tribunals rather than courts in the strict sense of the word."\textsuperscript{150}

The right to hold a fair court, known also as a court of pie-powder, formed part of the grant of the right to hold a fair, issued by the king or local lord. The grant established the jurisdiction of the fair court and provided for its general administration. The following provides an example of a grant from the fifteenth century:

\textit{...it hath been all times accustomed, that every person coming to the said fairs, should have lawful remedy of all manner of contracts, trespasses, covenants, debts, and other deeds made or done within any of the same fairs, during the time of the said fair, and within the jurisdiction of the same, and to be tried by the merchants being of the same fair.}\textsuperscript{151}

The origin of the name pie-powder is somewhat in dispute. Some attribute it to the fact that in fair courts justice was administered "as speedily as the dust could fall or be removed from the feet of the litigants," while others attribute it to the fact that "the court was frequented by chapmen with dusty feet, who wandered from mart to mart."\textsuperscript{152} Whatever the origin, the courts of pie-powder were known for

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the speed with which disputes were settled and the informality of the procedures adopted. The law applied was the law merchant and the judgments rendered issued from juries of merchants. It has been noted that "the important thing about these fair courts was not, however, that they applied the law merchant, although they did, but that their decisions were actually made by merchants. ' [T]he merchants were the suitors or doomsmen; they found the judgment or declared the law.' Consequently, the law applied would be the local mercantile understanding of what the law of the particular situation was." 153 Fair courts throughout England and the Continent applied the law merchant, enforcing transactions unenforceable in the local common and civil law courts. 154

Merchants also had recourse to staple courts held in staple towns. "Justice...was to be done to the foreigner from day to day and hour to hour, according to the law of the staple or the law merchant, and not according to the common law or particular burghal usages." 155 Merchants elected a mayor of the staple and officers who were


empowered to keep the peace and to enforce or execute judgments of the court. In England, the Statute of the Staple of 1353 granted significant privileges, protections and independence to the staple courts. Pollock observes that the statute is "an epitome" of the royal policy whereby foreign merchants were treated tenderly in return for their payment of royal customs duties.

Merchant courts also sat in towns and boroughs applying the law merchant before juries composed of merchants and merchant guilds provided facilities for the arbitration of disputes between members. Generally, however, guilds did not exercise a regular jurisdiction.

In addition, courts in seaport towns applied the law merchant to maritime disputes. In England, the jurisdiction of the Court of Admiralty originated in the fourteenth century and was established by the fifteenth century:

It practically comprised all mercantile and shipping cases. All contracts made abroad,


159. Ibid., p. 300.

160. See generally Mears, "The History of the Admiralty Jurisdiction."
bills of exchange...commercial agencies abroad, charter parties, insurance, average, freight, non-delivery of, damage to, cargo, negligent navigation by masters, mariners, or pilots, breach of warranty of seaworthiness...in short, every kind of shipping business was dealt with by the admiralty court.\textsuperscript{161}

It is noteworthy that, at the time, the common law courts did not have jurisdiction over contracts entered into or torts committed abroad. Furthermore, common and civil law courts did not recognize or enforce the transactions utilized in maritime trade. Such transactions, along with the various financial and insurance instruments used by merchants, could only be enforced under the law merchant and in merchant courts.

During the medieval phase, the above courts operated independently and at the suit of merchants, evidencing the influence of the principle of merchant autonomy. Furthermore, the influence of the informality principle and the arbitration principle is evident in the informality and flexibility in procedures adopted\textsuperscript{162} and in the use of merchant juries. The merchant courts provided an efficacious system for settling merchant disputes and for enforcing transactions. The self-enforcement actions of merchants included the imposition of the sanctions of market


\textsuperscript{162} See generally Burdick, "The Contribution of the Law Merchant to the Common Law."
exclusion, bankruptcy, and loss of reputation and provided the foundation for a system of private adjudication suited to the needs of commercial actors. This system facilitated exchange by lowering transaction costs and by enforcing agreements. As Milgrom et. al., contend:

...an enduring pattern of trade over a wide geographical area cannot be sustained if it is profitable for merchants to renege on promises or repudiate agreements. In the larger trading towns and cities of northern Europe in the 10th through 13th centuries, it was not possible for every merchant to know the reputations of all others, so extensive trade required the development of some system like the Law Merchant system to fill the gap. 163

By centralizing enforcement in merchant courts, the system provided invaluable information about the credit-worthiness of those with whom a merchant traded. 164 In addition, it functioned as a valuable reputation system, enforcing honest behaviour.

The Law Merchant enforcement system...restores the equilibrium status of Honest behavior. It succeeds even though there is no state with police power and authority over a wide geographical realm to enforce contracts. Instead, the system works by making the reputation system of enforcement work better. The [law merchant] institutions...provide people with the information they need to recognize those who


164. See ibid., p. 6 for a game theoretic modelling of the law merchant enforcement system that represents "in an uncluttered way the basic facts that traders have opportunities and temptations to cheat and that there are gains possible if the traders can suppress these temptations and find a way to cooperate."
have been cheated to provide evidence of their injuries. Then, the reputation system itself provides the incentives for honest behavior and for payment by those who are found to have violated the code, and it encourages traders to boycott those who have flouted the system. Neither the reputation mechanism nor the institutions can be effective by themselves. They are complementary parts of a total system that works together to enforce honest behavior. 165

This system of private enforcement made commercial exchange over time and space possible by lowering the costs of exchange and providing merchants with some security that their agreements would be honoured.

B. Summary

This review of the substantive and procedural dimensions of the regime in the medieval phase shows that there were many overlapping authorities who sought to influence and control commercial activities. Kings and local lords, church authorities, and private merchant institutions all exercised some influence on the regulation of trade and commerce. This system of overlapping authorities is consistent with the political structure of medieval Europe, where

...far from constituting a system of independent political associations, the defining feature of Medieval Europe was the decentralization of political authority. The political map of thirteenth century Europe revealed not a clearly demarcated set of territorial units, but a tangle of overlapping feudal jurisdictions, plural allegiances and asymmetrical suzerainties.

165. Ibid., p. 19.
Within this maze no state system ever developed because the division of power among a multitude of different actors prevented it.  

This structure contributed to the absence of a clear distinction between and the conflation of domestic and foreign affairs. "In the Middle Ages, the modern distinction between domestic and international law was therefore unknown. Law was either peculiar to one community (jus civile) or common to many (jus gentium)."\(^{167}\)

Furthermore, there was no unambiguous distinction between matters of a public and a private nature. "The picture of an authoritarian control is everywhere in evidence; yet the lines of the agencies of supervision are far from clean-cut. The activities of a people passing out of feudalism do not lend themselves to our distinction between public and private."\(^{168}\) However, in spite of these ambiguities, as commerce expanded, private actors created an efficacious system regulating international commercial transactions. This system embodied shared merchant values regarding the desirability and purposes of commercial regulation and the procedures for implementing regime standards. Commercial actors developed customary laws that facilitated exchange by lowering the costs of doing business. Merchant customs

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minimized formal requirements and made informal and expeditious exchange possible. Merchants devised private institutions for the settlement of disputes that operated according to procedures consistent with the goal of facilitating exchange in a manner that did not impose undue formalities or restrictions on merchant autonomy.

...the merchants in Western Europe enhanced and refined their private legal code to serve the needs of the merchant trade -- all prior to the rise of the nation-state. Without this code and the system of enforcement, trade among virtual strangers would have been much more cumbersome, or even impossible. Remarkably, the Law Merchant institution appears to have been structured to support trade in a way that minimizes transaction costs, or at least incurs costs only in categories that are indispensable to any system that relies on boycotts and sanctions.169

Merchants and merchant law exercised considerable independence and autonomy from local authorities and local systems of law, which evidences the presence of a dualistic system of regulation governing domestic and international trade. The strength of the permissive and facilitative rules adopted by merchants and governing international transactions contrasts starkly with the weakness of the prohibitions and mandatory rules imposed by local religious and political authorities on domestic transactions.

The review of the regime's substantive dimension discloses that mandatory rules imposed by religious and

local political authorities governing prices, product quality, and interest charges were not comprehensive in coverage and were not widely regarded as legitimate by commercial actors. Although they were strictly enforced against local and retail trade and petty transactions, they were not enforced against larger scale wholesale and foreign trade. Indeed, the law merchant did not recognize these prohibitions and, in the case of the prohibition against usury and the market offences, it enforced ingenious agreements that evaded or concealed the prohibited practices.

In contrast, the permissive rules governing sales, transportation, insurance, and financing arrangements received uniform and universal application. These rules were comprehensive in the coverage of medieval commercial transactions and were widely regarded as legitimate by commercial actors. Indeed, their genesis in commercial custom and practice underlines the importance that merchants attached to regularizing their commercial relations in a certain and yet flexible manner.

In the procedural dimension, the medieval regime exhibits moderate strength in the recognition of legitimate agents capable of generating standards of broad application. Merchants were generally regarded as the legitimate agents for creating and enforcing standards of broad application for international transactions. Predominantly domestic transactions, however, were subject to local authorities and
local regulations. In addition, strong support for custom as a source of international commercial law and the adoption of uniform practice as an appropriate coordinative strategy evidence methods of law creation capable of generating standards of broad application and support. Widespread support for private adjudication and arbitration and the ability of merchants to impose effective sanctions for noncompliance provided the foundations for an efficacious private enforcement system. While we saw that religious authorities sought to infuse commercial exchange with canonical standards of equity and that local authorities attempted to regulate market activities, these challenges to merchant autonomy were of limited success. Although the law merchant embodied equitable standards, they functioned as discretionary correctives and not as distributional guidelines.

The broad appeal of the principle of merchant autonomy derived both from the inability of the "inchoate nation-state system" to regulate the "geographically dynamic" activities of the medieval merchant and from a hands-off approach to foreign merchants who were regarded as providing valuable revenues and supplies of foreign goods.\textsuperscript{170} Local

\textsuperscript{170} Cremades and Plehn, "The New Lex Mercatoria," p. 318. Medieval historians like Pirenne, Clough and Cole also emphasize the inability of local authorities to impose restrictions upon foreign and wholesale trade, in addition to the recognition that foreign merchants provided valuable sources of revenue, goods, and foreign exchange.
political, religious, and guild authorities lacked the capacity to regulate international transactions. We have seen that the local courts and local legal systems did not recognize law merchant transactions and, thus, were powerless to regulate or to enforce them. Bare promises, agreements entered into abroad, and the broad range of financial, transport, and insurance agreements entered into by merchants were recognized and enforceable only in private merchant courts. Furthermore, the discipline of guild authorities was limited to the activities of guild members, while limitations imposed by local political and religious authorities were most often relaxed for international transactions. Foreign merchants were often exempted from local price, quality, and interest restrictions. In return, merchants engaged in international transactions provided a valuable source of foreign exchange and revenue from the payment of customs duties and taxes. This suggests that, in addition to simply being unable to regulate international transactions in any significant way, the local authorities were unwilling to do so. Thus, while "[t]he ability of the merchant class to both generate and enforce its own norms of behavior allowed it to achieve a large degree of independence from these local sovereigns,"171 one must also consider the reluctance of the local authorities to interfere. In addition, while there are no reliable figures

on the volume of foreign trade in this period, most economic historians estimate that it was relatively modest in comparison to the increase in volume that occurred with colonial expansion.\footnote{172} It is likely that the reluctance of local authorities to intervene in foreign transactions was also a result of the relatively insignificant volume of foreign trade.

As we now turn to review the second phase in the development of the regime we will see that the emergence of states and their attempts to nationalize and control foreign commercial activities, which were increasing in volume, signalled a change in both the ability and the willingness of political authorities to regulate international transactions. This resulted in a decline in the influence of merchant autonomy and the principles associated with a flexible and adaptable regime.

\footnote{172. Trade statistics were not kept until the sixteenth century and Clough and Cole in \textit{Economic History of Europe}, p. 257 note that "statistics before the nineteenth century are notoriously unreliable and can be trusted only as general indications." They estimate that while trade expanded with the commercial revival of the eleventh century, greater expansion occurred in the seventeenth and eighteenth centuries with the rise of colonial trade.}
CHAPTER V

PHASE II: STATE BUILDING AND THE REGULATION OF PRIVATE INTERNATIONAL TRADE, 17th to 19th Centuries.

There was a profound transformation in the substantive and procedural dimensions of the regime during the second phase in its evolution. These changes reflect a declining commitment to the principle of merchant autonomy and a growing commitment to the principle of local or national intervention, as the dualistic regulation of commerce of the medieval phase was replaced by unitary systems of national control. However, as shall become evident, states differed in precise nature of the balance struck between the two competing principles. In addition, the importance attached to the informality principle and the arbitration principle declined in favour of increased formality and national adjudication. These alterations in the normative foundations of the regime contributed to an erosion of the universality of regime standards and, ultimately, to a decline in the strength of regime. However, the continuing value placed on the principles of freedom to contract and sanctity of contract and reliance on merchant custom provided considerable continuity in principles, leading to the conclusion that the regime did not disappear or die, but rather underwent transformation.

The Law Merchant did not die. It changed in the seventeenth century, becoming less universal and more localized under state influence; it began to reflect the policies, interests and procedures of kings. Merchant
custom remained the underlying source of much
of commercial law in Europe, and to a lesser
degree in England, but it differed from place
to place. 'National states inevitably
required that their indigenous policies and
concerns be given direct consideration in the
regulation of commerce. As a result,
distinctly domestic systems of law evolved as
the official regulators of both domestic and
international business.'

In order to fully understand these changes it is
necessary to consider the historical context within which
they occurred. Accordingly, before addressing the
substantive and procedural dimensions in detail, attention
will turn to the complex mix of political, economic, and
social developments that accompanied the changes in the
normative structure of the regime.

A. Nationalizing and Localizing the Law Merchant

A number of developments during the second phase
changed the environment for international commerce. A shift
in commercial power to the Atlantic states, which was
related to the establishment of strong nation states in
Western Europe engaged in state building and in overseas
expansion, the universal acceptance of the idea of national
sovereignty, the Reformation, the rise of capitalism, an
increase in the volume of foreign trade, and an enhanced
understanding of the economic basis of national power all
contributed to an alteration in the environment for

1. Bruce L. Benson, "The Spontaneous Evolution of
Commercial Law," Southern Economic Journal 55
Trakman, The Law Merchant.
commercial exchange. States engaged in the process of state building sought control over commercial activities. One of the means adopted to achieve national control was the nationalization and localization of trade law and practice. States came to incorporate the law merchant into their national legal systems. This process of nationalization, "though universal, was carried out in the various countries for different reasons, in different manners and in differing degrees." 2 In England, the incorporation of the law merchant occurred, in part, as a component of the consolidation of the system of the common law and its courts and, in part, as a necessary complement to the country's growing commercial power. In France, incorporation was achieved through various codifications motivated in the early years by concerns of economic state building, or mercantilism, and in the later years by French revolutionary ideals. In Germany, incorporation occurred through codifications aimed at securing political unification through the creation of uniform laws. In the United States, incorporation was achieved by the adoption of English commercial law and the unification of state commercial law practices. We will consider the experience of each country after a brief review of the impact of the most significant developments: the growth of the nation state and mercantilist commercial policies, the increase in the volume

of foreign trade, the rise of capitalism, the Reformation, and the advent of laissez-faire theory and the values of economic liberalism.

It is no accident that the states that were the major actors in the development of commercial law were those that were to become the most significant commercial powers. By the beginning of the sixteenth century Mediterranean trade had declined in importance as Atlantic ports became the major focus of commercial activity. The shift in commercial activity from the Mediterranean to the Atlantic was a result of the discoveries and overseas expansion, undertaken by the Western states, and the assistance that their strong national governments gave to the promotion of commerce. Spain and Portugal were the major commercial powers in the sixteenth century, France and Holland in the seventeenth century, France and England in the eighteenth century, and England in the nineteenth century.

The Mediterranean from the central position in Europe trade [sic] sank till it was almost a backwater. In part the change was caused by political factors. The new, strong, national states threw their weight behind their merchants and pushed their trade by force of arms. Lusty young countries like France and Spain made Italy their battleground.... Spain, Portugal, France and England (and later Holland) - all had good harbours on the Atlantic coast. They had governments strong and rich enough to push the explorations and develop the colonies. The very fact that they had not played a major role in medieval commerce made them all the more eager to seize the new opportunities and all the more ready to venture in untried
ways. Moreover, in the era that was dawning, the state was to play an active role in commerce. A city which was not part of a big national state could scarcely hope to compete in naval rivalry, in tariff wars, in the struggle for markets.³

Baltic trade too declined in importance as commercial opportunities were lost to the newly emerging nation states and as the Thirty Years War (1618-1648) contributed to the economic decline of Germany.

While we saw in the last chapter that local authorities did intervene to regulate markets and to direct certain, primarily local, aspects of commercial activity in the medieval phase, intervention took on a new meaning in the second phase as states adopted overtly mercantilist policies for a broad range of commercial activities. This was due, in part, to the tremendous increase in the volume of foreign commercial transactions generated by colonial expansion. It is estimated that British exports and imports increased by 500 per cent from the seventeenth to the eighteenth centuries.⁴ The experience in France was similar, with the major commercial expansion occurring in the eighteenth century. In Holland, in contrast, the expansion took place in the seventeenth century.

Mercantilism can be defined as 'economic state building' and involves the use of national policies and

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practices to achieve a variety of goals. These goals include securing economic unity through the creation of a national economy, attaining control over domestic economic processes and actors through a weakening of controls exercised by church, town, and guild authorities, and enhancing national power through the development of industrial and economic strength. "Mercantilism varied in every country, according to local conditions and traditions; yet it can be said in a general way that it was the economic counterpart of the political process by which the national states were being built up." The mercantilism of Portugal and Spain was more protectionist than that of the Dutch, while English and French mercantilism stressed the need to encourage domestic industrial production in addition to the expansion of trade and the accumulation of wealth.

5. See *ibid.*, pp. 197 et. seq., and see Clough, *The Economic Development of Western Civilization*, chap. 2.


7. Portuguese mercantilism focussed almost entirely upon the adoption of policies aimed at securing and maintaining royal control of the spice trade with India. Portuguese policies included exploiting the colonies for the exclusive benefit of the mother country, ensuring an excess of exports over imports, and accumulating bullion. Spain adopted similar policies, imposing considerable controls on colonial trade, while the Dutch adopted more open policies aimed at the facilitation of trade through the imposition of few customs duties and tariffs on imports. England and France, in contrast, emphasized the importance to economic state building of both domestic production and trade expansion. In England, the guild system and protective tariffs served to encourage domestic industry, while the Navigation Acts and Corn Laws were designed to protect and enhance national trade. In France, high protective tariffs, policies to encourage
However, what united the various approaches was the increased recognition of the role that economic matters played in the determination of national power. This recognition is closely linked to the rise of capitalism and to the economic expansion of Europe.

It was the increase in capitalist business that turned the attention of people to economic matters as the key to wealth and power. Sometimes the businessmen supported the mercantilist policies; sometimes they opposed them. In a general way, however, mercantilism helped the capitalist by putting the power of the state behind him, even though it hampered and restricted him at the same time. When the businessman had grown strong enough and wealthy enough (by the eighteenth century) he began to think about shaking off the control of the state and using it for his own purposes. The expansion of Europe made the search for national strength in part a competition for commerce, sea power, and colonies and greatly widened the field in which mercantilism could be applied. Furthermore, it brought to the fore just those areas on the Atlantic where the new states were developing national and mercantilist policies.  

In addition, the rise in capitalist business techniques and the growth in mercantilist doctrine had a major impact upon moral theology, and in effect sanctioned "a new degree

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exports and to enhance the productive capabilities of domestic producers formed the core of mercantilist practice. For a fuller review of the various forms that mercantilism took in these countries see Clough and Cole, *Economic History of Europe*, chap. 7, Clough, *The Economic Development of Western Civilization*, chap. 2 and North, *Structure and Change in Economic History*, chap. 11.

of freedom from religious constraints on individual enterprise and individual aspirations for economic betterment." With the growth of investment practices, capital markets, and new forms of business enterprises the church had increasingly to adapt moral theology to commercial practices. While the impact of such developments was felt more strongly in Protestant theology than in Catholic theology, by the end of the Reformation there was a considerable erosion of the church's influence on commercial activity.

The rise of nation states, the expansion of national control to virtually all aspects of commercial activity, and the Reformation had a significant impact upon the procedural dimension of the regime, affecting the locus of regulation, the methodology of rule creation, and dispute settlement. The substantive dimension of the regime was also affected by these developments, as religious controls on prices, product liability and usury weakened and as states developed different national standards governing substantive issues.


10. Viner, ibid., attributes the differential impact of these developments on Protestant and Catholic theology to the fact that the Protestant churches were more closely tied to the state. "Mercantilism, which was nationalistic in essence and stressed national objectives against the moral claims of individuals or other peoples, found an easier entry into the doctrinal teaching of clergymen belonging to the various state-established, state-supported, and largely state-dominated churches of Protestantism than into the corpus of tradition-bound and supra-national Catholic Church."
However, sources of continuity at the level of fundamental principles remained. Furthermore, they were bolstered by the development of influential reactions to mercantilist national control in the key commercial states and by a continuing, although weakened, influence of merchant custom.

The advent of laissez-faire theory and the values of economic liberalism in the eighteenth and nineteenth centuries and their adoption by the important commercial powers gave new meaning to the principles of merchant autonomy in contract law. Merchant autonomy was recast in a manner consistent with the principle of freedom of contract and, in combination with the principle of the sanctity of contract, provided the foundations for modern contract theory. The will theory of contract, which stresses the free will of parties to contract on terms agreeable to themselves, replaced medieval notions of equity in contracting and significantly influenced substantive and procedural norms and rules. In addition, continued, albeit lessened reliance on merchant custom provided further continuity. However, it will become evident as we turn to consider the experiences of the key commercial powers, that these influences did not have a uniform impact on states. The nationalization and localization of the law merchant proceeded differently and produced different results for each state. The loss of merchant autonomy in the procedural dimension was more pronounced in common law countries, particularly in England where merchants disappeared as a
special class. In contrast, on the Continent, many countries retained special jurisdictions and courts for commercial actions. Furthermore, national differences emerged in the specific content given to many regime rules.

As national judges and legislators codified commercial law, it tended to lose its cosmopolitan character and outlook. This process of nationalization of commercial law and of its increasing divorce from experience was characteristic of legal development not only in England and the United States, but also in France, Germany, and the other countries of Europe. When this process was coupled, as it often was, with a hostility toward the proof of mercantile custom, the result was to impede the adaptation of law to new economic circumstances. The tendency of traders to develop new commercial devices thus ran headlong into the tendency of national legal systems to codify, whether through statute or precedent or legal doctrine.11

Legal developments in England, the United States and France have been the most significant in the evolution of regime standards. English commercial law formed the foundation for commercial relations in the common law countries of the world. Laws modelled upon British statutes and common law were adopted by countries of the common law tradition. Through colonial expansion and trade relations the standards embodied in English commercial law have been transmitted throughout the world.12 While the influence of


British law, arguably, was most significant at the height of Britain's commercial supremacy in the activities of English traders and the great trading companies, the influence has been more subtle and enduring. The principles embodied in English commercial law established the core for a major part of western commercial law and though they have been subject to some modification over time, they have provided much consistency at the level of principle. While changes in commercial norms and rules have occurred, reflecting a different weighting of principles, the basic emphasis upon freedom of contract and the sanctity of agreements has endured.

As British commercial supremacy waned and the United States gained in strength as a commercial power, the influence of American commercial standards became more significant. The United States adopted British commercial law during the formative stages of its municipal legal system, but later came to enact significant reforms under the Uniform Commercial Code (UCC). As we will see, the standards embodied in the UCC became influential in establishing guiding principles for the development of modern commercial law in the third phase of the regime.

Developments in French commercial law, and to a lesser extent in German law, have been significant as sources of civilian commercial law. Civil or Romano-Germanic law developed on the basis of the Roman jus civil and has also been transmitted and received throughout the world through
the processes of colonization and adoption.\textsuperscript{13} Although different in many respects, the common law and civil law share much at the level of guiding principle, thus enabling their classification as one 'great family of Western law.' "In both, the law has undergone the influence of Christian morality and, since the Renaissance, philosophical teachings have given prominence to individualism, liberalism, and individual rights."\textsuperscript{14}

In England, nationalization of the law merchant proceeded on two fronts. One front involved the disappearance of the specialized merchant courts as their jurisdiction was absorbed by the common law courts. The other front involved the absorption of substantive merchant law into the common law.\textsuperscript{15} While more will be said later about the disappearance of the merchant courts, during the seventeenth century the staple courts died out, while the courts of pie powder declined in importance.\textsuperscript{16} Competition between the common law courts and the Admiralty Court was resolved in favor of the former, as the jurisdiction of the

\begin{itemize}
\item \textsuperscript{13} Ibid., p. 21.
\item \textsuperscript{14} Ibid., p. 24.
\item \textsuperscript{16} Burdick, "Contributions of the Law Merchant to the Common Law," pp. 43-4.
\end{itemize}
latter was severely curtailed in the same century. By the end of the seventeenth century the law merchant "was being gradually absorbed into the general legal system of the country. As in the case of internal trade, so in the case of the foreign trade, the older mercantile courts had ceased to exist. Jurisdiction was therefore assumed by the ordinary courts of law and equity." But the disappearance of commercial courts and the assumption of commercial jurisdiction by the common law courts produce certain anomalies. As previous discussions have shown, the common law courts did not recognize or enforce most transactions and procedures enforceable under the law merchant. As a result merchants were either forced to resort to private arbitration or when possible to the courts of equity. The common law courts responded by absorbing the law merchant into the common law. Under Lord Coke, as Chief Justice in the seventeenth century, this involved application of the law merchant as custom and not as law, and only to merchants. Merchants had to prove that they were merchants and then prove the customs upon which they relied to the satisfaction of the common law courts. And


18. Ibid., p. 328.
...as the Law Merchant was considered as custom, it was the habit to leave the custom and the facts to the jury without any directions in point of law, with a result that cases were rarely reported as laying down any particular rule, because it was almost impossible to separate the custom from the facts; as a result little was done towards building up any system of Mercantile Law in England.  

However, there was considerable discontent with this approach. Berman and Kaufman note that, as a body of customary law articulated by juries, "the law merchant was hardly suited for a leading commercial power, which England had become in the eighteenth century." Furthermore, merchants needed the law to be more clearly defined, while "from the point of view of national policy, there was a need for the law to be developed officially and not merely informally by commercial experience." As a result, in the eighteenth century, under the direction of Lord Chief Justice Mansfield, the law merchant was made part of the common law, applicable to all persons.

The incorporation of the law merchant, however, did not have a uniform influence on different areas of the common


21. Ibid.

22. In Pillans v. van Mierop 3 Burr. 1663, 97 Eng. Rep. 1035. (K. B. 1765) Lord Mansfield held that the rules of the law merchant were questions of law to be decided by the courts and not matters of custom to be proved by the parties.
law. Merchant custom, formerly an integral component of the law merchant, came to be of variable importance in different areas of the law. Merchant customs significantly influenced the development of laws governing financial transactions, insurance, and shipping. As a result these areas remained truer to their law merchant origins. This was not the case for the law governing contracts of sale, which came to adopt distinctively English rules. In some cases, innovations from the law merchant were incorporated into the common law. In other cases, however, incorporation was carried out by modifying the law merchant to suit the common law and its procedures.


24. Ibid.

25. As in the case of actions of account and certain rights among partners, as well as the right of stoppage of goods in transit.

26. This was the case for the development of many of the doctrines of contract law (i.e., the rules governing formation of a contract and consideration) and for the standards of liability for carriers of goods by sea.
period of absorption, therefore, the commercial law of England still might be based fundamentally on the customs of merchants, and to that extent might retain a cosmopolitan flavor as its chief distinction; but the direct reflection of former days had become a refraction.  

During the nineteenth century, significant areas of commercial law were codified on the basis of common law decisions. In some cases, codification contributed to a further decline in the cosmopolitan nature of English commercial law, and ultimately a decline in the universality of the law merchant, by strengthening the national character of the rules. For example, codification of the law governing sales contracts embodied distinctively English rules. Discontinuities appear, however, in that in other areas codification incorporated merchant custom. Codification of the laws governing bills of exchange, insurance, and maritime matters (e.g., shippers, carriers, general average, and salvage) incorporated international mercantile custom and thus retained significant universality.


28. For example, the laws governing the sale of goods, bills of exchange, carriers' liability, marine insurance, merchant shipping, bills of lading, partnerships, and companies.

Departures from the medieval law merchant were also evident in the procedural dimension. The declining role of custom as a source of law, the subjection of commercial transactions to increasing formalities, and the disappearance of merchant courts signalled significant deviations from the medieval regime.

In the United States, the law merchant was applied from the eighteenth century. Commercial law was regarded as part of the ordinary law and administered by the ordinary courts. It was only in the nineteenth and twentieth centuries, however, that codification of commercial law occurred. As in England, the common law was codified into and supplemented by commercial statutes governing the sale of goods, bills of lading, negotiable instruments, and other commercial matters. English legislation provided the model and foundation for American legislation in many areas and English case law was relied upon extensively in commercial disputes. As a result, commercial law in the United States embodied similar reflections of and departures from the medieval law merchant.


31. Due to the federal structure these statutes were enacted at the state level.

Local particularisms emerged in state laws, generating a movement in the twentieth century for the unification of state laws. Unification ultimately took the form of the Uniform Commercial Code (UCC). While the UCC unified domestic commercial laws, it also had an impact on international transactions by rendering American commercial rules more consistent with international usage. This brought American practices somewhat closer to Continental legal theory and practice in significant areas.

The nationalization and localization of the law merchant took quite a different course on the Continent. Many European countries retained distinct commercial jurisdictions, specialized commercial courts, and special treatment for merchants and commercial transactions.

On the Continent it was the appearance of national legislation in the age of mercantilism which effectively promoted the commercial law, but which at the same time led to the loss of its universality and to its splitting-up into particular national laws. The leading role here fell to France.

33. This is particularly so for the provisions governing the sale of goods, terms of trade in transport documents, and negotiable instruments. See Berman and Kaufman, "The Law of International Commercial Transactions (Lex Mercatoria)," p. 228. And see Trakman, The Law Merchant, p. 35.


In France, separate mercantile tribunals established in the sixteenth century increased in importance and proliferated. By the seventeenth century every major commercial town of France had a consular court for commercial causes. Land-based commerce and maritime trade were codified in the seventeenth century in the legislation of Colbert. The *Ordinance sur le commerce* (1673) and the *Ordonnance sur la marine* (1681) provided the models for the Napoleonic *Code de Commerce* (1807). The Napoleonic commercial code established the pattern of the separate and distinctive treatment of commercial matters, a practice subsequently adopted by many civil law countries. However, while this Code established the practice of separate treatment for commercial matters, it was inspired by French Revolutionary values that stressed the equality of citizens and freedom of commerce. Trade guilds were suppressed and the notion of a distinct status for merchants was replaced with the idea of a distinct status for


37. This code was one of the five Napoleonic codes enacted. In combination with the Civil Code of 1804 it marks the beginning of the distinction between commercial law and civil law.

38. von Cammerer, "The Influence of the Law of International Trade," p. 90. The distinction is recognized in the Spanish Commercial Code of 1829, the Portuguese Code of 1833, the Dutch Code of 1838, the Brazilian Code of 1850, the Italian Commercial Codes of 1865 and 1883, and the German codifications of 1861 and 1900.
commercial transactions. Tallon argues that the latter was more consistent with French Revolutionary values, though there was continuing hostility to the preservation of distinctive commercial courts. 39 As Schmitthoff notes, the Napoleonic codes gave final expression to the political ideals and the philosophy of the French Revolution. The fundamental concepts of the Napoleonic codification are freedom of contract and the assertion of ownership as an absolute right. The Napoleonic codes have been described as ratifying the triumph of the tiers etat in which, as we know, the commerçants and the liberal professions were prominent. The French codification is thus the final seal of a victorious political movement. 40

The French Commercial Code has been adopted or copied by Belgium, Luxembourg, Greece, and the French colonies. 41 In France, in the nineteenth century, legislation outside the Commercial Code was enacted governing a number of commercial matters, including bills of lading and cheques. 42

In comparison to the Anglo-American experience, the nationalization of French commercial law has resulted in less of a loss in universality. French commercial law retains a distinctiveness, more consistent with the medieval

39. "Civil Law and Commercial Law," pp. 8-9, 30. However, the distinction would appear to be less important than the author suggests, for he notes at p. 36 that French commercial law constitutes a "special regime" and confers on merchants a special status.


41. See Tallon, "Civil Law and Commercial Law," pp. 41-4 for a discussion of the experiences of these countries.

42. Ibid., p. 30.
law merchant, but lost to the commercial law of common law countries. Merchants have special rights and duties, the rules of evidence applied to commercial transactions are more liberal, while commercial transactions are subject to special jurisdiction in commercial courts comprised of merchant judges and subject to swifter and simpler procedures. 43

In Germany, the foundations of commercial law derive from the customs and rules of the merchant guilds. As in France, the separate commercial jurisdiction of the sixteenth century persisted, however, in Germany there were no separate commercial courts. The courts did retain a separate division for commercial matters, presided over by a judge and two merchant assessors, but no special rules of evidence or procedure applied. 44 While some commercial legislation was enacted in the eighteenth century, 45 the multiplicity of German states prevented codification prior to the nineteenth century. 46 The incorporation of the law merchant was largely achieved through commercial codifications of the nineteenth century. Schmitthoff argues that "in Germany the creation of commercial codes was the

43. Ibid., pp. 36-8.
44. Ibid., p. 16.
legal reflection of the struggle for political unity; it was a deliberate attempt to give impetus to the movement for German political unification by means of the creation of a uniform law.\textsuperscript{47} The first unitary commercial code was enacted in 1861. The General German Commercial Code became the law of the Confederation of Northern Germany and was extended to the entire German empire in 1871. It was revised in 1897 and, as in the case of France, legislative enactments in the nineteenth and twentieth centuries governing a variety of commercial matters outside the Code have added to German commercial law.\textsuperscript{48} The German Commercial Code has been adopted by Austria and forms the basis for Japanese commercial law.\textsuperscript{49}

While the distinctiveness of merchant law is not as pronounced in the German system as in the French system, it too appears to bear a greater likeness to the medieval law merchant than do its Anglo-American counterparts. The existence of a special commercial division and the use of merchant assessors are reflective of the medieval law merchant.

\textsuperscript{47} "International Business Law," p. 136.

\textsuperscript{48} For example the law on insurance contracts of 1908, the law on credit instruments of 1961, laws on transportation by river (1895), road (1952), air (1922), rail (1938), and various laws governing competition, and industry.

\textsuperscript{49} Tallon, "Civil Law and Commercial Law," pp. 18-20.
This review of the experiences of the major commercial states suggests that the process of nationalizing and localizing the law merchant did not produce uniform results. Common law jurisdictions emerge as more distinctively 'national' than do civil law jurisdictions. We will now turn to take a closer look at the impact that these developments had on the substantive and procedural dimensions of the regime in the second phase.

1. Substantive Dimension

(a) Prices. During the second phase in the evolution of the regime, the norm for international transactions continued to be contractual prices. Furthermore, while local regulation of prices and markets persisted into the second phase, eventually the rules governing domestic transactions were brought into line with those governing international transactions. These changes reflect a weakening of the distinction between local or retail transactions and foreign or wholesale transactions as national regulation became more comprehensive, subjecting all commercial transactions to similar discipline. The changes also reflect a decline in the influence of canonical notions of equity and the principles of local intervention and the enhancement of political autonomy as local authorities came to adopt the principle of freedom of contract in price setting.

The requirement of just prices and the enforcement of market offences persisted into the seventeenth and
eighteenth centuries. By the seventeenth century, however, there was an erosion of the just price requirement as a number of permissible exceptions proliferated.\textsuperscript{50} Considerable elasticity had entered into the definition of just prices as theologians came to adapt moral theology to developing commercial practices. As Viner notes:

\begin{quote}
...the doctrine of the just price lost most of whatever practical importance it may have had earlier as a justification for state, guild, or ecclesiastical interference with routine free-market, or competitive, processes. It retained doctrinal importance and practical value as a restraint on monopoly and as a guide for dealing with disputes in cases where there was no ascertainable market price, and where abnormal conditions, such as famine or siege, seemed to justify interference with ordinary market processes. But, except in cases of usury, the traditional questioning of the legitimacy of ordinary trading profits and the role of the middleman had almost completely disappeared from treatises on moral theology by the seventeenth century.\textsuperscript{51}
\end{quote}

The 'paternalist model' of price fixing and the enforcement of market offences continued into the seventeenth and eighteenth centuries. Regulatory statutes continued to be enacted in the eighteenth century controlling prices, but with less frequency.\textsuperscript{52} So too,

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local authorities continued to enforce the market offences of forestalling, regrating, and engrossing. "Indeed, for most of the eighteenth century the middleman remained legally suspect, and his operations were, in theory, severely restricted." These regulations formed part of the measures adopted by local and state authorities to gain control over economic activities in the era of mercantilism and state building.

As the rationale for mercantilist regulation came under attack, so too did the foundation for fixed prices and market regulations. England played a leading role in changing domestic pricing practices and thus exerted a profound influence on states that inherited or adopted the common law system. In 1772 legislation in England against forestalling was repealed, signalling a victory for the "new political economy" of laissez-faire and economic liberalism. As Thompson suggests, the "new political economy entailed a demoralizing of the theory of trade and consumption no less far-reaching than the more widely-debated dissolution of restrictions upon usury. By 'demoralizing' it is not suggested that Smith and his colleagues were immoral or were unconcerned with the public good. It is meant, rather, that the new political economy


54. Ibid., p. 89.
was disinfested of intrusive moral imperatives."  

Liberal economists argued that fixed prices distorted market mechanisms and that the marketing offences restricted the valuable role played by middlemen in the rationing of supplies. By the nineteenth century it was generally accepted that such practices interfered with natural patterns of exchange. Marketing offences disappeared and the requirement of the just price was superseded by what Adam Smith referred to as the "natural price." In law this came to mean the price agreed to by the contracting parties and, in the absence of agreement or in cases of underspecification, the courts implied that the parties intended the current market price to apply.  

The influence of liberal political economy extended beyond the common law family and embraced all Western systems of law in some degree. The principle of freedom of contract became the foundation for contract law on the Continent and beyond. The emphasis upon contractual prices reflects the growing importance that state authorities came to attach to the principles of merchant autonomy, freedom of contract, and the facilitation of  


58. See David and Brierley, *Major Legal Systems in the World Today* for the foundations of contract law in the different legal systems of the world.
exchange. In Anglo-American legal theory, these principles were ultimately embodied in the will theory of contract. "The autonomy or free choice of private parties to make their own contracts on their own terms was the central feature of contract law....[and] had a profound effect on the functions of contract law as perceived by the courts...[the] primary function [being] facultative."\(^{59}\) The judicial implication of market prices, in cases of disagreement or underspecification, reflects the influence of the principles of market allocation and the sanctity of contract. The willingness of the courts to imply a contract price embodies the belief that they have a duty to enforce bargains arrived at by competent and consenting parties, while the reliance upon current market prices shows their faith in market mechanisms as the proper arbiter of price disputes. The medieval notion that exchange could be measured by some objective standard of fairness, thus drops out of the picture and is replaced with the belief that the value of exchange is a matter of subjective choice.\(^{60}\) Furthermore, the development by the common law courts of rules precluding judicial evaluation of the equivalence of

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60. "The extreme individualism, the belief that all prices are a matter of subjective choice, the stress on the will and intention of the nineteenth century were not found in the law of the eighteenth century to any significant degree. They only really emerged in the late eighteenth century", ibid., p. 167.
exchange or the prudence of bargains, embodied in the doctrine of consideration, came to narrowly circumscribe judicial intervention on grounds of fairness.\footnote{61. The doctrine of consideration did not come from the law merchant, but was developed by the common law. Under the common law, an agreement is unenforceable unless it is contained in a sealed instrument or is supported by valuable consideration. While the origins and evolution of the doctrine of consideration are complex, at the core of the doctrine is the belief that there must be an exchange of value arrived at by way of a bargain in order for a promise to be binding. The doctrine was developed in the late eighteenth century by common law judges. While early statements of the doctrine might suggest that the doctrine was intended to regulate equivalence in exchange, in deference to free market values, the common law adopted the rule that it is not for the courts to enquire into the adequacy of consideration. "A court of equity, for example, should not be permitted to refuse to enforce an agreement for simple 'exorbitancy of price' because 'it is the consent of parties alone, that fixes the price of a thing, without reference to the nature of things themselves, or to their intrinsic value'....'a man is obliged in conscience to perform a contract which he has entered into, although it be a hard one....'" Horowitz quoting Powell, "The Historical Foundations of Modern Contract Law," p. 918. For a fuller discussion of the origins of the doctrine of consideration see Farnsworth, "The Past of Promise: An Historical Introduction to Contract" and Atiyah, \textit{The Rise and Fall of Freedom of Contract}.}

No similar requirement exists in the civil law. While some civil law countries, like France, require the existence of a sufficient \textit{causa} to make a contract valid, this concept is not the same as the common law concept of consideration. The modern doctrine of \textit{causa}, rooted in Roman law, was developed in the seventeenth and eighteenth centuries and came to signify a juridical reason, rationale or purpose for contracting. See Ernest G. Lorenzen, "\textit{Causa and Consideration in the Law of Contracts}," \textit{Yale Law Journal} 28 (May 1919): 621- 46.
of the medieval tradition of substantive justice and the equitable conception of contract.

Modern contract law is fundamentally a creature of the nineteenth century. It arose both in England and America as a reaction to and criticism of the medieval tradition of substantive justice that, surprisingly, had remained a vital part of eighteenth century legal thought, especially in America. Only in the nineteenth century did judges and jurists finally reject the longstanding belief that the justification of contractual obligation is derived from the inherent justice or fairness of exchange. In its place, they asserted for the first time that the source of the obligation of contract is the convergence of the wills of the contracting parties.... [I]n a society in which value came to be regarded as entirely subjective and in which the only basis for assigning value was the concurrence of arbitrary individual desire, principles of substantive justice were inevitably seen as entailing an 'arbitrary and uncertain' standard of value. Substantive justice, according to the earlier view, existed in order to prevent men from using the legal system in order to exploit each other. But where things have no 'intrinsic value,' there can be no substantive measure of exploitation and the parties are, by definition, equal. Modern contract law was thus born staunchly proclaiming that all men are equal because all measures of equality are illusory.\textsuperscript{62}

Whereas the medieval equitable theory of contract limited and defined contractual obligations in terms of the fairness of exchange, under modern contract theory contractual obligation depends upon the convergence of the wills and desires of the individual.\textsuperscript{63} "The role of


\textsuperscript{63} Ibid., p. 923.
contract law was not to assure the equity of agreements but simply to enforce only those willed transactions that parties to a contract believed to be to their mutual advantage."\textsuperscript{64}

The norms for domestic transactions came to be the determination of prices according to the will of individuals bargaining freely in an exchange relationship and the application of current market prices in cases of underspecification.\textsuperscript{65} These norms were evident in both common law and civil law countries, although the zeal with which the common law courts embraced the free market approach\textsuperscript{66} and the peculiarities associated with the common

\textsuperscript{64} \textit{Ibid.}, p. 947.

\textsuperscript{65} Horowitz notes \textit{ibid.}, pp. 952, 946–7 that modern contract theory arose to articulate the will theory of contract, as an expression of the ideology of the market economy in the nineteenth century. "The development of extensive markets at the turn of the century contributed to a substantial erosion of belief in theories of objective value and just price. Markets for future delivery of goods were difficult to explain within a theory of exchange based on giving and receiving equivalents in value. Futures contracts for fungible commodities could only be understood in terms of a fluctuating conception of expected value radically different from the static notion that lay behind contracts for specific goods; a regime of markets and speculation was simply incompatible with a socially imposed standard of value. The rise of a modern law of contract, then, was an outgrowth of an essentially procommercial attack on the theory of objective value which lay at the foundation of the eighteenth century's equitable idea of contract."

\textsuperscript{66} See Atiyah, \textit{The Rise and Fall of Freedom of Contract} for a detailed exploration of the particular influence that liberal political economy had on the bench and bar in England.
law doctrine of consideration, 67 might suggest that the norm was stronger for common law than for civil law jurisdictions.

The rules governing domestic transactions were brought into line with those previously applied only to international transactions. Now, however, the norms of contractual and market prices were premised upon an articulated theory of contract. The will theory of contract was in turn rooted in liberal political and economic theory which emphasized the values of individualism, the efficacy of free markets as regulative institutions, and the facilitative role of legal regulation. The principle of merchant autonomy took on new meaning as a necessary complement to the principles of freedom of contract and the sanctity of agreements. But now merchant autonomy operated, not by virtue of the absence of political authority, but with the sanction and support of state authorities.

(b) Liability for Defective Goods. During the second phase of the regime the breakdown of the dualistic system of regulation was also evident in the norms regulating liability for defective goods. The norm was the application of national standards. In many jurisdictions, standards of strict liability were replaced by limited liability for defective goods.

67. See above note 60.
In common law countries, there was a decline in the priority given to the equity principle as the standard of strict liability for defective goods was replaced by that of limited liability. While quality controls persisted into the seventeenth and eighteenth centuries, the common law developed the rule of caveat emptor or buyer beware. The rule limits the liability of sellers for defective goods to only those instances where the seller provided an express warranty of quality or was guilty of fraud. It is said to be an "ancient maxim of the common law," not traceable in origin to Roman law, ecclesiastical law or to the law merchant.\textsuperscript{68} In England, it first appeared in print in the sixteenth century and gained in acceptance in the seventeenth century.\textsuperscript{69} However, it was only in the eighteenth and nineteenth centuries that it came to be widely applied. As the "apotheosis of nineteenth century individualism," it was consistent with the developing model of contract law which left each party to rely upon his own judgement and imposed no duty to volunteer information to the other.\textsuperscript{70} Caveat emptor was associated with the ideals of the new political economy. The responsibility to inspect

\begin{itemize}
  \item \textsuperscript{68} Hamilton, "The Ancient Maxim Caveat Emptor," pp. 1156-63.
  \item \textsuperscript{69} Ibid., p. 1164.
  \item \textsuperscript{70} Atiyah, \textit{The Rise and Fall of Freedom of Contract}, p. 464.
\end{itemize}
goods for defects was placed upon the purchaser, for it was assumed that prices would be determined accordingly.

...[I]t was assumed that buyers discounted the prices and were prepared to pay to allow for the risk that the commodity they were buying might prove to be defective. If the buyer were given statutory protection for defective goods, as the rationale went, he would be given a bonus for which he hadn’t paid. This theory, or set of ideas, grew up with the new political economy. It differed without doubt from the paternalistic traditions of the eighteenth century judges who felt that a man was entitled to receive fair value from a sale.\textsuperscript{71}

The rule came into prominence in England as the common law courts replaced the law merchant courts and as canon law declined in influence.\textsuperscript{72}

In the United States, the rule was applied with even more vigour. "In the new republic the tradition of authority did not linger long after the war for independence, the intellectual individualism was reinforced by the spirit of the frontier, an emerging industrial system was not to be shackled by formal control, and the courts were quite loath to take up the shock of business friction."\textsuperscript{73} The rule was consistent with prevailing views of free market exchange, for it was felt that in an exchange relationship the purchaser was in the best position to bear

\textsuperscript{71} Ibid., p. 466.

\textsuperscript{72} Chief Justice Lord Mansfield is credited with stating its definitive application. See Horowitz, "The Historical Foundations of Modern Contract Law," p. 945.

\textsuperscript{73} Hamilton, "The Ancient Maxim Caveat Emptor," p. 1178.
the risk of defective goods as he could inspect such goods upon receipt and refuse to accept delivery of substandard goods or guard against loss by negotiating an express warranty of quality.

The laws contrived for the protection of the consumer were repealed or forgotten; the machinery of law enforcement fell into disuse. The matter of the quality of the ware, passed out of the province of government into the economic order. In the market, as the schoolmen of the day were wont to argue, sellers were balanced against buyers, each was in his mercenary methods checked by the competition of others of his kind, and quality even as price was neatly accommodated to individual want.74

Thus the common law countries adopted the norm of limiting the sellers liability for defective goods to a narrow set of circumstances (express warranty and fraud). This norm, embodied in the rule of caveat emptor, reflects the growing influence of the principles of the facilitation of exchange, merchant autonomy, freedom of contract, and market allocation.

In contrast, civil law jurisdictions did not limit liability for latent defects in goods to cases where an express warranty was provided or where fraud was established. For most civil law countries, national commercial codes established rules governing liability for defective goods, carving out a broader scope for liability than under the common law and imposing liability standards

74. Ibid., p. 1183
closer to the strict or absolute liability of the medieval period.\textsuperscript{75}

Further differences have emerged in national approaches to liability for defective goods in the form of different rules governing recoverable damages and notice periods for defective goods claims.\textsuperscript{76}

\textit{(c) Allocation of Transportation Costs and Liabilities:}
During the second phase in the evolution of the regime the norm continued to be the adoption by merchants of uniform standards allocating costs and defining obligations of transportation. This norm reflected the continuing influence of the principles of merchant autonomy, freedom of contract, and the facilitation of exchange. In the earlier part of this phase, merchants devised uniform terms that today are called terms of trade. These terms were utilized in the drafting of transportation and payment documents,

\textsuperscript{75} See Tallon, "Civil Law and Commercial Law."

\textsuperscript{76} The concept of damages in the various national legal systems is not uniform. Some countries focus on the concept of actual damage or loss, while others, like Germany consider damages to be the difference between what the injured party actually received and what would have been received had there been no breach of contract. With regard to the issue of notice for defective goods, German law requires notice only between merchants engaged in international transactions, while American, Swiss, and Scandinavian law require notice of defect for transactions involving domestic transactions as well. See von Caemmerer, "The Influence of the Law of International Trade on the Development and Character of the Commercial Law in the Civil Law Countries," pp. 92–7.
like bills of lading, and became part of merchant custom and practice, enforceable in merchant courts. Later, as the principle of state intervention increased in importance, states came to adopt national laws governing the area. However, many states incorporated these terms of trade into their national legal systems and provided considerable room for merchant choice in the particular arrangements adopted to govern their transport obligations. The norm of state control thus did not severely curtail merchant autonomy and freedom of contract in this area, although national differences began to emerge as states defined and courts interpreted the terms in different ways.

Trade terms constitute an early example of simplification of commercial practices. By reference to shorthand expressions, such as FOB and CIF, merchants could determine the division of important functions, costs and risks between themselves. Thus, trade terms deal with inter alia: transfer of risk; arranging carriage and insurance; export and import licences and duties; packing and marking of goods; nature and type of documents; checking operations and certificates of the quality of the goods; notifications of arrangements made.77

Contracts for the sale of goods "free on board," known as the f.o.b. sale or term, is the oldest trade term and was used originally for carriage by sea.78 The first reported

77. Jan Ramberg, "Incoterms 1980," in Horn and Schmitthoff, eds., The Transnational Law of International Commercial Transactions, p. 138. A variety of trade terms are used today, f.o.b. and c.i.f. being the oldest. For full discussion of the various terms see Berman and Kaufman, "The Law of International Commercial Transactions (Lex Mercatoria)."

78. This term came to be used in land transport as well.
decisions dealing with the term appeared in the early nineteenth century.\textsuperscript{79} Under the f.o.b. term the seller is responsible for the cost of transport and bears the responsibility for the safety of the goods until the point of their passing the ship's rail. Once delivery is complete the risk of loss to the goods and further costs of transport are transferred to the buyer. The f.o.b. term developed to suit the needs of merchants in the late eighteenth and early twentieth centuries, prior to the establishment of regular shipping lines. At that time it was customary for buyers to charter vessels for the transport of their purchasers and to accompany the vessel on the voyage. It thus made sense for the buyer to assume responsibility once the goods were on board. However, with the establishment of regular shipping lines and the development of new forms of finance, the buyer was often not present at the point of delivery and payment was often made at a future date. To meet these new conditions the c.i.f. term was developed, gradually replacing the f.o.b. term as the most commonly used contract in ocean trade.\textsuperscript{80} Under a c.i.f. contract (cost, insurance,
and freight) the seller is responsible for shipping the goods or furnishing the documentation for goods already seaborne and for tendering the documents to the buyer. The documents include a bill of lading, a policy of insurance, covering the goods and an invoice showing the amount due from the buyer. Delivery and transfer of risk is satisfied upon delivery by the seller of the documents and not upon physical delivery of the goods. The price comprises the costs of the goods, insurance, and freight, and the arrangement relieves the purchaser of having to attend to such concerns. The buyer is then obligated to pay the invoice price and bears the costs of discharging the goods at the point of destination.

Differences have emerged, however in how national courts define and interpret the c.i.f. contract. Some courts have held that the contract is "merely a mercantile method of expressing a comprehensive price," while others have held that it is "a contract of strict law entailing definite legal consequences in regard to the passing of risk and title." In addition, American and English courts have differed in the interpretations placed on the word "insurance." The latter have held that what is required is an actual policy of insurance, as defined by the Marine Insurance Act, while the former have held that alternate

insurance arrangements were adequate. Further differences emerged in the interpretation of trade terms as a result of the different national rules governing the passage of risk of loss and title or ownership in the goods. Some countries attach the passing of risk to the conclusion of the contract, some to the passing of property or ownership, and others to the passing of possession. Traditionally, the common law regarded risk to pass when ownership or property in the goods passed to the buyer upon delivery of the goods. As a result, the American Uniform Sales Act placed property and risk on the seller during transit, a position "flatly contrary to the understanding implicit in international c.i.f. contracts." National differences have also emerged over the right of the buyer to examine the goods before


84. Honnold, "The Influence of the Law of International Trade on the Development and Character of English and American Commercial Law," p. 75. And see Trakman, The Law Merchant, pp. 31-2 for a discussion of a similar position adopted by English courts on c.i.f. contracts. Honnold notes at p. 84 that the American position was eventually changed and U.S. treatment of trade terms was brought into line with international practice with the enactment of the Uniform Commercial Code in phase three in the development of the regime.
payment. As we will see when considering the third phase in the evolution of the regime, such national differences generated a movement for the international unification of trade terms.

In addition to utilizing uniform terms of trade, merchants continued to regulate the costs and liabilities of transport according to many of the standards established in the medieval phase. In some cases, national legislation governing matters such as jettison, shipwreck, collision, salvage, and the like generally applied the standards in current commercial usage and thus marked no significant departure from the law merchant. In other cases, however, further national differences emerged. The bill of lading, described as "the most important document in a sale involving carriage by sea," was treated differently under different systems of national law. "The threefold character of the bill of lading, for example, as contract of carriage, receipt for the goods shipped, and document of title, has led to developments sufficiently complex." Under English, French, American, and German law the transfer of a bill of lading gives the holder a title to the document and to the goods. However, the exact rights of the holder (i.e., right

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85. Ibid., p. 75.
86. Ibid., p. 76.
87. But also commonly used for other modes of transport.
to sell or to take an action for possession or actions in

tort) differ in the different systems.\textsuperscript{89} Furthermore, national differences are apparent in the treatment given to attempts to limit the liability of the shipowner under liability limitation clauses in bills of lading. The medieval law merchant adopted the rule of limited liability, whereby liability was contingent on fault. Shipowners were liable for loss or damage to goods due to unavoidable accidents and losses occasioned by common safety. This rule appeared in French codifications, excusing liability in cases of \textit{force majeure} or \textit{cas fortuit}. German law imposed liability only in cases where the loss could not be prevented by ordinary care, while English law "in the grip of historical accidents similar to those which resulted in the doctrine of consideration, had evolved a standard of absolute liability for the shipowner subject only to exceptions entirely English."\textsuperscript{90}

Thus we see that the norm of adopting uniform terms governing transport costs and liabilities weakened somewhat in the second phase in the development of the regime as


\textsuperscript{90} Thayer, "Comparative Law and the Law Merchant," p. 151. O. W. Holmes, \textit{The Common Law} (Boston: Little, Brown, and Company, 1881), pp. 177-205 traces the origin of the strict liability rule to the English law of bailment. He further shows that the exceptions to strict liability, being acts of God or of the public enemy, are also of peculiarly English origin.
national differences in the interpretation of trade terms and bills of lading and in liability standards emerged. At the same time, however, national laws governing other maritime matters like salvage, jettison, collision, and shipwreck retained more uniformity.

(d) Insurance. In the second phase merchants continued to apportion their risks and limit liabilities through a variety of insurance practices. However, states became involved in the regulation of insurance law, reflecting the increasing influence of the principle of state intervention. While insurance contracts were the subject of local intervention and legislative action as early as the fifteenth century, significant state or legislative intervention really only occurred in the seventeenth century. Although legislative intervention and intervention by national courts came to undermine the universality of certain aspects of insurance law,

91. Marine insurance, life insurance and fire insurance comprised the principal forms of insurance prior to the mid-nineteenth century. Marine insurance developed first, while fire insurance became more common in the seventeenth century and life insurance in the eighteenth century. This discussion focuses exclusively upon marine insurance as this is the form of insurance most central to international commercial transactions. For discussion of the other forms of insurance see Clough and Cole, Economic History of Europe, p. 497 and Clough, The Economic Development of Western Civilization, pp. 199-200.

considerable uniformity was retained. This is due to the fact that in many cases states incorporated the law merchant into national law. In addition, the activities of merchants and large insurance companies, who adopted similar standards and practices, contributed to significant uniformity in practices.

In England, while marine insurance had been utilized early in the middle ages, it became highly specialized by the seventeenth century. The first English insurance act was enacted in 1601 at the instance of marine underwriters who were dissatisfied with the ability of the existing courts to adjudicate maritime insurance disputes. Prior to the accession of Lord Mansfield to the bench, insurance disputes were handled by merchant courts and private arbitration. "It was generally understood that the common law courts, which did not recognize the quasi-international customs of merchants, afforded no fit forum for the determination of causes among merchants." 93 However, merchants were unable to enforce the judgments of the merchant courts and private arbitrators and so they turned to the courts of admiralty and common law. These courts too proved inadequate.

...[T]he common law courts of that day, with their highly technical and tedious rules of procedure, as governed by precedents of agricultural rather than mercantile origin, were ill adapted for the settlement of merchant disputes. Thus it appears that at

93. Ibid., p. 111.
the beginning of the seventeenth century persons having insurance causes were without a satisfactory tribunal for their determination. The conventional [merchant] courts could not enforce their judgments, the courts of admiralty had proved inadequate, possibly because of the vexatious jealousy of the common law courts in unreasonably restricting their jurisdiction, while the common law courts were wholly unfit. 94

The Insurance Act of 1601 established a special court of insurance commissioners, comprised of an admiralty judge, civil law and common law lawyers, and merchants, to hear insurance cases. However, the court was not successful due to its limited jurisdiction and it lapsed into disuse by the end of the century. 95 As a result merchants continued to pursue private means to settle insurance disputes. With the accession of Lord Mansfield to the Bench in the eighteenth century, the incorporation of insurance principles from the law merchant into the common law began. "In insurance causes, as with causes involving other branches of the law merchant, he impanelled juries of merchants and underwriters, to establish customs and usages current among those who made insurances, and diligently consulted the time-honored maritime laws of the Continent, and the treatises of English and Continental writers." 96

94. Ibid., p. 113.

95. Its jurisdiction applied only to policies issued in London and to insurance on goods. Only the insured and not underwriters could take actions and its judgments were not a bar to actions in other courts. Ibid., p. 114.

96. Ibid., p. 116.
Mansfield often cited the Sea Laws of Rhodes, the Consolato del Mare of Barcelona, the Laws of Oleron and of Wisby in his decisions. The common law courts adopted the law merchant principles governing sea loans and in 1801 first recognized the right to recover general average contributions at common law. However, national distinctions began to appear. The common law rejected the civilian and law merchant-based rule that repairs to a ship or the provision of necessaries gives rise to an implied maritime lien, while subtle differences began to emerge in the common law rules governing general average contributions. Although the basic norm of contribution to the general average persisted, differences in interpretation and application were sufficient to generate a movement for the unification of the law governing general average contributions in the late nineteenth century.

In England, uniformity in marine insurance law was also facilitated by the actions of private groups of merchants engaged in the insurance business. These merchants developed an institutional framework that facilitated

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99. Ibid., p. 244.

100. See William Tetley, Marine Cargo Claims 2nd ed. (Toronto: Butterworths, 1978), chap. 32 for discussion of different approaches to the general average adopted by common law and civil law jurisdictions.
commercial exchange by providing information on insurance practices and by developing insurance standards. A group of marine underwriters would regularly gather at a coffeehouse run by Edward Lloyd and engage in the practice of underwriting marine risks. Lloyd published the News relating to current developments in shipping matters. It was replaced by Lloyd's List in 1734 and in 1760 the underwriters began to jointly publish Lloyd's Register of Shipping. "From a loose association of men doing business at the same place, the Lloyd's underwriters slowly became a well organized society, with rules, standard policies, high ethical standards, and a marvellous information service. From the mid-eighteenth century to the present, Lloyd's has dominated the field of marine insurance."101 The adoption of standardized contracts of insurance, crystallizing customs and usages, and their widespread use throughout the world contributed to the universalizing of insurance practices.102 In addition, the development of insurance standards and the provision of an information service functioned to lower transaction costs and contributed to greater certainty in transacting.

101. Ibid.

In France, in the seventeenth century, codifications of marine law under Colbert provided "for the regulation of the business of insurance with a completeness of detail that speaks clearly both of the importance of commercial insurance at that time and of the age and extent of practice that could make such detail possible."\(^{103}\) The Marine Ordinances of 1681 were premised upon standards and rules derived from the law merchant. Colbert organized an insurance company in Paris in 1668 and the French came to engage extensively in the marine insurance business, conducting their affairs according to standards established under the law merchant.\(^{104}\)

The norm of adopting uniform standards governing insurance thus weakened somewhat in the second phase in the development of the regime, as differences in national rules emerged. However, the differences did not really challenge the basic principle that risk should be shared and apportioned between the parties to a maritime adventure. The practice of contributing to the general average remained intact, albeit in modified terms under common law and civil law jurisdictions. Furthermore, in spite of increased state regulation, private actors continued to develop customary norms to facilitate the practice of insurance.

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(e) Financing and Credit. During the second phase the norm continued to be the utilization of uniform payment and credit documents and procedures to facilitate sales transactions. Merchants continued to exercise considerable autonomy in the choice of documents utilized to finance sales agreements. Indeed, the development of new techniques that rendered credit instruments more negotiable and therefore easier to use in business provided more choice for merchants and contributed further to the facilitation of exchange.  

All these developments in the use of credit instruments (bills of exchange, notes, etc.) were in the direction of making them more negotiable - that is, easier to transfer from person to person, easier to turn into cash, easier to use in business. Greater negotiability made for greater use of credit and helped merchants and others to do business in distant cities and lands. It caused a great many legal problems about the responsibilities of endorsers, accepters, and others which were settled only slowly in the ensuing centuries. The validity of endorsements by the man to whom a bill was payable was not fully established in Holland till the mid-seventeenth century or in England before the end of the century...

By the eighteenth century the practices of acceptance and endorsement of bills of exchange together with improvements in commercial law had greatly increased their [bills of exchange] negotiability.  

105. The development of the practice of endorsing bills of exchange, the use of accepted bills of exchange, and promissory notes payable to the bearer and the practice of discounting all made credit instruments more transferable. See ibid., pp. 141-2.

106. Ibid., pp. 142, 292.
National legal systems came to recognize the various credit instruments, formerly recognized only under the law merchant, and states became involved in their enforcement. However, national particularisms began to creep into the definition and interpretation of financial instruments and states developed different rules regulating the formalities that had to be met to create and to enforce them. Differences also began to appear in the nature of the obligations generated by various credit instruments.

Uniformity in the rules governing negotiable instruments was significantly undermined from the seventeenth century onward. The "French, the Italians, the English, and the Germans nationalized their commercial law, and developed their own concepts by means of judicial decisions, without paying any attention to decisions in foreign countries. The differences became accentuated in the nineteenth century, giving rise to conflicts of laws which greatly hindered the circulation of bills of exchange." As we shall see in the next chapter, this gave rise to a movement in the late nineteenth and early twentieth century for the unification of the law governing financial and credit instruments.

With regard to bills of exchange, states adopted different conceptual and theoretical foundations regarding the nature of the transaction that gave rise to divergent

legal consequences. French law adopted what is referred to as the 'Mercantile theory,' which is regarded as reflective of the medieval law merchant. According to this theory, a "bill of exchange in its origin was an instrument by which a trade debt, due in one place, was transferred in another. It merely avoided the necessity of transmitting cash from place to place." English case law, in contrast, developed the 'Banking or Currency theory,' "under which bills have developed into a perfectly flexible paper currency," departing from the medieval view. Whereas in France the bill of exchange came to be regarded as a documentary representation of a commercial transaction, in England it functioned as a flexible instrument of credit. The different theoretical foundations for bills of exchange produced different legal consequences for issues concerning the effect of bills payable to the bearer, the possibility of acceptance by a separate instrument, the necessity for


109. Ibid., pp. xlv- xlv.

110. Ibid., p. xlv.

111. See also Thayer, "Comparative Law and the Law Merchant," pp. 149. Thayer notes that German law was rather late in developing a theory of bills of exchange. The theoretical foundations ultimately adopted "went even beyond the English view in building on the conception of a bill of exchange as substantially a unilateral promise addressed to the public."
delivery to complete acceptance, the validity of a provision regarding specific payment in a foreign currency, and the consequences of forgery.\textsuperscript{112} English law, in general, tended towards maximum transferability of bills of exchange, while the French law contained significant limitations on transferability.\textsuperscript{113}

Different conceptions of cheques also emerged. In Anglo-American common law a cheque was considered to be a special form of a bill of exchange and thus subject to similar rules. Under the civil law it was regarded as a separate category and subject to distinct and different rules.\textsuperscript{114}

With regard to letters of credit, the modern letter of credit "was first used in Anglo-American and European trade toward the middle of the nineteenth century and, in less than 100 years, it acquired guiding legal principles which hold true with a remarkable degree of uniformity across the boundaries of nations and legal systems."\textsuperscript{115} While the

\textsuperscript{112} Ibid., pp. 150-1.

\textsuperscript{113} See Chalmers' Digest, pp. xlv-xlvi for specific comparisons of English and French laws regulating bills of exchange.


modern letter of credit bears a likeness to the medieval letter of payment and fair letter, significant differences came to characterize modern letters of credit. More parties became involved in financing sales transactions, which gave rise to greater complexity in the legal incidents of the credit arrangement. As Ellinger notes "in the majority of legal systems, letters of credit have not been the subject of specific legislation. Courts of law are, therefore, able to give full effect to principles concerning letters of credit developed by the mercantile community." However, while the basic features of the credit transaction are treated uniformly, significant differences in national treatment of other aspects became evident as modern techniques developed. This is particularly so with regard of the development of documentary credits in the form of irrevocable letters of credit. Documentary letters of credit were used in the late nineteenth century, but became more important in the twentieth century, and will be considered in the next chapter.

The second phase in the development of the regime also witnessed the disappearance of the prohibition of usury.

116. Ibid., p. 4 and see E. P. Ellinger, Documentary Letters of Credit, chap. 2.


The norm of the widespread practice and legitimacy of interest charges reflects the declining influence of religious notions of equity and the increasing importance attached to the principle of facilitating exchange. As the Reformation and the development of capitalistic business techniques had an impact on the regulation of prices, so too did the same developments change the attitudes towards the charging of interest. However, full play was not given to the market allocation principle and the principle of freedom of contract, for states continued to regulate the rate at which interest could be charged, permitting the charge of moderate rates.  

Some states came to establish different interest rates for international transactions and for domestic transactions, allowing merchants to charge a higher rate of interest for the extension of credit in international transactions than in domestic transactions.

The second phase thus witnessed the continued development of new financial and credit transactions to facilitate exchange. However, there was some weakening in the norm of adopting uniform credit and financial arrangements as national particularisms emerged. This was particularly so regarding the development of different national standards governing the formalities necessary to


create and to enforce binding financial obligations. While the increasing importance of the principle of state intervention is evident in the trend towards national recognition and enforcement of financial transactions formerly enforceable only under the law merchant, the disappearance of the prohibition of usury suggests that the normative content of local or state regulation had changed. The declining influence of canonical notions of equity and the broader acceptance of freedom of contract as regards credit and interest arrangements, suggest a shift away from viewing exchange in distributive terms and towards an emphasis upon the facilitation of exchange.

We will now turn to consider the developments occurring in the procedural dimension of the regime.

2. Procedural Dimension
(a) Locus of Regulation. During the second phase in the evolution of the regime there was little or no recognition of legitimate agents for the creation and enforcement of rules of international application or of broad appeal. The norm was greater state control of commercial matters and the normative influence of merchant custom as a source of uniform law declined. States replaced merchants as the legitimate agents of law creation and enforcement as the law merchant was incorporated into national legal systems and as national legislatures and courts assumed a central role.
The enactment of national commercial laws and codes and the assumption of jurisdiction by national courts became the norm, undermining the primacy previously accorded to merchant autonomy and to merchant custom. The enhanced role of the state in defining and enforcing property rights reflects the growing influence of the principles of state intervention and the enhancement of political autonomy through the achievement of national goals. It also reflects the declining influence of the principle of merchant autonomy. However, while states assumed more of a role in determining the conditions necessary to create and enforce binding commercial obligations, the principle of state intervention admitted exceptions. Merchant autonomy was evident in the latitude accorded merchants in determining much of the substantive content of commercial agreements and in their retention of special status in some national systems. Furthermore, the declining influence of merchant autonomy was not uniform. In some areas, like insurance, merchants continued to exercise considerable control over the development of standards and practices.

While states exercised more authority in establishing formal procedures governing the creation and enforcement of commercial transactions, the competing principles of merchant autonomy, freedom of contract, and reliance on market allocation mechanisms provided the foundation for significant latitude for merchants in defining the substantive content of their agreements. The repeal of
market offences, the disappearance of price regulations and the prohibition of usury, and the declining influence of quality controls broadened the scope of merchant control over the substantive content of all commercial agreements. Issues of price, interest charges, and quality came to be regulated by the free will of the contracting parties in many legal systems. The emphasis placed upon freedom of contract and the removal of restrictions on the market activities of middlemen reflect the belief that commercial exchange is best facilitated by minimizing restrictions on contracting. Furthermore, as we will see in discussing Dispute Settlement, the continuing efficacy of private arbitration suggests that the norm of state enforcement was not absolute.

Although the dualistic system of regulation characterizing the medieval period disappeared as the distinction between the regulation of foreign or wholesale trade and local or retail trade diminished in importance, the decline of merchants as a special class was not uniform. In some states, like England and the United States, merchants did disappear as a special class. For both states the development of a unitary commercial system applying alike to merchants engaged in international transactions and to others engaged in domestic transactions effectively brought to an end the special rights accorded merchants in
the past. 121 This was achieved through the incorporation of merchant law into their national commercial laws and the absorption by their courts of the jurisdiction of the law merchant courts. However, the decline of special merchant status was less pronounced on the Continent. France and, to a lesser extent Germany, continued to recognize special rules for merchants and retained specialized merchant courts and jurisdictions. 122

The period of nationalizing and localizing the law merchant thus evidences significant strengthening of the norm of state control and weakening of the norm of merchant control. However, contrary trends are also evident in the latitude accorded merchants to structure their own agreements and in the special status accorded them under some national legal systems.

This phase also witnessed a change in the nature of state control and intervention. While the paternalistic regulation of prices, quality controls, interest charges, and market offences persisted into the early stages of the period, their disappearance with the advent of laissez-faire theory and the values of economic liberalism signalled a decline in the influence of canonical notions of equity. Furthermore, increased importance was attached to viewing

121. Note, however, that U. S. law did later develop some distinctions between domestic and international transactions under the UCC. See Trakman, The Law Merchant, pp. 35–6.

122. See generally Tallon, "Civil Law and Commercial Law."
the purpose of regulation in terms of the facilitation of exchange, while less importance was attached to the distributive function of exchange.

During this phase the norms regarding the locus of regulation were very weak. Merchants and merchant custom declined in legitimacy as agencies for creating law of international application, although this was less so in the area of insurance. States were simply unable to function as agents for creating international standards for reasons that will become evident as we turn to consider the norms governing the methodology of rule creation.

(b) Methodology of Rule Creation. The norm with regard to the identification of legitimate sources of commercial law during the second phase was the widespread acceptance of national positive law. The decline in the efficacy of custom as a source of law reflected a weakening in the influence of the principles of merchant autonomy, informality, and the facilitation of exchange. The principles of state intervention and the regulation of international commerce to enhance political autonomy were accorded primacy as the law merchant underwent nationalization and localization. The notion of a jus commune disappeared as states focussed on the creation of national commercial law.\(^{123}\)

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123. David and Brierley in Major Legal Systems in the World Today, p. 62 note that this period of codification "engendered an attitude of legal positivism which was
The universities in each country no longer taught anything but the national law. This gave birth to a new and revolutionary concept. Law came to be regarded as a national phenomenon, controlled by politics and bound up with the existence of the state. The idea of common law disappeared. The existence of natural law, its force drawn purely from the idea of justice, and independent of all state-authority, was challenged: and this idea came to seem more moral than legal, even to those remaining faithful to it. In the eyes of international lawyers, private international law itself ceased to be anything but a regulation of international commercial relations by the will of the national legislature in a particular state. It became simply a national system of conflict of laws: its object is, and can only be, to say which national law governs a particular transaction.124

As Berman and Kaufman note, "this was an age not only of nationalism but also of positivism."125 The role of commercial custom declined as states came to regard national legislation and case law to be definitive sources of the law. The "pre-eminence of custom [was] attacked in the West, by philosophy and by lawyers anxious to base law on reason. In the nineteenth century this long struggle terminated. People ceased to believe that wisdom lay in conformity with tradition; they wanted, too, to unify the

further aggravated by nationalist sentiments. Jurists now considered their national law to be the Law. They took refuge in their codes, abandoning the idea that law, as a norm of social conduct, was in essence supranational."


law at the national level, and to increase the certainty considered indispensable in legal relations. Customary law gave way to law based essentially on legislation in the countries of the European Continent, and on judicial decisions in England."\textsuperscript{126}

However, the norm of custom-based regulation weakened differentially among states. National legal systems developed different notions of custom and adopted different criteria governing the efficacy of commercial custom. In England the courts often refused to admit custom into evidence\textsuperscript{127} and imposed demanding criteria for admissibility. Customs had to be shown to be of "ancient" origin, certain, reasonable, continuous, and universally recognized as obligatory.\textsuperscript{128} Furthermore, because custom

\begin{itemize}
  \item \textsuperscript{127} This was enforced with particular vigour when litigants attempted to establish customs that differed from the common law. Chief Justice Cockburn articulated this position in \textit{Goodwin v. Robarts}, L. R. 10 Ex. 337, 357 (1875): "We must by no means be understood as saying that mercantile usage, however extensive, should be allowed to prevail if contrary to positive law, including in the latter such usages as, having been made the subject of legal decision, and having been sanctioned and adopted by the courts, have become by such adoption, part of the common law. To give effect to a usage which involves a defiance or disregard of the law would be obviously contrary to a fundamental principle."
\end{itemize}
cannot override statute law and "because of the rule of precedent...the custom once stated is frozen. It is then up to the party opposing the custom to prove that it no longer exists." Merchant custom thus ceased to provide the flexibility and adaptability evident in the medieval phase. "A narrow sense of positivism was firmly entrenched among English courts. Judges preferred to use strict legal logic at the expense of variable principles of commerce. The formalities of English law thereby overrode the informalities that were associated with business practice." Indeed, the very premises of legal positivism as advanced by Austin, for example, militate against the robust reception of merchant custom. The definition of law as the 'command of a sovereign' leaves no place for customary law.

In the United States, the courts appeared more willing to admit commercial customs at variance with positive law. This tendency became more pronounced in the third phase of the regime under the Uniform Commercial Code, which signalled the adoption of a distinctive theoretical approach to the admissibility of custom. As we shall see in the next


131. See Berman and Kaufman, "The Law of International Commercial Transaction (Lex Mercatoria)," for discussion of specific areas where American courts have been more receptive than English courts to merchant custom. And see Trakman, The Law Merchant, pp. 32- 3.
chapter, American law came to adopt a behavioral as opposed to normative test of custom, signalling a departure from traditional approaches to custom under international law. Traditionally, in order for a practice to constitute a custom under international law, it is necessary that it meet the behavioral test of uniform usage over time and the normative test of *opinio necessitatis ac juris*, the community must consider the custom to be legally binding.\footnote{132}{David, "Sources of Law," p. 101 and see J. Brierley, *The Law of Nations*, p. 59.}

On the Continent, national codifications of commercial law accorded commercial custom different treatment in different jurisdictions. In instances where national commercial codes embodied or articulated commercial custom the parties were strictly bound by custom.\footnote{133}{David, "Sources of Law," p. 100.} In Germany, the law accorded an objective status to customs codified in legislation. Such customs were automatically applicable and admissible, unless they had been expressly excluded by the parties. However, only non-mandatory statements of custom could be subject to express exclusion.\footnote{134}{Tallon, "Civil Law and Commercial Law," p. 16.} In addition, court decisions were regarded as custom when they constituted settled case law.\footnote{135}{David, "Sources of Law," p. 102.} According to one view, in "the absence of judicial decisions it is frequently uncertain whether it has all the characteristics required
for an enforceable legal custom."\textsuperscript{136} This suggests the virtual impossibility under German law of establishing new commercial customs on the basis of commercial usage or under a behavioral test, in the absence of judicial recognition.

In France, there is some suggestion that commercial custom was accorded more significance in that some theorists believe that it may be invoked to vary or to contradict positive law.\textsuperscript{137} French law also came to differentiate between custom, regarded as a binding source of law, and business practices, which have no legal effect except as invoked by the free will of the parties. The latter are admissible upon proof of their general usage by business specialists.\textsuperscript{138}

The decline of custom as a source of law and the identification of national positive law as the legitimate source of law weakened the ability of commercial actors to generate uniform standards.

With regard to the \textit{coordinative strategies} adopted by states in the second phase of the regime, the norm was to regulate international commercial relations through national conflicts of law rules. These rules function to localize transactions with a foreign element in a particular national

\textsuperscript{136} Ibid., p. 102.

\textsuperscript{137} Tallon, "Civil and Commercial Law," p. 38.

\textsuperscript{138} Ibid., pp. 38-9.
system of law. This norm reflects the growing influence of the principles of state intervention and the enhancement of political autonomy. It also reflects the declining efficacy of uniform commercial custom as a method of regulating commercial transactions. Reliance upon national conflicts of law rules underscores the importance states came to attach to the national regulation of international commerce. The belief that all transactions should be subject to the jurisdiction of some national legal system (i.e., the belief that there are no homeless contracts), most commonly one's own state, epitomizes the national approach to regulation and is the legal manifestation of the doctrine of sovereignty.

Thus, according to the nineteenth century point of view, efforts must above all be directed to the field of conflict of laws and jurisdictions. The aim is to decide which national system of law governs a given legal relationship having international elements, to fix, if possible, which national court shall be exclusively competent to take cognizance of it, and, finally, to ensure the international validity of duly executed documents and of foreign judgments delivered in accordance with these principles.139

Each legal system developed its own system of conflicts of law, giving rise to significant differences in the conflicts rules operating to localize commercial transactions. Important differences emerged among and between civil law and common law jurisdictions. Thus, it

was possible that a particular transaction could be localized in one country under one system of conflicts rules, but in another country under a different system of rules. Toward the end of the second phase there were some efforts by states to harmonize national conflicts rules so as to avoid such conflicting results. However, these efforts were undertaken by civilian jurisdictions and did not attract the attention or support of common law jurisdictions. The Hague Conference on Private International Law was the main body that engaged in the harmonization of conflicts rules in the late nineteenth century.  

The first Hague Conference for the harmonization of conflict rules took place in 1893. Only European states were invited; the United Kingdom was invited but did not attend. Membership in the Hague Conference was limited to Continental states until the twentieth century. David notes that obstacles of a "dogmatic nature" inhibited the success of these efforts. "[T]he lawyers from the various countries, delegated by their governments, did not want to abandon, without good reason which was lacking, the positions which their international

140. See generally, ibid., pp. 141-50. Other notable efforts to harmonize conflicts of laws rules were those of Latin and South American states, resulting in the Montevideo Convention of 1889, and the Pan-American Conference that first met in the same year and eventually produced the Code Bustamante in 1928.

[conflicts] systems of law had adopted for doctrinal reasons or sometimes fortuitously.\textsuperscript{142} These early efforts of the Hague Conference did produce some results, but it was only in the twentieth century that significant efforts were made to unify substantive rules of commercial law. These developments will be considered in the next chapter.\textsuperscript{143}

Thus with regard to the methodology of law creation, the second phase in the development of the regime exhibits considerable weakness. The declining normative significance of custom as a source of law, the increasing importance of positive national law, and the regulation of international commercial relations through national systems of conflicts of laws rules became the norms. These developments are consistent with the central position occupied by the state and concerns of national sovereignty. States came to apply national solutions to international commercial relations, leading one authority to conclude that "\textit{[O]ne has to be a lawyer not to notice that the modern world holds in derision the national systems of conflicts of laws, which usually result in the national law (\textit{lex fori}) being applied, and which are pompously baptized private international law.}"\textsuperscript{144}

\textsuperscript{142.} "The International Unification of Private Law," p. 142.

\textsuperscript{143.} See \textit{ibid.}, pp. 145-6 for a list of conventions produced by the Hague Conference in the twentieth century.

\textsuperscript{144.} \textit{Ibid.}, p. 209. Conflicts of law are also referred to as 'private international law.' However, the latter term is a misnomer for it obscures the fact that it is national law and not international law that is applied under the conflicts rules.
During this phase, there was little or no support for methods of law creation capable of generating standards of broad or near universal appeal and application. The ability of merchants to do so was undermined by the declining influence of merchant custom, while states' concerns with national sovereignty and their preoccupation with developing nationally-based conflicts of law rules prevented their development of international standards and rules.

(c) Dispute Settlement. During the second phase the norm was the acceptance of state offices for the settlement of disputes and the enforcement of commercial agreements. Reliance on private arbitration and self-enforcement by merchants declined as the principles of national adjudication and state intervention increased in importance. However, as we shall see, this decline was not uniform among states.

During this period, the geographic expansion of commercial relations rendered the self-enforcement system of merchants less successful and more costly. The collection of information regarding the credit-worthiness and honesty of merchants became more expensive. The sanctions of market exclusion and loss of reputation became difficult to enforce as markets proliferated in number, as commerce extended to far away places, and as the practice of simultaneous
exchange in markets was replaced by non-simultaneous exchanges over time and space.

The Law Merchant system of judges and reputations was eventually replaced by a system of state enforcement, typically in the late middle ages or the early modern era in Western Europe. Enforcement of the private codes by the state added a new dimension to enforcement, especially in later periods when nation states exercised extensive geographic control. Rather than depend for punishment upon the decentralized behavior of merchants, state enforcement could seize the property of individuals who resisted paying judgments, or put them into jail. If judgments could be enforced this way, then, in principle, the costs of keeping merchants well informed about one another's past behavior could be saved.... As the volume of trade increased in the late middle ages, the cost saving from that source [state enforcement] would have been substantial.... [T]he importance of the role of the state enforcement of contracts.... was to reduce the transaction costs of policing exchange. 145

The imposition of the sanction of bankruptcy and the enforcement of agreements became the prerogatives of states and thus contingent upon national intervention as states adopted laws and procedures governing the enforcement and execution of commercial agreements. Effective enforcement, thus, lay with the state.

The trend towards increasing reliance upon national adjudication and enforcement was reinforced by the incorporation of the jurisdiction of merchant courts into national judicial systems. However, as discussed earlier, states differed in the extent to which national courts

assumed jurisdiction over commercial matters. England and the United States adopted unitary systems, wherein the national courts assumed jurisdiction for most commercial matters. The specialized merchant courts disappeared, with the exception in England of the Admiralty Court, whose jurisdiction had been severely limited by the common law courts,\textsuperscript{146} and the rather unsuccessful Commercial Court.\textsuperscript{147}

In France, special commercial courts and commercial jurisdictions were retained. Tallon notes that "these courts have retained the greatest importance. Some merchants consider them to be an essential element of their status as merchants. Despite all the criticism directed towards them they have survived a succession of reforms of the judicial organization in France."\textsuperscript{148} The commercial courts are independent of the regular courts and operate under special rules of procedure. Merchant judges are elected by merchants and business corporations.

\textsuperscript{146} See generally, Mears, "The History of the Admiralty Jurisdiction" and Holdsworth, "The Development of the Law Merchant and its Courts."

\textsuperscript{147} While the Commercial Court was created in 1895 and recognized in 1970 by the Administration of Justice Act as a specialized division of the Queen's Bench of the High Court, it does not operate as an independent court with a separate fixed jurisdiction and has not been very successful. See Tallon, "Civil Law and Commercial Law," pp. 51-2 and see Kilmuir Devlin, "The Future of the Commercial Court," \textit{Journal of Business Law} (1961): 8-11 and Lord McNair, "A Note on the History of the Commercial Court," \textit{Law Quarterly Review} 86 (1970): 313-17.

\textsuperscript{148} \textit{Ibid.}, p. 139.
In Germany, the jurisdiction of the merchant courts was assumed by the national courts, however jurisdiction was retained in a special division for handling commercial matters. The commercial chamber comprises an ordinary civil judge and two commercial judges appointed upon recommendations of business organizations.

While states expanded their controls over dispute settlement, the adjudication principle did not completely displace the arbitration principle. The norm of state adjudication and enforcement was not absolute, as reliance on private arbitration persisted, albeit in a less comprehensive manner and in some cases with the assistance of state offices. Indeed, for some states, particularly England and the United States, the sanction of market exclusion continued to be utilized by private trade associations to discipline the actions of their members and merchants turned to private arbitration when the national court systems were unable to settle disputes in an expeditious and satisfactory manner.\(^{149}\) In England, for example, for some time insurance disputes continued to be settled in private arbitrations due to dissatisfaction with the abilities of the common law courts.\(^{150}\) The practice of

\(^{149}\) Jones in "An Inquiry into the History of the Adjudication of Mercantile Disputes in Great Britain and the United States," shows that merchants continued to utilize private arbitration during the period of the nationalization and localization of the law merchant.

private arbitration persisted and came to be bolstered by state intervention in the form of legislation providing for the enforcement of arbitration agreements.\textsuperscript{151} Jones observes that by the end of the nineteenth century in England it was estimated that "almost all mercantile cases, even those that eventually came to the courts, went to arbitration. Exchanges such as the Liverpool Cotton Exchange, the London Stock Exchange, the London Corn Trade Association, and the Coffee Trade Association, had machinery for arbitration."\textsuperscript{152}

In the United States, private arbitration continued to be the norm until the end of the eighteenth century.

\begin{quote}
Merchants avoided government courts because those tribunals did not apply commercial law in a just, and inexpensive fashion. Furthermore, public courts did not accept new commercial practices rapidly enough. Indeed, it was not until the end of the eighteenth century that public judges began to convince merchants that they could understand complex business issues and practices, and that they accepted as law, agreements established to facilitate the reciprocal self-interest motives of traders. Once government courts began to apply the merchants' law as the merchants had established it, without delay, the commercial arbitration system began to disappear.\textsuperscript{153}
\end{quote}

\textsuperscript{151} In England the Arbitration Act was enacted in 1697 providing for the enforcement of arbitration awards. It was amended in 1889 to provide for the enforcement of agreements to arbitrate future disputes.

\textsuperscript{152} "The Adjudication of Mercantile Disputes," p. 462.

Courts in the United States came to regularly invalidate arbitration clauses and agreements, evidencing considerable judicial hostility to the practice of arbitration. In England courts deemed arbitration agreements to be against public policy because they ousted the jurisdiction of the courts and the guarantees of procedural justice afforded only in courts of law. The practice of private arbitration in the United States became common again at the end of the nineteenth century as a reaction to intrusive state intervention. A change in judicial attitude resulted from the adoption of national policies and legislation more hospitable to arbitration. Exchanges and mercantile associations proliferated at this time, providing arbitration facilities for their members. The New York Chamber of Commerce and a number of other exchanges established in New York, Chicago, St. Louis, Philadelphia, Kansas, Milwaukee, and other places provided for compulsory arbitration for their members.


157. These include the New York Stock, Produce, Mercantile, Cotton and Coffee and Sugar Exchanges, the Chicago Board of Trade, the St. Louis Merchants Exchange, the
associations were formed towards the end of the nineteenth century, providing for the arbitration of disputes. Legislation was passed in New York in 1791 providing for the enforcement of arbitration agreements and awards. In England, as well, judicial hostility toward arbitration began to weaken as national arbitration legislation was enacted. Jones concludes that in England and the United States in the nineteenth century "there was a development of private mercantile tribunals in which the bulk of mercantile disputes was settled entirely outside the state judicial system. The indications are that this trend has continued and exists today in a strengthened form." 

In France, judicial attitudes toward arbitration exhibited similar hostility, but later underwent similar revision.

Thus we see that in the second phase the norms of private arbitration and enforcement weakened. National adjudication and enforcement became more common. However, as norms they were only moderately strong, given the


158. The Grain and Feed Dealers Association, the National Hay Association, the National Cotton Seed Products Association and the American Seed Trade Association. Ibid., pp. 462–3.


160. Ibid., p. 463.

161. Ibid., pp. 53–7.
continuing and increasing recourse to private arbitration in some jurisdictions. Moreover, the connection between private arbitration and national adjudication and enforcement became more complex. While private trade associations may have been capable of enforcing arbitral awards against their members, their ability to police the activities of non-members was questionable. The discipline of non-members could only be achieved through court proceedings. The hostility that national courts had for arbitration, until they were forced to change in response to legislative enactments, and the proclivity of judicial authorities to intervene in arbitration proceedings and to set aside arbitral awards weakened the efficacy of private arbitration. Furthermore, the enforcement of foreign awards and awards of other arbitration tribunals remained problematic. It became apparent in the third phase of the regime that mechanisms were necessary to facilitate the recognition and enforcement of foreign arbitral awards. The state thus came to be intimately involved in the practice of arbitration by recognizing and enforcing arbitration agreements and awards, both foreign and domestic. Furthermore, national differences emerged in the treatment and status accorded private arbitration by various legal systems. The procedures and rules adopted by American and English arbitration laws generated a movement for the unification of arbitration law in the third phase.
B. Summary

This review of the second phase in the evolution of the regime shows that states came to assume a central role in the regulation of international commercial relations. State authority replaced the overlapping authority structures of the medieval period. The dualistic system of regulation characteristic of the medieval phase was in many jurisdictions replaced by unitary systems of state control. Furthermore, states exercised stronger and more comprehensive control than did the local religious and political authorities of the earlier phase.

In the early part of this period, the advent of capitalism, the expansion of trade through colonization, and the development of mercantilist doctrine brought new insights into the role of commerce in determining national power. Political authorities developed a new understanding of the importance of regulating international commerce for achieving national welfare goals and political autonomy. This understanding, coupled with the development of the institutional and legal machinery capable of disciplining international transactions, rendered states more willing and more able to regulate international trade. State controls extended to most areas of international commercial activity, although the decline of merchant autonomy varied from jurisdiction to jurisdiction.
However, while states exercised greater control, the nature of authoritative intervention changed. One of the most profound changes was the replacement of medieval paternalism and religious restraints with a more permissive and facilitative approach. This approach had its origins in liberal political economy, which appeared later in the period. Liberal political and economic thought sanctioned capitalist business techniques and provided a normative and a theoretical rationale for free market principles. England, as the birthplace of the new political economy, and as a leading commercial power, played an instrumental role in developing the free market principles that were to form the foundation for contract law in the common law world and beyond.

With regard to the substantive dimension of the regime, the weakening and disappearance of price and quality controls, market offences, and the prohibition of usury evidences the declining influence of canonical notions of equity. The widespread acceptance and legitimacy of prices as established under freedom of contract or by the market, the weakening influence of strict liability standards for defective goods, and the growing legitimacy of interest charges show the increased importance of free market principles and the value of facilitating exchange.

At the same time, however, state intervention served to weaken the uniformity of regime norms and rules. Significant national differences arose in sales law and the
norm of contractual and market prices was enforced more rigorously in common law jurisdictions than in civil law jurisdictions. Different national rules came to govern liability for defective goods. Common law jurisdictions, unlike civil law jurisdictions, adopted significant limits to liability for defective goods. While the basic principles informing transportation, insurance, and financial transactions remained uniform, national differences regarding their specific nature and character, as well as their legal incidents began to emerge. National differences appeared in the legal interpretation and effect of trade terms, bills of lading, and liability standards in transportation. In the area of maritime insurance, national distinctions became evident, particularly as regards maritime liens and general average contributions. With regard to financial and credit transactions, while states adopted similar instruments, like bills of exchange and letters of credit, differences appeared in national interpretations of their nature and legal consequences.

With regard to the procedural dimension of the regime, the review shows the weakening of secondary rules or rules of recognition governing the creation, modification, and extinction of international commercial law. The state became the legitimate agent for law creation and enforcement. National positive law replaced merchant custom as the primary source of commercial regulation. National positive law systems produced less flexible and adaptable
standards and procedures and were incapable of generating standards of international application. Furthermore, national differences in the effect given to commercial custom became evident. The weakening of uniform practice as the appropriate coordinative strategy and the adoption of nationally-based and insular conflicts of laws rules further entrenched the position of the nation state. Finally, differential weakening in the norm of private arbitration and the growing strength of national adjudication and enforcement reinforced national controls and national particularisms. These developments were consistent with the acceptance of national sovereignty and political autonomy as the fundamental ordering principles in international relations. Legal positivism articulated these principles by elevating positive law over custom as the major source of law and by generating nationally-based conflicts of law systems to regulate international transactions.

Many of these developments generated efforts in the third phase of the regime to regain the universality and distinctiveness of the medieval law merchant and to reassert merchant autonomy, with a view to further facilitating commercial exchange.
CHAPTER VI


The third phase in the evolution of the regime is witnessing a revival of the medieval internationalism of the first phase. The decline in the universality of the law merchant, caused by the proliferation of national differences in the period of nationalisation, has generated efforts to unify international commercial law. The unification movement seeks to recreate the tradition of jus commune, which disappeared as international commercial law was assimilated by national legal systems.

The legal process in general was characterised in the nineteenth century by a disappearance of the traditional jus commune which had developed in the field of international commercial law over centuries; the engine behind this process was the drive toward the nationalisation of the law, an outcome of converging political, philosophical and cultural developments dominant in this period. This nationalisation of international commercial law has in its core been preserved ever since, and the past and current efforts at unification by international agencies may, in the historical context, be seen as attempts to modify, in a limited manner, the adverse affects which the extreme emphasis upon national laws in international commercial legal relations has had upon the flow of trade between states.

The unification movement has made significant progress in restoring the universality of international commercial law and practice. Indeed, it has been observed that "we are discovering the international horizon" in commercial law and furnishing the basis for "the first common law of the world."\(^2\) "It may be said without exaggeration that the revitalization of the ancient lex mercatoria in the process of creating a new uniform commercial code for world trade should be recognized as a major accomplishment in this century."\(^3\)

Unification efforts are reasserting many of the values embodied in the medieval law merchant. In addition, renewed emphasis is being placed on the primacy of liberal, capitalist values. Proponents of the new law merchant, predominantly representatives of Western industrialized states, stress the self-regulating abilities and capacities of merchants.\(^4\) In asserting either explicitly or implicitly

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that the purpose of commercial regulation is to facilitate international economic exchange, they believe that the best way to achieve efficiency and certainty is to give maximum play to the principles of merchant autonomy, freedom of contract, and arbitration and to recognize the critical role played by commercial custom.

What merchants do in international trade is the result of what they have learned to do, what other merchants in similar positions have done in the past and what merchants should continue to do in the future in the interests of economic survival and the just allocation of resources. The legal regulation of such business activity can only truly advance when the law reflects upon, indeed embodies, merchant values. To create law in disregard of the context in which international commerce operates is to deplete the self-sufficiency of the merchant regime; it is to create a legal system in a vacuum at the expense of the practical necessities of business.

Freedom to transact is a necessary component in the evolution of international business. Merchants engaged in world trade do have the facilities to overcome trade barriers threatening their business affairs. Commercial practices facilitate their daily enterprises. Trade conventions delineate the permissibility of their business habits; while customs codify their trade adventures.\(^5\)

While recognizing the legitimate interests that states have in regulating international commercial activities, they emphasize that such regulation should be permissive, suppletive, and facilitative. While national public policy concerns establish mandatory limits to freedom of contract, such limits should be sensitive to the international

dimension of transactions and the furtherance of international comity. Moreover, as mandatory rules, they should be recognized as "exceptions from and restrictions of the general principle which is still that of freedom of contracting, i. e., optional law." Proponents emphasize the ability of merchants to manage their own affairs under 'self-regulating' contracts that establish the rights, obligations, and remedies of the parties and designate the applicable law and dispute settlement procedures.

Freedom of contract is a delegation by the state to individuals of the power to enter


"The age of independence, or even interdependence, has already gone and we are now in the age of interpenetration, where national boundaries lose their meaning. For a global legal order to be established to govern business transactions 'ignorant' of national boundaries, such a legal order must first free the business world from the dogmas that heretofore have shaped the traditional local orders. This is a road for the restoration of lex mercatoria, in the same manner as it existed in the medieval age, at a global dimension in relation to the so-called 'international' transactions."


into binding contracts. In exercising this power, parties are free to define their contractual relationship subject to certain limits and procedures. An expanded use of this power in international transactions is essential to the development of a non-national New Lex Mercatoria because it permits parties to enter into self-regulatory contracts and determine their disputes by arbitration.9

However, the primacy accorded to the principles of the facilitation of exchange, merchant autonomy, freedom of contract, arbitration, and the renewed emphasis upon merchant custom are being challenged by those asserting the primacy of equity concerns. Reflecting the belief that commercial law exercises a distributive function by promoting fairness and equality in exchange and by protecting weaker parties, others have sought to limit the laissez-faire approach. Critics argue that unrestricted reliance upon merchant autonomy and freedom of contract are unacceptable foundations for the unification of commercial law.

Many vital questions are at stake, ranging from the reconciliation of common and continental law to the protection of the weaker party and the satisfactory regulation of transactions between parties from different social and economic systems or from developed and underdeveloped countries, and it would be irrational madness to leave the legal responses to these problems to an uncontrolled laissez-faire in a world in perpetual strife. It is a fact that the economic and political matters involved in international trade transactions considerably exceed the narrow margins of private

interests which are often - and mistakenly - understood to be only concerns in the private law regulation of international commercial issues.  

It is argued that merchant autonomy "tends to annihilate freedom of contract" and does not guarantee a fair result, particularly for weaker parties, like the less developed countries. As we shall see in reviewing the substantive dimension of the regime, there have been attempts to revive the equity principle as the foundation for the determination of prices and for the rules governing liability for defective goods. States have enacted mandatory domestic consumer protection legislation and have been unwilling to submit to international standards. There has been an attempt to infuse the rules governing transportation costs and liabilities with equity concerns as well. In the procedural dimension, equitable considerations have been asserted with regard to the locus of regulation and the methodology of rule creation. Such efforts also reflect the belief that the furtherance of national policy concerns is a fundamental principle of commercial regulation.

However, before turning to the substantive and procedural dimensions, it will be useful to briefly review


the motivations for and the early history of the unification movement.

A. The Movement for the Unification of Private International Trade Law

We saw in the last chapter that as the law merchant was incorporated into domestic systems of law, national differences emerged in the substantive law governing international commercial transactions. In addition, states developed complex conflicts of laws rules which function to localize or fix transactions of an international nature in one national system of law. Differences also emerged in these national systems of conflicts rules. Dissatisfaction with the proliferation of different national standards generated a movement for the unification of commercial law. Practical reasons are most commonly cited as providing the inspiration and motivation for the movement.\(^\text{12}\) The general presumption is that greater trade will result as a consequence of removing barriers to trade generated by legal uncertainties.\(^\text{13}\) The unpredictability, inconvenience, and

\(^{12}\) David in "The Movement in Favour of the Unification of Private Law," p. 123 notes that the nineteenth century movement for the unification of private law was inspired by practical concerns and by a desire to return to a more universal conception of the law, lost with the disappearance of the *jus commune*.

costs generated by uncertainty as to the legal standards that will be applied under different national systems of commercial and conflict laws are most commonly cited as the practical reasons for unification.\textsuperscript{14} Unification of commercial law is regarded as contributing to reduction of the costs of doing business.

Non-uniformity of substantive legal rules imposes transaction costs on businesses engaged in international trade. A business that wishes to know if it has entered into an enforceable contract with a foreign trading partner, for example, must first go through a choice-of-law analysis [i.e., conflicts of law analysis] to determine which country's laws govern contract formation. The business must then construe the applicable substantive legal rules, which well may be the rules of a foreign legal system. Both steps in this analysis are difficult and may involve greater risk of error than is present in a purely domestic transaction.

To reduce these transaction costs one could unify either the choice-of-law rules [conflicts rules] or the substantive legal rules themselves.\textsuperscript{15}

The earliest modern unification efforts were undertaken in the late nineteenth century by private trade associations, like the Hamburg Bourse for Corn Traders, the Bremen Cotton Bourse, the Silk Association of America, and the London Corn Trade Association. These associations "were


aim of establishing norms to be adopted voluntarily by all members." At about the same time the International Law Association and the Institut de Droit International were founded for the purpose of unifying private and public international law. The International Maritime Committee, also a private body, was created in 1896 for the purpose of unifying private maritime law, while later, in the twentieth century, the International Chamber of Commerce was founded as a private French association of national chambers of commerce and engaged in a number of projects aimed at unifying international commercial law.

Governments became involved in the unification movement late in the nineteenth century, primarily through the Hague Conference on Private International Law, which as noted in the last chapter, focussed primarily on the unification of conflict rules. Indeed, early unification efforts were directed primarily at harmonizing conflicts of laws rules. Only later did states attempt to unify substantive commercial laws. The Economic Committee of the League of Nations in the inter-War period undertook the unification of


17. The International Law Association is a private association founded in 1873. Its original title was 'The institution for the reform and codification of the *jus gentium,*' but it was changed in 1895 to reflect its involvement in private as well as public international law. See David, "The Movement in Favour of the Unification of Private Law," pp. 151-2.

limited commercial law subjects, mainly dealing with financial and credit transactions, while the International Institute for the Unification of Private Law (UNIDROIT) was formed in 1926 within the framework of the League of Nations and engaged in the unification of certain areas of commercial law. However, significant global intergovernmental involvement in the unification of commercial law really only occurred after the Second World War. Indeed, one of the distinguishing characteristics of the modern law merchant is the proliferation of intergovernmental agencies, representing most economic and legal systems of the world, involved in the unification of commercial law. While more will be said about these agencies when we consider the Locus of Regulation, it is important to consider the context in which global intergovernmental cooperation emerged.

An important limitation to the success of early unification efforts was their regional character. The Hague Conference on Private International Law and UNIDROIT were for some time limited in membership to European states and to those who shared the civil law tradition. As a result, their early unification projects were not greeted with much enthusiasm by common law jurisdictions. The United States, for example, only became involved in both organizations in the 1960s. Due to the essentially European and civilian nature of their unification efforts, their texts and conventions did not receive broad acceptance outside Europe.
Common law states, less developed states and states with centrally planned economies objected that their interests and legal systems were not adequately represented.

The creation of the United Nations and its network of specialized agencies after the Second World War provided the first truly global institutional context for the unification movement. The mandate of the U. N. General Assembly includes the unification of commercial law under its duties regarding the progressive development and codification of international law (art. 13) and under its competence to promote international economic cooperation (art. 13, no. 1(b)). The General Assembly established a number of bodies and specialized agencies engaged directly or indirectly in the unification of commercial law. The International Maritime Organization (IMO), created as a specialized agency in 1948 but entering into force in 1958, has engaged in a number of projects unifying private maritime law. The United Nations Conference on Trade and Development (UNCTAD) was created as an organ of the General Assembly in 1964 and has engaged in a number of projects involving the unification of law, as too has UNIDO, which was established in 1966 as an organ of the General Assembly and acquired status as a specialized agency in 1983.

The main global forum for the unification of commercial law, however, was provided with the creation of the United Nations Commission on International Trade Law (UNCITRAL) in 1966. UNCITRAL was given a mandate to "further the
progressive harmonization and unification of the law of international trade."19 This mandate includes, among other undertakings, the preparation or promotion of international conventions, model laws and uniform laws, and the promotion of codification and wider acceptance of international trade terms, customs, and practices. UNCITRAL was created in response to observations made by Clive Schmitthoff, regarded as the 'conceptual father' of UNCITRAL,20 in a report to the General Assembly concerning a lack of coordination among organizations engaged in the unification of trade law.21 He further observed that unification efforts failed to achieve universal application due to the lack of participation of the developing and centrally planned economies and to the European and civil law basis of earlier unification efforts. UNCITRAL was thus created with a view to representing "the principal economic and legal systems of the world, and of the developed and developing countries."22 Membership in


22. General Assembly Resolution 2205 (21).
the organization is designed to represent all major legal systems in the world and states of various levels of development, including both planned and market economies. The success of UNCITRAL in promulgating widely adopted texts and conventions unifying commercial law can be attributed to its ability to accommodate a variety of different interests and to arrive at acceptable compromises between often incompatible legal rules.

More importantly, however, the creation of UNCITRAL marked the real beginnings of the involvement of the United States in the unification movement. Indeed, the United States has become a leader in the unification movement and today exercises considerable influence over the nature and content of regime standards. Prior to the creation of UNCITRAL the attitude of the United States was "one of indifference towards all efforts at international cooperation in private commercial matters." 23 This indifference was born out of a preference for judge-made or common law, ignorance of the civil law, and the belief that civilian efforts at unification could not accommodate common law concepts and theories. In addition, the perception that the unification of private law was unnecessary and the existence of limitations on the treaty-making power of the executive in matters of private law posed further obstacles

to the cooperation of the United States. However, the success of domestic unification efforts under the Uniform Commercial Code generated a change in attitude regarding the merits of unifying commercial law. In 1963 Congress authorized the United States to join international organizations engaged in the harmonization and unification of private law and membership in the Hague Conference and UNIDROIT followed. This was a response to the recognition of the tremendous increase in the volume of trade and commerce and the concern that unification efforts in Europe would proceed with or without the participation of the United States. As one Commissioner on Uniform State Laws said in a statement before Congress "[w]e must enter into the problems of great unification in fields of law touching social intercourse and business activity at a time when we can get the viewpoint of the United States heard in the original drafting, not at the time it is considered for final adoption. It is in the preparatory stages that there is an opportunity to weave into it the basic problems that we face in the United States and upon which the commissioners [on Uniform State Laws] have been working for

24. Ibid.

years." 26 In addition, with the creation of UNCITRAL and the adoption of a programme of work that included significant areas of commercial law, the United States was prompted to reassess its attitude towards international unification. Concern was expressed that if American representatives did not take the work of UNCITRAL seriously, they would be faced with the development of standards that were unrepresentative of their interests. 27 The United States thus began participating in UNCITRAL in earnest, adopting a leadership role. Other states, including Great Britain and Canada, also began to take a greater interest in the unification movement with the creation of UNCITRAL.

While significant practical considerations generated by conflicting systems of commercial law underlie UNCITRAL's unification projects, other influences have also been significant. As part of the post-War growth of multilateral international organizations, it was thought that the creation of a truly global organization facilitating international cooperation in commercial matters would contribute to international peace and stability. 28


27. As we shall see later, this prompted U.S. participation in the unification of sales law.

Furthermore, UNCITRAL was formed at a time when the developing countries were first articulating demands for the creation of a New International Economic Order and the formulation of economic regimes more sensitive to their development concerns. At the same time, the governments of centrally planned economies were beginning to assert the need for the commercial regime to accommodate their special concerns. As we shall see in turning to the substantive and procedural dimensions of the regime, these demands have created or revived tensions between conflicting regime principles. In some cases, the tensions have been resolved by changing the rules, creating new norms of commercial behaviour. In other cases, however, the tensions persist and pose a continuing challenge to the formulation of universally acceptable commercial standards.

1. Substantive Dimension

(a) Prices. The norm in the third phase of the regime continues to be the establishment of prices by contract and, in cases of underspecification, by market prices. These norms are embodied in the United Nations Convention on Contracts for the International Sale of Goods (Vienna Sales
Convention) promulgated by UNCITRAL in 1980 and which came into force in 1988.\(^{29}\)

The conclusion of the Vienna Sales Convention marked the culmination of efforts to unify international sales law extending over a fifty year period. Preparation of a uniform sales law began in 1930 under the auspices of UNIDROIT.\(^{30}\) Work was interrupted during the War but later resumed and resulted in the adoption at the Hague Sales Conference in 1964 of two sales conventions.\(^{31}\) However, the Conventions were not widely adopted outside Europe. Of the twenty-seven original signatories, twenty-two were European. The United States began participating after most of the work had been done and was therefore unable to accomplish significant changes. As a result, there was little interest in becoming party to the Conventions which were regarded as embodying civil law sales rules that were unsuitable for a common law jurisdiction.\(^{32}\) Neither were the Conventions


adopted by developing states and socialist states, which on the whole did not participate in the drafting of the Conventions. While the Conventions entered into force in 1972, their adherents were primarily Western European.

This regional character gives us a significant message. In preparing this uniform law, there was negligible input from the common law world, and no significant participation from North or South America, Eastern Europe, Africa or Asia; the uniform law was a distinguished and sophisticated product of Western European legal science. However, the lack of participation by most of the world stood in the way of world-wide adherence. The problem was not merely psychological - a lack of a feeling of paternity. The lack of world-wide participation also produced technical problems.33

The experience of the United States as "Johnnies-come-lately" at the 1964 Hague Sales Conference and the resulting inability to significantly adapt the civilian-based sales regime to the needs of common law sales prompted the United States to take an early and a leading role in the drafting of the Vienna Sales Convention.34 In fact John Honnold, one of the U. S. representatives to the 1980 Vienna Sales

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Conference, was head of the UNCITRAL Secretariat during the drafting of the convention, while Allan Farnsworth served as a U. S. representative to the conference and to UNCITRAL and served on the working group engaged in unifying sales law.\textsuperscript{35} The extent of U. S. influence led Honnold to conclude that "the 1980 Sales Convention bears a much closer resemblance to the UCC [U. S. Uniform Commercial Code] than to any other legal system."\textsuperscript{36}

While the creation of UNCITRAL addressed the need for world-wide participation in the unification of sales law, this did not relieve the tension posed by technical problems generated by different common and civil law concepts and traditions. Nor did it reduce the tensions between the developed and developing countries and between planned and free market economies. These tensions were evident in the disputes over the rules governing prices.

The Vienna Sales Convention embodies the principles of freedom of contract and merchant autonomy in that the parties are free to determine the price of the goods sold under the contract of sale (art. 85). Where the tensions arose, however, was in the determination of prices in cases


of underspecification. Some countries, like the United States, wanted minimum regulation of price specificity and supported the enforceability of "open price" contracts. It was feared that predetermined prices would inhibit a seller's ability to raise prices in response to changing market conditions and thereby extend undue benefits to purchasers under contracts for long-term supplies. In contrast, developing countries, socialist countries and some civil law countries, like France, objected to a rule premised upon open prices.

Socialist countries objected to the conclusion of contracts with open price terms, because the parties are expected to conform their contracts to a predetermined macroeconomic governmental plan. This view makes sense in a planned economy, in which contracts with open price terms are a nullity from the perspective of the superintending state planning agency. Also in some civil law systems contracts of sale with open price terms are viewed with hostility, particularly when the unilateral fixing of the price works to the disadvantage of the weaker party. It was also argued at the Vienna Conference that contracts with open price terms do not serve the interests of the developing countries as a result of the unfavorable terms of trade for raw materials, in contrast with the ever-increasing price of manufactured goods. In contrast, the policy prevailing in the United States on this matter encourages the conclusion of sales contracts for long-term supplies, leaving the price and the quantity of goods open to be adjusted in light of the sellers' output and buyers' requirements. 37

In the case of developing countries it was feared that prices under open price contracts would ultimately be determined by courts in developed countries which would impose high prices for manufactured goods. "Such contract prices would tend to be the sellers' prices and, as is well known, while the prices of the raw materials exported by the developing countries are generally fixed in the commodity markets of the developed world, the prices of manufactured goods are usually determined by the manufacturers themselves." 38

The Vienna Sales Convention embodies a compromise, not a consensus. 39 Furthermore, it is a compromise that gives rise to conflicting interpretations. Article 14 provides, inter alia, that enforceable offers of sale must be "sufficiently definite." Sufficiently definite is defined as a proposal that indicates the goods to be sold "and


expressly or implicitly fixes or makes provision for determining the quality and the price." This provision suggests that open price contracts are unenforceable. However, article 55 was included by way of a compromise and provides the following:

Where a contract has been validly concluded but does not expressly or implicitly fix or make provision for determining the price, the parties are considered, in the absence of any indication to the contrary, to have impliedly made reference to the price generally charged at the time of the conclusion of the contract for such goods sold under comparable circumstances in the trade concerned.

This article suggests the opposite of art. 14 for it suggests that an open price contract is enforceable and that prices will be determined by the price charged at the time the contract is concluded (i.e., the market price at the time of contract formation\(^4\)). Indeed, legal scholars are not in agreement as to the meaning of these provisions. Some believe that open price contacts are enforceable,\(^4\) while others argue that they are not.\(^4\) The ambiguity with


regard to the legal status of contracts in which prices are underspecified thus gives rise to the potential for different interpretations and results. As one author notes, "[i]n a period of rapid price fluctuation, however, it is to be expected that if a controversy arises in the courts of a country that is not receptive to open price contracts, the wording of article 14(1) and a narrow construction of article 55 may lead to nullity of the contract." 43

The ambiguous legal status of open price contracts reflects the absence of a normative consensus regarding the principles that are to be accorded primacy. While the developing countries did enjoy modest success in protecting against rising prices and price setting by sellers by amending earlier drafts of the relevant provisions, they were unable to establish the general primacy of the equity principle. Earlier drafts of article 55 had established the rule of applying sellers' prices in instances of underspecification. 44 By succeeding in establishing the rule of market prices at the time the contract was entered into, the LDCs gained some protection against rising prices and against price fixing by sellers. However, the ambiguous

44. S. K. Date-Bah, "Problems of the Unification of International Sales Law from the Standpoint of Developing Countries," p. 50.
The legal status of open price contracts gives rise to the possibility that divergent judicial interpretations of the articles could dilute the protections accorded by the Convention.

The civil law countries also succeeded in the inclusion of provision of the civil law remedy, not available at common law, of a price reduction for nonconforming (i.e., defective goods (art. 50)). However, the inclusion of this provision did not appear to have generated significant opposition from common law states for, as Winship notes, "its formula has been amended so much that it resembles the common law right to deduct damages from the price...."  

The norm of contractual and market prices thus remains strong in the third phase of the regime. States have relied upon the assertion of the equity principle and the political autonomy principle to prevent or at least inhibit the entrenchment of an open price rule and price setting by sellers. However, the ambiguity over the legal status of open price contracts suggests some weakness in the rule. The extent to which open price contracts will be rendered invalid will depend very much upon the interpretations of articles 14 and 55 adopted by judicial and arbitral authorities. The strength of the norm of invoking market

prices at the time the contract of sale is formed in cases of underspecification will thus turn on uniformity in interpretation.46

It should be noted, however, that the Vienna Sales Convention applies only to international sales transactions.47 Domestic consumer sales are excluded. As a result, sales that do not fall under the sphere of application of the Convention will continue to be governed by the applicable domestic law governing prices.

(b) Liability for Defective Goods. While some international standards embodying limited liability have been created, in general, liability for defective goods in the third phase continues to be regulated predominantly by national standards. In addition, there has been a departure from the norm of limited liability in the national standards adopted by some states.


47. Article 1 provides that the Convention applies to "contracts of sale of goods between parties whose place of business are in different States: (a) when the States are Contracting States; or (b) when the rules of private international law lead to the application of the law of a Contracting State." Article 2 excludes its application to goods bought for personal, family or household use; sales by auction; sales on execution; sales of stocks, shares, investment securities, negotiable instruments or money; sales of ships, vessels, hovercraft or aircraft and sales of electricity.
There has been an erosion in common law jurisdictions of limited liability standards. In the United States, in particular, the development of consumer protection and products liability law has displaced the rule of *caveat emptor* and established strict liability standards governing death or harm to consumers resulting from defective goods.\(^48\)

In England, the development of products liability law has not been as "spectacular," although consumer protection law and developments in the law of negligence have widened the scope of the seller's liability for defective goods.\(^49\) On the Continent, the ability to disclaim liability has been curbed by the courts and by consumer protection laws.\(^50\)

Attempts to create comprehensive, uniform international standards embodying strict liability for defective goods have been unsuccessful. Reflecting the priority given by states to the political autonomy principle, states have generally been unwilling to submit to international standards. As most states rely upon consumer protection legislation to affect important domestic public policy

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\(^50\) See *Ibid.*, chap. 2.1.4, 5 and 6 for the West German, French, and Dutch positions.
goals, they have resisted encroachments upon their abilities to enact domestic standards. States objected to the inclusion of liability standards for defective goods in consumer transactions in the Hague Sales Convention on the grounds that they might conflict with national consumer protection laws.\textsuperscript{51} The Hague Conference on Private International Law undertook unification of conflict rules governing liability for defective goods and produced a convention on the matter in 1973.\textsuperscript{52} However, this convention unifies only conflicts rules and not substantive national legal rules. Furthermore, its supporters are exclusively European.\textsuperscript{53}


\textsuperscript{53} Ibid., p. 199, note 188.
UNCITRAL took up the issue of unifying products liability law in 1973, but discontinued its work in 1978. Many developing states objected to the development of international standards of strict liability on the grounds that such standards would add to their costs and thereby inhibit the development of their export trade.

The Vienna Sales Convention does address liability for defective goods, but not in a comprehensive manner. As noted earlier, the Convention does not apply to domestic consumer transactions. Nor does it govern liability for death or personal injury, which continues to be governed by national laws. While the Convention does establish rules governing "nonconforming goods," the rules do not extend to liability for death or personal injury, but establish standards regulating the conditions that must be met for conforming goods and the remedies of parties when the goods are nonconforming. The regulation of warranties of merchantability and fitness for purpose under the Convention closely parallels modern developments in the common law and, in particular, in the U. S. law of warranty, as modified by


56. See article 5.

the Uniform Commercial Code.\textsuperscript{58} These laws embody standards of limited liability, but no longer limit liability to instances where an express warranty or fraud has been shown. In general, the seller is liable for goods that are not of merchantable quality or are not fit for the purposes for which they would ordinarily be used. The seller is also liable for latent defects of which he had knowledge, but failed to disclose. The buyer has a duty to inspect the goods and inform the seller of non-conformity. As noted earlier, the Convention embodies the civil law remedy of a price reduction for nonconforming goods, which in combination of other civilian sales concepts and remedies, creates a sales regime that blends both common and civil legal traditions.

The Convention did succeed in unifying certain procedural aspects governing nonconforming goods. This was an area that invoked substantial equity concerns and reflected the tension between many developing and developed states. The developed countries wanted strict treatment of notice periods for defective goods, while the developing countries wanted more accommodating standards governing notice periods.\textsuperscript{59} The former argued in favor of the


certainty that fixed and strictly enforced notice periods would provide, while the latter objected that strict notice periods worked against their interests. Many developing countries are unfamiliar with the practice of giving notice as they do not have domestic notice requirements. Moreover, it was argued that even if they are aware of the requirement, logistical and technical considerations could render the giving of prompt notice impossible. Countries that lack the technical expertise to adequately inspect complicated machinery often have to rely on bringing in foreign experts for inspection, which would be difficult under strict time periods. Furthermore, in some countries the goods often remain at the port of arrival for a long time and delivery to the point of destination is often subject to lengthy delays. The "most controversial issues centered around the period of time within which the buyer is required to discover a nonconformity, the nature and timing of the buyer's obligation to give notice of nonconformity, and the consequences for the buyer's failure to give said notice. Those issues created a division between the delegates from the industrialized and developing


60. Date-Bah, "Problems of the Unification of International Sales Law from the Standpoint of the Developing Countries."

countries." The resulting provisions reflect a compromise between the concerns of the developing and developed countries. Under article 38 the buyer must inspect delivered goods "within as short a period as is practicable in the circumstances," acknowledging that the length of time required in order to inspect will differ from country to country. Article 39 provides that in order for the buyer to preserve the right to remedies for nonconformity, notice of non-conformity must be given to the seller within a reasonable time of discovery. A failure to give adequate and timely notice results in the loss of the buyer's remedies. However, the developing countries objected to the draconian results of a failure to give notice and to soften the impact of the rule, additional provision was made for the remedy of a reduction in price if the buyer had a "reasonable excuse" for failing to give notice (art. 44). As Patterson notes, article 44 "attempts to achieve a delicate balance: to preserve the seller's right to receive timely notice of nonconformity and to protect the buyer who has a "reasonable excuse" for failing to give that timely notice. The extent to which this delicate balance can be maintained in practice will depend upon future cases."
Unification has been achieved in another area of relevance to the assertion of defective or nonconforming goods claims. While the Vienna Sales Convention establishes time limits within which buyers must notify sellers of defective goods claims, it does not deal with the limitation period within which the parties must bring legal action to assert a legal claim. Domestic limitation periods vary widely, from six months in some countries to thirty years in others. In addition, common and civil law jurisdictions have adopted very different rules governing limitation periods.65 The uncertainties and possibilities of opportunistic forum-shopping generated by such divergent rules provided the impetus for adopting an internationally uniform limitation period.66 The United Nations Convention on the Limitation Period for the International Sale of Goods67 came into force in 1988 among ten contracting states


and has been referred to as UNCITRAL’s "first-born."\textsuperscript{68} The Convention provides a uniform limitation period within which parties to an international sales contract may exercise claims arising out of the transaction.\textsuperscript{69} The unification of limitation periods reflects the value placed upon promoting certainty in and transparency or visibility of the parties’ obligations in contracts for the international sale of goods. By establishing a uniform time period within which claims must be exercised, the Convention creates a certain and visible time limitation on the parties’ obligations.

The above discussion discloses that regime standards governing liability for defective goods in the third phase of the regime are weak. Attempts to create international products liability standards have not been successful and the existing rules are not comprehensive. Liability for defective goods under the Vienna Sales Convention does not extend to consumer sales or to claims for death and personal injury. Liability standards for these transactions and claims continue to be regulated by national laws. In addition, international standards establishing remedies for


\textsuperscript{69} As a general rule the Convention provides for a four year limitation period. The Convention was adopted by UNCITRAL in 1974 and modified by a 1980 Protocol (UN Doc. A/Conf. 97/18, Annex II) bringing it into conformity with the Vienna Sales Convention. Like the latter, it does not apply to claims arising from death or personal injury.
non-conforming goods continue to reflect the norm of limited liability.

(c) Allocation of Transport Costs and Liabilities. The adoption of uniform terms governing transport costs and liabilities continues to be the norm in the third phase of the regime. Indeed, uniformity has been strengthened by efforts to unify matters subject to different national standards in the second phase. Significant differences in the standards governing the passing of risk in sales transactions, the interpretation of trade terms, the interpretation of bills of lading, and the enforceability of clauses limiting liability in bills of lading are generating efforts to establish a normative consensus by unifying the standards applied by courts and arbitrations. In addition, new developments in transportation and in financing and documenting sales transactions are producing further unification initiatives.

National differences in the rules governing the passing of risk of loss from the seller to the buyer in international sales transactions and in the interpretation of terms of trade have been reduced by the development of uniform standards. The Vienna Sales Convention unifies rules governing the passing of risk and establishes the bearing of transit risk of loss by the buyer as the norm, unless the transportation contract provides otherwise.70

This norm is regarded as reflecting the practical considerations that the buyer is in a better position to inspect the goods, to identify any damage, and to claim against the carrier or insurer for losses. The Convention does not tie risk to ownership, as is the case with many common law systems, but attaches the risk of loss to the transfer of physical possession of the goods. This is consistent with the U. S. Uniform Commercial Code and many Continental sales laws and is more appropriate for new transport techniques of containerisation and multimodal transport.

In addition, the Convention establishes standards governing the passing of risk for goods sold in transit, an issue of considerable concern for the less developed countries. Ghana and Pakistan wanted the passage of risk for goods sold in transit to occur at the time of contracting and not at the time that possession is transferred to the carrier, arguing that the latter might work against LDCs which generally dispatch bulk commodities


72. For example, when handed to the first carrier (art. 67(1)) and the buyer's taking over physical possession (art. 69(1)).

73. See Honnold, "Uniform Law and Trade Terms," p. 163 and note 3 for the positions of several other states.
to be sold in transit. Other states, including Sweden, Japan, Finland, and Norway opposed this position, arguing that sellers' damages for losses during transit are generally covered by insurance and that it would be difficult to determine whether damage occurred before or after the sale. The Convention embodies a compromise between these two positions that has been said to create an unworkable rule. It establishes a general rule that risk passes at the time of sale (i.e., when the contract is concluded), but is followed by an exception whereby risk retroactively passes from the moment the goods are handed to the carrier 'if the circumstances so indicate' (art. 68). Critics argue that the compromise fails to provide any guidelines as to when the main rule or the exception are to be applied by the courts or arbitrators. Garro concludes that "by masking an irreconcilable position behind an illusory compromise, article 68 of the Convention fails to provide a workable rule to fill the gap left by the parties." While the Vienna Sales Convention narrows the differences in national rules governing the passage of risk for goods sold in transit, the ambiguous drafting of the

76. Ibid., p. 476.
rule leaves scope for different interpretations and the potential for compromising the uniformity achieved.

Significant uniformity has been achieved in the formulation of terms of trade. The International Chamber of Commerce (ICC) undertook the unification of trade terms in the 1920s and produced a set of rules, known as Incoterms 1936, for the interpretation of the most commonly used trade terms. Incoterms were revised in 1953 and 1980 in response to technological advances in transportation and changes in documentary procedures. The Incoterms are designed as a set of uniform rules governing transportation costs and liabilities that may be incorporated by traders by referring to them in the contract of sale. They are designed to facilitate exchange by providing greater certainty as to the parties rights and obligations under the different terms. The voluntary application of terms of trade also reflects the principle of freedom of contract, as the parties are free to select the term deemed appropriate in the circumstances. As a private association, the ICC lacks international legal personality and is thus unable to generate rules of a binding or mandatory nature. However, reliance upon Incoterms has become so common and generalized that many regard them to have acquired the status of customary international law. 77 This is particularly so for European trade where Incoterms are applied to sales

transactions even in the absence of incorporation by the parties into the contract by reference.

Incoterms 1980 provide rules for fourteen trade terms. Uniform rules are provided for the more traditional trade terms, like c.i.f., f.o.b. and c. & f., and new additions have been made to reflect container and multimodal transport techniques and new forms for documenting sales transactions, like the shipped on board bill of lading. While Incoterms go along way to unifying the standards governing transport costs and liabilities, their usage is not yet universal. In the United States, for example, many merchants continue to rely upon the American Trade Foreign Trade Definitions of 1941, which though "substantially similar" to the Incoterms, are regarded as generally more favourable to exporters. There does appear, however, to be some movement in the U. S. towards reliance upon Incoterms.

Significant efforts to unify the rules governing maritime transport have occurred in the third phase of the regime, spawned by the inconsistent standards applied to bills of lading. At present there are three sets of rules governing liabilities in maritime transportation: the Hague

78. See ibid., and Honnold, "Uniform Law and Uniform Trade Terms" for full discussion of the various trade terms and the impact of new developments in transportation and documentation.


Rules, the Hague-Visby Rules, and the Hamburg Rules. By the end of the nineteenth century clauses in bills of lading exempting shipowners from liability had become common, complex, and subject to diverse national treatment. As Hellawell notes, carriers with superior bargaining power forced more and more exculpatory or exemption clauses into bills of lading. By 1890 bills of lading commonly exonerated carriers from almost every type of liability and loss, including liability for negligence, a type of liability traditionally imposed upon carriers.81 In the United Kingdom, the courts gave effect to clauses limiting or exempting liability in deference to the principle of freedom of contract.82 American courts, in contrast, were more cautious in the enforcement of such clauses. The different approaches of national courts resulted in confusion, uncertainty, and forum-shopping and so the International Law Association (ILA) undertook the formulation of uniform rules governing bills of lading. The ILA formulated the first set of rules, the Hague Rules, which formed the basis for the Brussels Convention of 1924.83 The Hague Rules impose certain minimum


83. International Convention for the Unification of Certain Rules Relating to Bills of Lading, Brussels August
responsibilities on the carrier that cannot be reduced and impose liability for the performance of these responsibilities, subject to certain maximum exemptions. The United States and the United Kingdom, both major carrier states, gave effect to the Hague Rules. The Hague Rules were amended in 1968, producing the Hague-Visby Rules. The amendment increased the carrier's maximum liability for loss and damage and adapted the definition of certain concepts to reflect changes in transportation techniques (i.e., container transport). The United Kingdom adopted the Hague-Visby Rules, but the United States did not. In response to complaints from many countries, particularly the LDCs, asserting equity concerns that the Hague Rules and the Hague-Visby Rules unfairly favoured the interests of shipowners, UNCITRAL, in consultation with UNCTAD, undertook a review of international shipping legislation. The bill of lading was selected as a "priority subject" because goods are normally carried under bills of lading which thus affect many interests.

As a standard form contracts or contracts

84. For example, the duty to exercise due diligence to provide a seaworthy ship, to load, handle, stow, carry, keep, care for and discharge the goods, and to issue a bill of lading in a particular form.


of adhesion supplied by carriers, bills of lading raise the concern that weaker parties are unable to significantly affect the balancing of the risks of transportation and are thus in need of special protection through the formulation of standard clauses that accommodate their particular concerns.

A contract of adhesion is a form proposed by one of the contracting parties to the other as the definitive form of the contract which is intended to be unalterable except in trifling and unimportant detail; the party to whom this type of contract is offered may 'take it or leave it' but cannot renegotiate its terms and conditions.87

UNCITRAL produced the Hamburg Rules regulating carrier's liability for loss, damage, or delay in the delivery of the goods and containing modern rules on bills of lading.88

The Hamburg Rules seek to remove uncertainties and ambiguities encountered with the Hague Rules, to take into account new transport techniques (e.g., the use of containers or LASH barges) and, above all, to achieve a more balanced allocation of the risk of carriage between cargo owner and the carrier, in harmony with the laws on other modes of transport.89

87. Schmitthoff, "Standard Form Contracts and the protection of the Weaker Party in International Trade Relations," in UNIDROIT, New Directions in International Trade Law, p. 177. And see Eorsi, "Contracts of Adhesion and the Protection of the Weaker Party in International Trade Relations."


89. Gerold Herrmann, "The Contribution of UNCITRAL to the Development of International Trade Law," in Horn and
The Hamburg Rules place a greater burden upon carriers than do the Hague-Visby Rules and narrow the exceptions to carrier's liability. The Hamburg Rules embody a victory for LDCs and other states representing the interests of cargo who were seeking a more equitable balancing of risks. They also bring the liability rules governing ocean transport in line with the rules governing transportation by rail, air, and road. These rules are embodied in a number of international conventions which set liability limits and generally restrict the ability of the carrier to contract out of a minimum degree of liability. As of January 1989, only fourteen of the twenty ratifications or accessions required to bring the Hamburg Rules into effect were in place. As of that date the U. S. had signed but not ratified the Convention. American shippers generally favour ratification of the Hamburg Rules, while carriers and marine insurers favour ratification of the Hague-Visby Rules. As Pfund notes, "for progress in the United States


on these conventions to become politically possible, some sort of accommodation by these private interests seems necessary."\textsuperscript{92}

Bills of lading and the allocation of costs and liabilities thereunder are thus subject to three sets of rules establishing different standards and limits of liability, suggesting that the goal of uniformity has yet to be achieved. While LDCs and other states representing the interests of cargo owners scored a victory in asserting the equity principle as a guideline for the Hamburg Rules, their success is as yet modest. The Hamburg Rules do not at present have sufficient support to bring them into force. As a result we are left with the Hague Rules and the Hague-Visby Rules, both of which are regarded as providing inadequate recognition of the interests of cargo owners.

In addition to the above unification efforts, other initiatives to produce uniform rules have been undertaken in response to the development of new transportation techniques and documentation. The ICC has adopted a Combined Transport Document to function in place of a bill of lading and applicable rules in instances where multiple modes of transport are used.\textsuperscript{93} These rules were influential in the formulation of the 1980 U. N. Convention on International


Multimodal Transport of Goods. UNCITRAL's unification efforts have extended to include the liability of transport terminal operators, filling a lacuna in the liability rules established by other international transport conventions.\textsuperscript{94} Further unification initiatives relating to transport by air, rail, and road\textsuperscript{95} and a number of conventions stating the rules governing maritime collisions, salvage, and other matters of private law relating to maritime transport\textsuperscript{96} have also been undertaken in the third phase of the regime.

The regime standards governing transport costs and liabilities are moderately strong. Greater uniformity has been achieved concerning the rules regulating the transfer of risk and terms of trade. However, ambiguity regarding the standards applicable to the transfer of risk for goods sold in transit suggests some weakness. Further weakness is evidenced by the existence of three different sets of rules governing bills of lading. The inability of states to agree upon uniform standards governing liabilities under bills of lading show that domestic interests can place significant

\begin{itemize}
  \item \textsuperscript{94} Convention on the Liability of Operators of Transport Terminals in International Trade.
  \item \textsuperscript{95} 1929 Warsaw Convention for the Unification of Certain Rules Relating to International Transport by Air; 1956 Convention on the Contract for the International Carriage of Goods by Road; 1961 International Convention Concerning the Transportation of Merchandise by Rail.
  \item \textsuperscript{96} See David, "The Movement in Favor of the Unification of Private Law," pp. 150 et seq., for discussion of these unification efforts.
\end{itemize}
limitations on the unification process. However, strength and vitality are evidenced by the expansion of the scope of the regime to address new developments in maritime transportation and documentation and to include other modes of transportation. Furthermore, uniform standards governing salvage and collision have now been codified in international conventions of broad application.

(d) Insurance. The norm in the third phase of the regime continues to be the adoption of uniform standards governing some insurance concerns. As in the case of transportation, efforts are being made to unify differences in some insurance standards that developed in the second phase. However, while merchants have devised new practices and instruments to meet their insurance needs, there is little movement to unify these practices through positive acts of law creation.

Efforts to unify the standards governing contribution to the general average undertaken by the International Law Association in the late nineteenth century produced the York–Antwerp Rules of 1890. These rules constitute a voluntary system of standards governing the adjustment of general average claims. They define the conditions that give rise to contribution to the general average and provide guidelines for apportioning contribution. The 1974 revision of the rules provides for contribution "when and only when, any extraordinary sacrifice or expenditure is intentionally
and reasonably made or incurred for the common safety for 
the purpose of preserving from peril the property involved 
in a common maritime adventure."97 The other rules provide 
specific guidelines for apportioning contribution and 
procedures for asserting claims. While the York-Antwerp 
Rules unify the insurance standards governing maritime 
transport, they are of a voluntary nature. Reflecting the 
principle of freedom of contract, merchants are free to 
choose whether or not to invoke them. However, the parties 
are also subject to national insurance laws governing 
general average contributions and the effect and 
interpretation that national courts give to the rules 
differs from state to state. Thus uniformity is often 
undermined by differences in national interpretation and 
application.98

During this phase merchants also devised new methods 
for creating and documenting insurance transactions. Marine 
insurance certificates evolved out of merchant practice in 
response to insurance needs generated by the increased use 
of floating insurance policies in the early twentieth 
century.99 The growth of international financing created a

98. See ibid., chap. 32 for a discussion of the approaches 
of English, American and French courts.
99. A floating or open policy is a policy that describes 
the insurance in general terms, leaving the particulars 
for later definition. They are designed to cover a 
number of shipments made over a certain time period 
within a particular geographic location and to obviate 
the need for many separate policies. See Thayer,
need for a negotiable insurance document that would provide financing banks or distant purchasers with adequate security.

With increasing volume of international sales, particularly sales on c.i.f. terms, with the expanding use of commercial letters of credit and the developing facilities of the banks as media in international commerce, there arose a demand for a document which might be used in company with the invoice, the bill of lading, and the bill of exchange, as negotiable evidence of the insurance on the relative [sic.] goods. None of the existing instruments familiar to the trade would answer this purpose.... The bankers and merchants who were feeling the need for a new document...wanted full protection for the innocent holder of the same kind that already was given him by the bill of exchange and the bill of lading, and they wanted this in the form of a mobile document, expeditiously issued, and immediately available for use with the other methods of commercial financing.100

Marine insurance certificates were developed by bankers and merchants to meet these needs. Their use has became common and widespread; however, they have been given different effect by different national courts. American courts generally enforce them as negotiable documents, regarding them as authoritative by virtue of commercial custom and usage. Justice Learned Hand stated the American position succinctly:

"Marine Insurance Certificates," p. 239 and Berman and Kaufman, "The Law of International Commercial Transactions," p. 260. Thayer notes at p. 244 that it was estimated that 90% of all ocean cargo insurance was conducted under floating policies as early as 1922.

When usage of this kind has become uniform in an actively commercial community, that should warrant enough for supposing that it answers the needs of those who are dealing upon the faith of it. I cannot see why judges should not hold men to understandings which are the tacit presuppositions on which they deal. From Lord Holt’s time on they have generally in one way or the other been forced in the end to yield to the more flexible practices of commercial usage. So far as I know the results have been acceptable to every one, once they were settled.101

British courts, however, were less disposed to accepting changes in commercial insurance practices and did not give the same effect to the certificates. Thus, while the practice of using marine insurance certificates has become uniform, their interpretation and effect is not. This would appear to be an area ripe for international unification, but such efforts have not occurred. Similar observations may be made with regard to other commercial practices. International factoring and leasing are forms of international financing that are present in their infancy, while the electronic transfer of funds provides a new medium of exchange. As we shall see in the next section, these matters are presently the subject of international unification with respect to matters of finance. However, the insurance concerns they raise have not surfaced as a subject for unification. It might be that due to their infancy attention has not yet turned to matters of insurance. However, this is not the case with marine

insurance certificates which have been in currency for some seventy years. It is interesting to note that while insurance contracts have been identified as standard form agreements that raise concerns regarding the protection of weaker parties and, in particular, LDCs, insurance law has not become the focus of efforts to create a new international economic order as have other areas of commercial law.\textsuperscript{102} While the equity principle has been advanced in reference to the law governing sales and transport, it has not been asserted in international forums in reference to insurance law. This is particularly significant when one considers that a few very powerful multinational corporations dominate the insurance field and deal with consumers on a 'take it or leave it' basis. Indeed, insurance contracts are forms of adhesion contracts \textit{par excellence}, where the insurance company, as the drafter of the standard form insurance contract, has the upper hand from the beginning.\textsuperscript{103}

\textsuperscript{102} See Eorsi, "Contracts of Adhesion and the Protection of the Weaker Party in International Trade Relations," for the identification of insurance contracts as standard form contracts that raise equity concerns. And see A. L. Parks, "Recent Developments in Marine Insurance Law," \textit{Journal of Maritime Law and Commerce} 14 (1983): 159-94 for discussion of the concerns developing countries have with the domination of insurance practices by the U. K.

\textsuperscript{103} See Eorsi, \textit{ibid}. The English Marine Insurance Act (1906), for example, codifies the law on marine insurance and provides a standard policy, known as Lloyd's S. G. policy which is widely used by Lloyds and other insurance companies. This standard policy is also used for aviation and overland insurance, areas in which standard form policies have not yet been
During the third phase of the regime while the norm of adopting uniform standards governing insurance has strengthened in some respects, the norms are generally quite weak. States have engaged in efforts to unify the law governing the general average. However, these rules at best have the status of commercial custom and are not uniformly interpreted by national courts. While the practice of contributing to the general average is a norm, variations in national interpretation weaken uniformity. Commercial practice continues to generate uniform documents, as in the case of marine insurance certificates. However, again this practice is at most customary law and subject to different national treatment. Furthermore, the scope of the regime has not broadened to include new developments like factoring, leasing, and the electronic transfer of funds that raise significant insurance concerns. Nor have the equity concerns raised by standard form insurance contracts been asserted in international arenas. While the infancy of some commercial practices and the fact that they have only recently become the focus of international regulation probably explains the failure to recognize and address some insurance concerns, the same does not apply to other concerns and practices.

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developed. See Jackson and Davies, Legal Problems of International Economic Relations, p. 51.
(e) Financing and Credit. In the third phase of the regime the norm continues to be the adoption of uniform credit and payment documents and procedures to facilitate sales transactions. The principles of merchant autonomy and freedom of contract are reflected in the broad choice open to merchants in financial procedures and documentation. Also, the primacy of the principle of the facilitation of exchange is being reinforced as commercial actors unify diversities that had come to characterize legal standards governing negotiable instruments in different states in the second phase, as they continue to develop new uniform documents and procedures to address technological advances and changing commercial needs, and as the practice of charging interest has widespread legitimacy.

The international unification of negotiable instruments was first raised in 1863 by the Association for the Progress of the Social Sciences at a congress held in Ghent. At the time three different sets of rules embodied in French, German, and Anglo-American law characterized the law governing negotiable instruments. The International Law Association formulated rules for bills of exchange, later in the nineteenth century. These rules were called the Bremen

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Rules and formed the basis for rules produced by the Institute of International Law in Brussels in 1885. In the same year an international congress held at Antwerp produced rules governing cheques. Unification was not undertaken again until 1905 when the International Chamber of Commerce and various national governments initiated an international conference which met in 1910. This conference produced draft uniform laws on bills of exchange and promissory notes. The unification process was interrupted by the war but was taken up again after the war by the Economic Committee of the League of Nations. Two international conferences held at Geneva produced uniform law on bills of exchange, promissory notes, and cheques.\textsuperscript{106} As David notes the Geneva conventions were for some "a brilliant success, for others almost a total failure."\textsuperscript{107} For common law countries they were regarded as based entirely upon Continental, civil law concepts and unsuitable to the common law governing negotiable instruments. As a result no common


\textsuperscript{107} "The Movement in Favour of the Unification of Private Law," p. 129.
law countries adopted them. In addition, while the Geneva conventions produced greater uniformity of German and French rules, differences persisted amongst civil law jurisdictions as the conventions permitted significant reservations.

UNCITRAL at its first session in 1968 identified the unification of negotiable instruments or international payments as a priority subject on the basis of broad support from member states for the initiative. A report prepared by UNIDROIT and the response of states to a questionnaire on the subject disclosed widespread recognition of the need to unify the common law system, embodied in the U. K. Bills of Exchange Act and the U. S. Uniform Commercial Code, and the civilian system, embodied in the Geneva conventions.

UNCITRAL thus undertook the formulation of uniform rules for

108. Von Marschall, "UNCITRAL'S Proposed International Bill of Exchange," p. 8 cites differences in common and civil law governing the transfer of risk in forged endorsements and the rules governing defects in title and defenses as providing barriers to support of common law countries.


the optional use of parties in international payments. The Draft Convention on International Bills of Exchange and International Promissory Notes was adopted by UNCITRAL in 1981 and revised in 1985. The convention was approved by the General Assembly and opened for signature in 1988. It is generally believed that the convention provides a workable reconciliation of common and civil law standards and rules.\textsuperscript{111} Furthermore, the optional character of the convention is applauded by those who support leaving maximum scope to merchant autonomy and freedom of contract.\textsuperscript{112}

Work on unifying the law on international cheques produced a Draft Convention on International Checks in 1981, which was circulated to governments for comments. However, the work was postponed in 1984 as many states expressed doubt regarding the practical need for a convention.\textsuperscript{113}

Efforts to unify the law governing letters of credit also characterize the third phase in the development of the


\textsuperscript{112} \textit{Ibid.}

regime. During the third phase merchants continued to devise uniform methods for effecting international payments by developing new documentary transactions like the irrevocable letter of credit. However, uniformity came to be limited as states enacted legislation governing documentary credits and as significant differences emerged in national treatment and interpretation of letters of credit. The International Chamber of Commerce undertook the task of unifying the rules governing letters of credit, issuing a set of rules for the optional use of parties in 1933. These rules are known as the Uniform Customs and Practices for Documentary Credits (UCP) and are used by merchants, banks, and other financiers by incorporating them into their letters of credit. They were revised in 1951, 1962, and 1983. The UCP

114. Ellinger, Documentary Letters of Credit, p. 37 accounts for the increased use of documentary credits in the post-War period as a response of commercial actors to the economic instability that prevailed. "Merchants prospered and overnight became insolvent. The use of letters of credit as security became necessary. Moreover, once merchants became accustomed to obtaining securities for payment by way of letters of credit, they were not likely to discontinue the practice."

115. See Ellinger, *ibid.*, for a summary of national regulations governing documentary credits.

116. See Thayer, "Irrevocable Credits in International Commerce: Their Legal Nature," for a comparison of Anglo-American, French, and German theories on letters of credit.

117. ICC, Brochure No. 83.

118. ICC, Brochure No. 151.

119. ICC, Brochure No. 222.
significantly unify the law governing letters of credit and are widely used in international trade. Most agree that "apart from being used all over the world, documentary credits have achieved more uniformity than many other commercial instruments." Even though the UCP do not have the status of law, they are regarded by some as "a set of universally accepted norms" recognized as an independent source of law by virtue of commercial usage. It is estimated that banks in 165 countries utilize the UCP to regulate international payments.

In addition to standardizing the rules governing letters of credit, the UCP revisions accommodate changes in technology and transport customs and documentation.

120. ICC, Brochure No. 400.

121. Ellinger, Documentary Letters of Credit, p. 38 and see Jackson and Davies, Legal Problems of International Economic Relations, p. 53 who note that the "vast majority of letters of credit incorporate the UCP."

122. Ellinger, "Letters of Credit," pp. 252-3 notes that some French and German authorities regard the UCP to have the force of binding customary law, but that English and American authorities disagree. The latter argue that the norms have not evolved through independent practice but through bargaining and as such are binding only insofar as the parties incorporate them into their contracts. Ellinger also notes that Schmitthoff, von Caemmerer, Hartfield and Goldstjan regard the UCP to be binding customary law. See p. 252, note 39.


revisions accommodate new techniques in electronic data processing and the development of combined transport techniques and documents. In addition, they address new financial instruments like stand-by letters of credit, which are essentially bank guarantees.

Technological advances in communications and the development of new instruments for financing international transactions have also given rise to further unification efforts. UNCITRAL has undertaken unification of the law governing the electronic transfer of funds. The issuance of payment instructions by electronic means rather than by physical means generates legal problems concerning the payment process and liabilities (i.e., when does payment become final; who is liable for loss caused by delay in transmission or incorrect payment) and evidentiary matters (i.e., what is the evidentiary force of records kept in electronic form). As a new area replete with legal uncertainties, UNCITRAL undertook the preparation model rules on electronic funds transfers. The Commission decided to proceed by way of developing model rules rather than an international convention unifying national laws due to the

paucity of national law on the subject. The Model Rules on Electronic Funds Transfers, renamed the Model Rules on Credit Transfers, are still in the drafting stages and are designed for the optional use of parties, embodying the principles of merchant autonomy and freedom of contract. 125

Merchants have also devised new methods of financing transactions that are presently the subject of unification efforts. International factoring and leasing are two financing techniques that "have developed largely untrammeled by legal regulation." 126 Both methods of financing "developed in financial circles to meet newly perceived market needs created by the move towards a credit economy." 127 International factoring, a form of receivables financing, is increasingly being used by merchants in response to the expansion of credit in recent years. 128 By freeing up capital in the form of receivables, international


127. Ibid.

128. "The huge growth in the extension of credit over the last fifty years has meant that the trader finds more and more of his capital locked up in the form of receivables; and to help him convert these into cash he has turned increasingly to receivables financiers who will either buy the receivables at a discount or advance money on the security of them." See R. M. Goode, "A Uniform Law on International Factoring," in Diamond, ed., Unification and Comparative Law in Theory and Practice, p. 91.
factoring facilitates the financing of international transactions. This is an area largely untouched by national legislation. Factors have generally governed their own relations and have formed private national associations of factors and an international association called the Factors Chain International to provide forums for articulating commercial practices in the area. These associations have devised standard form contracts which are used by members as the foundation for factoring agreements. In addition, the Factors Chain International has produced a Code of International Factoring Customs, which like the UCP, does not have the force of law, but is given effect by the parties by incorporation into the factoring contract. International factoring raises a number of legal issues, including the rules governing the formalities for creating a factoring contract and governing the rights and liabilities of parties under the contract. These issues have been subject to different interpretation and treatment by national courts and rather divergent standards have emerged under the common and civil law.129

International leasing is another method of financing that has increasingly been used since the Second World War to facilitate the financing of capital equipment. Like international factoring, international leasing is subject to

129. See ibid., for a summary of the legal issues raised by international factoring.
varying treatment under different national legal systems.\textsuperscript{130} Furthermore, like international factoring and unlike more traditional forms of exchange, such as the sale of goods,

\ldots financial leasing is novel to many countries. The result is that domestic laws have yet to be developed in most jurisdictions to regulate adequately this type of financing, including some jurisdictions that in other respects have mature, highly developed systems of commercial law. Very few countries have enacted laws designed to deal specifically with the unique legal issues that arise in the context of this type of transaction. Consequently, both domestic and international financial leasing transactions are forced under the law of most jurisdictions into legal structures that were not designed to accommodate this type of transaction. Apart from the uncertainty that is associated with the application of existing national law to financial leases, there is the added problem of determining the law applicable to each aspect of an international financial leasing.\textsuperscript{131}

UNIDROIT undertook the unification of the law governing international factoring and leasing, producing two conventions that were adopted at a conference held in Ottawa in 1988. The UNIDROIT Conventions on International

\textsuperscript{130} L. Reczei, "Leasing and its Unification," in Diamond, ed., \textit{Unification and Comparative Law in Theory and Practice}, p. 212. The author notes at p. 209 that the volume of international leasing transactions rose from an annual of 40 million dollars in 1954 to 7 billion dollars in 1972. The American Association of Equipment Lessors reported the worldwide volume of leasing transactions as 150 billion dollars in 1979 and forecast an increase to 200 billion dollars by the mid 1980s.

Financial Leasing and International Factoring embody the principles of merchant autonomy and freedom of contract in that they establish a permissive legal framework. The parties to such agreements are left considerable scope to modify the rules provided for in the conventions.\textsuperscript{132} It is too early to evaluate the likely success of the conventions; however, they are generally regarded as contributing to the removal of legal barriers to these methods of financing.\textsuperscript{133} It is interesting to note that the conventions have attracted the support of many less developed countries who are increasingly looking to alternatives to conventional methods of borrowing.\textsuperscript{134}

In the third phase, the norm continues to be the widespread practice of interest charges, with the exception of Moslem countries in which such practice is prohibited. However, merchants are subject to national laws that establish limits on interest charges. In addition, national differences in the treatment of interest remain for in some countries, like Germany and Switzerland, different rates apply to commercial and to personal loans.\textsuperscript{135}

\footnotesize{\textsuperscript{132} See \textit{ibid}.}

\footnotesize{\textsuperscript{133} \textit{Ibid}.}

\footnotesize{\textsuperscript{134} The first five governments to sign the conventions when they were opened for signature were developing countries: Ghana, Guinea, Nigeria, the Philippines and Tanzania. Subsequently, Morocco signed.}

\footnotesize{\textsuperscript{135} Tallon, "Civil Law and Commercial Law," p. 78.}
The norms governing financial and credit arrangements have strengthened in the third phase of the regime as commercial actors unify diverse national standards and as they continue to develop new uniform documents and procedures to meet technological advances and changing commercial needs. The scope of the regime has broadened to include new forms of financial transactions and in some instances uniform standards are being created _de novo._

We will now turn to consider the procedural dimension of the regime.

2. **Procedural Dimension**

(a) _Locus of Regulation._ During the third phase the norm regarding the locus of regulation is the acceptance of a mixture of state, merchant, and international control. States, merchants and private merchant associations, and international organizations are recognized as legitimate agents for law creation and enforcement. States still exercise significant control over the development and nature of regime rules and norms, while private actors continue to develop commercial customs and are growing in status as legitimate agents for creating commercial law. States and private merchant associations cooperate in international organizations engaged in the unification of commercial law. In addition, the growth of international organizations engaged in the unification of commercial law and capable of
generating rules of broad application is one of the most significant developments in the evolution of the regime.

A variety of organizations are involved in establishing uniform commercial standards, although some have been more successful than others. While it has been noted that "so far no scheme of scientific classification has been found which would allow classification of all existing bodies into a few categories," it is common to differentiate between intergovernmental and non-governmental agencies or organizations. The main intergovernmental organizations are UNCITRAL, UNIDROIT, and the Hague Conference on Private International Law, while the significant non-governmental organizations include the International Chamber of Commerce (ICC), the International Law Association (ILA), and the International Maritime Committee (IMC).


138. This list is not exhaustive. UNCTAD has adopted codes of relevance to commercial law including the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practice, U. N. Doc. A/Conf. 2/35/6 and the Code of Conduct for Liner Conferences. UNCTAD is also working on a Code of Conduct on Transfer of Technology, a model contract for marine hull insurance (U N Doc. TD/B/847, p. 52 et seq) and rules protecting industrial property. UNIDO, established in 1966 as an organ of the General Assembly, is working on the development of model contracts for specific industries, while the World Bank and the IMF have established Guidelines for Procurement under World Bank Loans and IDA Credits that establish standards for contracting. IMCO (now IMO) has also been active in the unification of maritime law. For
As was noted at the beginning of this chapter, early unification efforts were almost exclusively limited to the activities of private merchant associations. Merchant trade associations and private groups like the Institute de Droit International, the ILA, the IMC, and the ICC formulated statements of commercial customs and norms for the voluntary use of their members. These associations have been generally quite successful in articulating standards of broad application. Government involvement in unification began with the Hague Conference on Private International Law. However, the work of the Hague Conference is generally limited to unifying conflict rules and not fuller discussion of these agencies see Dolzer, "International Agencies for the Formulation of Transnational Economic Law" and David, "The International Unification of Private Law."

substantive rules of law. Furthermore, in its early days the Hague Conference functioned more as a regional rather than as a global organization as membership was largely confined to European states and the texts it produced reflected civilian legal traditions. After the First World War, government involvement increased with the creation of UNIDROIT, established within the framework of the League of Nations. However, as in the case of the Hague Conference, unification undertakings were primarily regional and civilian in character and did not attract broad support. The post World War Two period witnessed an increase in governmental involvement in the specialized agencies created by the United Nations. The creation of UNCTAD in 1964 and

140. UNIDROIT was established in 1926 on the basis of a bilateral agreement between the Italian government and the League of Nations. UNIDROIT separated from the League in 1935, following the withdrawal of Italy from the League, and in the 1950s entered into cooperation with a number of international organizations, including the U. N. Since 1940 UNIDROIT has been operating as an independent international organization. UNIDROIT has a membership of some forty-eight countries, including most Western European states, some Eastern European states and a number of African and Asian states. UNIDROIT has worked on the unification of a number of commercial law subjects including the international sale of goods, international agency, validity of sales contracts, rules of road and waterway, recognition and enforcement of arbitral awards, bills of exchange, intellectual property, leasing, factoring, warehousing, garaging, the law of contract, and powers of attorney, a code on international trade law, and the law of franchising and security interests in mobile equipment. See generally, Riccardo Monaco, "The Scientific Activity of UNIDROIT," in UNIDROIT, New Directions in International Trade Law, pp. xvii- xxxix; M. J. Bonell, "The Unidroit Initiative for the Progressive Codification of International Trade Law," and Matteucci, "Unidroit, The First Fifty Years."
UNCITRAL in 1966 marked the creation of global forums for unification initiatives. UNCITRAL, in particular, provided the first global forum and the real impetus to the unification movement.\textsuperscript{141} Indeed, UNCITRAL is the most successful of the intergovernmental organizations in generating rules of broad application and support. This is because membership in UNCITRAL is designed to represent all major legal systems in the world and states of various levels of development, including both market and planned economies. Membership is determined on a basis of regional representation,\textsuperscript{142} and pursuant to the rules of procedure adopted by UNCITRAL, decision-making proceeds by way of two-thirds majority vote. However, according to Canadian representatives at UNCITRAL, no decision has yet been put to a vote. The Commission has always reached a decision by


\textsuperscript{142} The scheme is regional and membership rotates. Initially UNCITRAL membership included twenty-nine states: seven African; five Asian; four Eastern European; five Latin American; eight Western European and 'other states.' See art. 1, General Assembly Resolution 2205 (21). In 1973 membership was increased to thirty-six states, adding two African; two Asian; and one additional Eastern European, Latin American, and Western European (including 'other states') states. See "Working Methods of the Commission: Note by the Secretariat," U n Doc. A/Conf. 9/299, reprinted in UNCITRAL Yearbook 19 (1988): 165-6. Canada, Australia and the United States qualify as 'other states.'
consensus. Work is undertaken by Working Groups, which are assigned specific areas of the law for unification. The Working Group on Time-Limits and Limitations (Prescriptions) was created in 1969 and went out of existence after the preparation of the above-mentioned Convention on the Limitation Period in the International Sale of Goods. The Working Group on International Shipping Legislation, also created in 1969, was similarly phased out after the adoption of the Hamburg Rules, discussed earlier. The Working Group on the International Sale of Goods was created in 1969 and renamed the Working Group on International Contract Practices in 1979 after completing work on the unification of sales law. This working group is engaged in developing uniform law in a number of areas including liquidated damages and penalty clauses, independent guarantees and standby letters of credit, liability of transport terminal operators, and freight forwarders.

UNCITRAL's most successful unification efforts to date, however, relate to the unification of sales law, discussed above in reference to the Vienna Sales Convention, and the unification of arbitration law, to be discussed later under

143. Senior Legal Counsel, Federal Department of Justice, Ottawa. See also Honnold, Uniform Law for International Sales, chap. 1.

Dispute Settlement. In addition, the Working Group on International Payments successfully concluded unification of the rules governing bills of exchange and promissory notes and is presently working on a model law governing the electronic transfer of funds, discussed above.

UNCITRAL responded to the assertion of equity demands by less developed countries by creating a Working Group on the New International Economic Order. The work of this group, however, has largely been restricted to devising guides and model laws for the optional use of developing countries. Many developed states were insistent that the working group restrict its activities to the formulation of texts that assist developing states in the negotiation of commercial agreements, but that do not in any way bind the parties.\textsuperscript{145} This is the case for the Legal Guide on Drawing up International Contracts for the Construction of Industrial Works, drafted and adopted by UNCITRAL. The Guide is designed as an optional set of guidelines to assist less developed countries in the negotiation and drafting of construction contracts. The working group is also preparing an optional Model Law on International Procurement which

\textsuperscript{145} According to Canadian representatives at UNCITRAL the developing countries have been unable to generate sufficient support in the Working Group on the New International Order for the creation of conventions or model laws that impose obligations upon signatories to structure their commercial relations with development concerns in mind.
seeks to render government procurement practices more uniform, transparent, and equitable.

UNCITRAL is also working on a Legal Guide on Countertrade, a concern of some importance to developing countries, but this work has not been assigned to a particular working group yet.

In addition to these agencies, it should also be noted that unification efforts are also underway in regional organizations, including the European Economic Community and the Inter-American Specialized Conferences on Private International Law held by the Organization of American States.\textsuperscript{146}

Dolzer observes that there appears to be a "special rhythm" in the development of new agencies engaged in unifying commercial law:

...new agencies appear, in general, only in response to extraordinary events. So far, the practical need to regain some basic international rules in the second half of the nineteenth century, the desire to establish a more stable world order after the end of the two World Wars and the newly acquired self-confidence of the developing countries in the framework of truly global organizations within the past two decades have provided the

These agencies are engaged in the creation of a permissive regime that allows maximum play for merchant autonomy, freedom of contract, and informality and that emphasizes the facilitative nature of the exchange relationship. Insofar as the equity principle is recognized, it is done so within the context of permissive and voluntary standards. The principles of state intervention, merchant autonomy, and international intervention coexist, although their influence or weight varies for different substantive issues.

The continuing influence of the principle of state intervention is evident in the fact that state control remains the norm for a number of substantive issues. States have resisted the development of rules in areas considered to encroach too greatly upon their political autonomy. We have seen that states remain the legitimate authorities for regulating liability for defective goods. They have simply been unwilling to submit to international regulation of products liabilities that limits their ability to implement domestic consumer protection policies. In some cases, the fear that other states will benefit more under specific standards has produced ambiguous rules that have the potential of divergent interpretation and application. Such ambiguity enables national courts to exercise considerable

147. "International Agencies for the Formulation of Transnational Economic Law," p. 64.
influence over the normative content and effectiveness of the rules through the imposition of national standards in their interpretation and application. The ambiguous legal status of open price contracts leaves room for considerable national control over interpretation and enforcement. Similar ambiguity characterizes the rules governing the passage of risk for goods sold in transit. National control is also evident in the area of insurance concerning the interpretation and enforcement of the rules governing the general average and marine insurance certificates.

In addition, most developed states prefer the development of optional and voluntary rules and have opposed attempts to create mandatory obligations. As a result, the regime embodies predominantly optional standards and rules. Most of the conventions are of optional application or may be contracted out of by merchants in their commercial agreements. Furthermore, most are limited in application to international transactions, leaving domestic transactions untouched and suggesting a revival of the earlier dualistic system of regulation. UNCITRAL's Vienna Sales Convention is limited to international sales agreements and is premised upon merchant autonomy and freedom of contract. The parties to an international sales contract may opt out of the application of the convention. UNCITRAL's Conventions on International Bills of Exchange and Promissory Notes and Model Rules on Credit Transfers and UNIDROIT's Conventions on International Factoring and Leasing are also of voluntary
application, and limited in application to international transactions.

Exceptions to this predominantly permissive regulatory framework do, however, exist. They include the rules regulating the limitation and exemption of carrier's liability under bills of lading.\textsuperscript{148} The Hague Rules, Hague-Visby Rules, and Hamburg rules establish mandatory standards regulating the carrier's liability that cannot be contracted out of by the parties. However, while the LDCs and other cargo states were successful in establishing mandatory standards governing the liabilities of carriers, the Hamburg Rules have not attracted sufficient support to bring them into force or to replace the Hague and the Hague-Visby Rules. Furthermore, the mandatory character of the rules has been attacked by those who argue that they are out of keeping with the predominantly voluntary nature of the regime. Kopelmanas argues that the mandatory regulation of carriers' liability may have been justifiable "at a time when carriers were above all powerful maritime enterprises or state monopolies" and when it was thought reasonable to protect the consignor against abuse. However, it is not justifiable today "in view of the competition between the various modes of transport" and thus the contract between the carrier and the consignor of the goods should be "left

\textsuperscript{148}. As we shall see in discussing Dispute Settlement, the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards also creates mandatory standards.
to the free negotiation of the parties.\textsuperscript{149} Arguably, the mandatory application of the Hamburg Rules is more reflective of the tradition established by the earlier transport conventions of dealing with transport obligations through mandatory rules, and not a particular victory of the LDCs and other cargo states. It is notable that, while the LDCs have favoured the establishment of mandatory rules in other areas, they have been largely unsuccessful. The guides and model laws produced by UNCITRAL'S Working Group on the New International Economic Order are entirely optional, while the concessions made to LDCs regarding prices for goods sold in transit and notice periods were made within the context of a convention of voluntary application.

The weight accorded the principle of merchant autonomy is evident in the enhanced recognition of the legitimacy of rule creation by private trade associations and merchant customs and practices. This is a result of the success experienced by these private agencies in the generation of standards that attract support throughout the world. The ICC is making a major contribution to the unification of commercial law through the articulation of commercial custom.\textsuperscript{150} The Uniform Customs and Practice for Documentary

\textsuperscript{149} "International Conventions and Standard Form Contracts as Means of Escaping from the Application of Municipal Law - II," p. 122.

\textsuperscript{150} See generally Michael C. Rowe, "The Contribution of the ICC to the Development of International Trade Law," in
Credits and Incoterms are widely used by merchants throughout the world and, as we shall see when we consider Dispute Settlement, the ICC has also made a major contribution to the unification of arbitration rules. The IMC and ILA have contributed to the unification of maritime law, particularly with regard to the rules governing bills of lading and the rules governing general average contributions. The ILA was also influential in the unification of bills of exchange. These private associations, though not competent to create binding uniform law, exercise considerable influence on the generation of norms by providing statements of commercial custom and practice and model laws for the optional use of parties. They work with their national chapters and with intergovernmental organizations, providing technical and legal expertise and advice. Furthermore, merchants continue to generate uniform customs and practices, as evidenced by the development of marine insurance certificates and new forms of international financing, like leasing and factoring.

The influence of the merchant autonomy principle is also evident in the predominantly voluntary nature of the

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regime. Merchants, like states, favour the creation of permissive, suppletive standards that give maximum play to the principle of freedom of contract in the belief that such standards facilitate more efficient exchange.

The weight accorded the principle of international intervention is evident in the success of the numerous international conventions and model laws generated by UNCITRAL and to a lesser extent by UNIDROIT and the Hague Conference. However, it is critical to note that the success of these texts lies in their fidelity to the principles of merchant autonomy and freedom of contract and in their deference to the principle of state intervention. They establish a permissive regulatory framework that poses minimal constraints on freedom of contract and touches lightly upon matters of national public policy.

The norms regarding the locus of regulation in the third phase of the regime are reasonably strong. While state control persists in significant areas, there is growing recognition of the legitimacy of international organizations, merchants, and private merchant associations as agencies for the creation of commercial rules and standards. In particular, the ability of UNCITRAL and the ICC to generate standards of broad application and support have contributed to the efficacy of international regulatory efforts. As a result there has been some weakening in the
norm of state control as states participate in the international unification movement.

The growing influence and legitimacy of intergovernmental and non-governmental organizations in the development of the regime can be attributed to their deference to state authority and to their commitment to the creation of a permissive, voluntary regime -- a commitment shared by the Western developed states.

(b) Methodology of Rule Creation. The norm in the third phase of the regime is the widespread acceptance of both positive law and custom as sources of law. The primary sources are positive laws in the form of international legislation and national legislation. The growing legitimacy of international legislation as a source of law marks a weakening of the norm of national legal regulation characteristic of the second phase. Furthermore, there has been a revival of commercial custom as a source, signalling a return to the medieval notion of a jus commune.

Schmitthoff notes that the term "international legislation" is a "misnomer", since "the power to create legal rules in a particular territory can only be exercised by, or by the authority of, the national sovereign." Thus international legislation refers to "deliberate normative regulations devised internationally and then introduced into
municipal law by municipal legislation. International legislation may be created by the adoption by states of a multilateral convention or the formulation of a model law, which is then adopted by states through the enactment of municipal law fashioned upon the model law. In contrast, international commercial custom "consists of commercial practices, usages or standards which are so widely used that businessmen engaged in international trade expect their contracting parties to conform with them and which are formulated by international agencies...or international trade associations." Schmitthoff further notes that the main difference between the two sources is that international legislation applies "by virtue of the authority of the national sovereign," while international custom "is founded on the autonomy of the will of the parties who adopt it as the regime applicable to the individual transaction in hand." This distinction is somewhat obscured by the fact that international legislation, as we have seen, may create a permissive regulatory framework whereby the application of the conventions is optional. This is the case with regard to the Vienna Sales Convention, the Convention on International Trade, Its Growth, Formulation and Operation," in Schmitthoff, ed., The Sources of the Law of International Trade, p. 16.

152. Ibid.

153. Ibid.

154. Ibid.
Bills of Exchange and Promissory Notes, and the Conventions on International Factoring and International Financial Leasing. These conventions embody the principles of merchant autonomy and freedom of contract, allowing merchants to exclude their application. In addition, in enacting municipal legislation bringing into effect model laws, like the UNCITRAL's Model Law on International Commercial Arbitration, Model Rules on Credit Transfers, and Model Law on International Procurement, national legislatures control whether the legislation is ultimately of a mandatory or optional character. In contrast, municipal legislation putting into effect the various transport conventions and the New York Convention on the Recognition and Enforcement of Arbitral Awards creates mandatory rules which application cannot be excluded.

The distinction is further obscured by different forms of commercial custom. International commercial customs like the Incoterms, the Uniform Customs and Practices for Documentary Credits, the Code of International Factoring Customs, the Uniform Rules for a Combined Transport Document, and the York-Antwerp Rules constitute customs that have been formally or deliberately articulated by formulating agencies. However, commercial custom can also take the form of practices that are in common usage, like the use of marine insurance certificates, but have not been deliberately or formally articulated by formulating agencies. The former has been referred to as formulated
international commercial custom, while the latter is unformulated commercial usage. While formulated international commercial custom has unquestionably gained legitimacy as a source of law in the third phase of the regime, as evidenced by the widespread use of Incoterms and other standards developed by non-governmental formulating agencies, the legitimacy of unformulated commercial usage is more controversial. As Honnold observes, "[G]overnments have sometimes viewed such custom as inconsistent with their sovereignty and with principles on which their regimes were based." The controversy emerged in negotiations concerning the legal status that was to be given to commercial usages and practices in the Vienna Sales Convention.

This controversy confronted the views of representatives from socialist and developing countries with those from Western, developed countries. Aside from the need of planned economies for security and foreseeability in contractual relationships, the main reason why many developed and socialist countries are suspicious of the impact of trade usages in the international sphere is based on the fact that those usages were settled primarily by industrialized nations and are likely to reflect the interests of such countries. In contrast, developed countries like the United States and Great Britain place prime emphasis on regularly observed trade usages, which are said to increase mercantile flexibility, and thereby, economic efficiency.

155. Ibid., p. 23.

156. Uniform Law for International Sales, p. 147.

Many developing countries tried to limit the influence of usages because they regard them as neo-colonial in that they derive from a past in which developing states did not participate.158 It was argued that "usages and customs usually crystallize from practice dominated by actors from the developed countries, particularly those in the West. Such usages are therefore likely to reflect the interest of such developed countries."159 Socialist states argued that usages should only prevail when parties to a transaction expressly agree to them in their contract. They rejected the view of Western industrialized states that usages should prevail even though not expressly stated in the contract if they could be reasonably implied. Farnsworth notes that

...usages are looked on with perhaps even more suspicion by Eastern European countries, because Eastern Europeans, being even more bureaucratic in outlook than our


159. Date-Bah, "Problems of the Unification of International Sales Law from the Standpoint of Developing Countries," p. 45.
multinationals, like to have everything in their files. There is nothing more distressing to a bureaucrat than the thought that some Englishman or Ghanaian is going to appear and claim that there is a usage that he does not have in his files.160

The Soviet delegate to the Vienna Conference stated that "usages [are] often devices established by monopolies and it would be wrong to recognize their priority over the law," while the delegate from Yugoslavia stated that trade usage "has been formed by a restricted group of countries...whose position did not express worldwide opinion."161

The Vienna Sales Convention embodies a compromise on the legal status of commercial usage. It provides that usages both explicitly agreed to and those that may be implied on the basis that such usage 'is known to' or 'ought to be known' to the parties and is 'widely known to' and 'regularly observed' by those in the trade are binding.162


162. See article 9(1), (2). Article 9, however, does not address the issue of whether usage or the Convention prevail if the two conflict. This was a sore point for socialist states which took the position that usage should not be able to override the Convention. Commentators believe that usage can in fact override conflicting provisions of the Convention on the basis of the principle of merchant autonomy. See Garro, "Reconciliation of Legal Traditions in the U. N. Convention on Contracts for the International Sale of Goods," pp. 479- 80. If this is in fact how article 9 is interpreted it will signal the elevation of custom over positive international legislation as a source of law.
It would appear that the requirements that usage should be widely known and regularly observed recognize the particular concerns of both the developing and socialist states.

The recognition of the authority of commercial usage in the Vienna Sales Convention shows that unformulated commercial custom has gained legitimacy as a source of law. Furthermore, the guidelines provided for establishing the existence of commercial custom contribute to the unification of differences in the treatment of such custom by national legal systems. The Convention provides a behavioral test of custom, similar to that employed in the U. S. Uniform Commercial Code.\(^{163}\) The test identifies repeated practices or behaviour as the essential criterion for establishing a custom, dispensing with the normative test which requires the psychological element that the practice should be generally recognized as obligatory.

The third phase thus exhibits the simultaneous influence of the principles of state intervention, international intervention, and merchant autonomy. The proliferation of international conventions and model laws that are achieving broad support and the revival of commercial custom evidences a strengthening of sources capable of generating law of universal application. While

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national legislation continues to be a significant source, and one that can frustrate the development of uniform standards, the growing legitimacy of international legislation is significant. In addition, the primacy of national and international legislation as sources of law suggest that the principles of state and international intervention are accorded greater weight than is the principle of merchant autonomy. However, the growing recognition of the legitimacy of formulated and unformulated custom as a source of law suggests that the principle of merchant autonomy is being reasserted with new vigour.

With regard to the dominant coordinative strategies the third phase has witnessed the development of new methods and strategies. Indeed, a distinguishing characteristic of this phase is the birth of the unification movement. States began with the unification of conflicts of law rules. This strategy continues to be utilized as is evident in the undertakings of the Hague Conference and UNIDROIT. However, unification efforts have expanded to include the unification of substantive rules of national commercial law. The work of UNCITRAL is central in this regard and shows that greater importance is being given to the principle of international intervention. The international unification of substantive rules of national commercial law has compromised states' abilities to establish unilateral standards and caused a weakening in the norm of state control characteristic of the
second phase. Furthermore, the revival of customary law evident in the broad support and legitimacy accorded the work of the ICC, ILA, and IMC and the growing legitimacy of commercial usage suggest a return to the norm of uniform merchant practice characteristic of the medieval law merchant.

The norm in the third phase is reliance on all coordinative strategies. Commercial actors and states, however, place different emphasis upon the various coordinative strategies. We have seen that reliance on uniform commercial custom as a coordinative strategy has been favoured by Western states who value the flexibility, adaptability, and efficiencies that custom based norms are regarded as providing.

Experience has shown that the development of uniform rules of international trade by practice is much more efficient and far-reaching than the unification of commercial law by means of international conventions. The technical process of the formation of a custom is already in itself more flexible and easier to carry out than the conclusion of an international convention which in this domain — where necessarily a modification of national law is involved — is inconceivable outside the context of ratification procedures.... And since the modification of particular legal rules which one wants to alter in order to achieve uniformity in the law of international trade, in many instances involves an attack on some general principles of national law of which the rules form part, the already considerable obstacles become insurmountable because, although one is only concerned with commercial law, one must rise
However, as discussed above, not all are in agreement regarding the merits of customary law. While recognition of the binding force of commercial custom in the Vienna Sales Convention can probably be regarded as a victory for Western states, the suspicion with which many states continue to hold for commercial custom and usage evidences weakness in the norm of reliance on uniform custom as a coordinative strategy.

The strategy of unifying conflicts of law rules is arguably supported more by states with developed systems of law. In particular, European states who have pioneered the movement for unifying conflicts systems appear to be the strongest supporters of this approach. The expansion of membership in the Hague Conference and in UNIDROIT to include broader global representation might signal a strengthening in the appeal of this strategy. However, proponents of the more ambitious strategy of unifying substantive rules of commercial law would argue that unifying conflicts rules is a minimalist approach. All that is achieved is uniformity of the rules governing what national law will apply to a transaction. Differences in

164. Kopelmanas, "International Conventions and Standard Form Contracts as Means of Escaping from the Application of Municipal Law II," p. 120.
substantive national law will remain.\textsuperscript{165} David argues that the unification of both conflicts rules and substantive rules of law is essential to the development of uniform commercial law.\textsuperscript{166} That being the case, it is indeed noteworthy that the unification of substantive rules has become the dominant strategy in the third phase of the regime. We have seen that a variety of governmental and non-governmental agencies are today engaged in the unification of substantive rules of commercial law. Unification efforts have taken the form of negotiating international conventions or formulating model laws. While there is general agreement on the need to unify substantive rules, there are differences of opinion regarding the appropriate methodology. The convention approach is regarded as producing greater certainty and maximum uniformity, but is subject to the drawback that agreement amongst states is often difficult to achieve and once in effect, conventions are difficult to amend. Model laws in

\textsuperscript{165} Kopelmanas, \textit{ibid.}, p. 119 argues that "standardization of the rules themselves [i.e. substantive rules] which are to apply to transactions of international trade thus appears, a priori, to be a more effective way of avoiding the difficulties caused by the division of the modern world into a series of political entities each of which has its own juridical norms and special commercial practices." See also David, "The International Unification of Private Law," p. 38 for the view that "a priori, it seems hardly debatable that here would be every advantage in getting legal systems to agree, if possible, on the substantive rules to be applied to international legal relations."

\textsuperscript{166} Ibid.
contrast are easier to develop, in that their application remains entirely optional, and they are particularly useful for states with undeveloped systems of commercial law and for addressing new developments. Furthermore, they are easier to amend because states are able to modify their content in enacting municipal legislation. However, this elasticity and flexibility can undermine the achievement of uniform results. Moreover, critics of the model law approach argue that conventions, and in particular those of mandatory application, offer better protection for weaker parties.\(^\text{167}\) Matteucci, while recognizing that merchant autonomy and freedom of contract are still considered to be 'articles of faith' for merchants, argues there is growing recognition of the need to protect the weaker party from those exercising monopolistic or quasi-monopolistic economic power.\(^\text{168}\) This is often cited as the reasoning behind the mandatory application of the transport conventions governing carriers liability in ocean transport.\(^\text{169}\) However, the establishment of mandatory rules is the exception and not


\(^{168}\) Ibid., p. 138.

the norm in development of uniform commercial law. We have seen that the majority of unification efforts have resulted in conventions, model laws, and uniform rules that are of optional application or whose application may be contracted out of by merchants. The inability of UNCITRAL's Working Group on the New International Order to generate texts of mandatory application attest to the continuing influence of the principles of merchant autonomy, freedom of contract, and political autonomy. It also reflects the subordination of the equity principle to the principle of the facilitation of exchange. Insofar as some states have been successful in asserting equity concerns, this has occurred within the context of a largely voluntary regime. Western developed states have succeeded in establishing the primacy of the principle which posits that the function of legal regulation is to facilitate efficient exchange. Merchants too have resisted attempts to assert the equity principle in the context of mandatory rules.

Furthermore, states favour optional rules in the form of model laws because they are less threatening to state sovereignty. The state retains ultimate control over the content of the law when enacting municipal legislation bringing the model law into effect. Indeed, the decision to unify commercial laws using model laws rather than international conventions is most often made when there is insufficient support among states for the negotiation of a convention. This was the case for UNCITRAL'S Model Rules on
Credit Transfers and Model Rules on Arbitration and Conciliation and for the work being undertaken by the Working Group on the New International Economic Order. It is curious that the principles of merchant autonomy and state intervention are both served by the creation of a permissive regime.

Thus with regard to the methodology of rule creation, developments in the third phase of the regime evidence a decline in the absolute primacy accorded national positive law as a source of law and weakening of regulation through conflicts of law systems. International legislation in the form of conventions and model laws and commercial custom have strengthened in legitimacy as sources of law, while international unification and reliance on uniform merchant practice are increasingly being utilized as coordinative strategies.

The growing strength of international legislation as a source of law and the adoption of the unification of substantive rules of law as the dominant coordinative strategy may be attributed to the permissive and voluntary nature of the regime. Under voluntary standards, states retain ultimate control over the contractual obligations of their merchants. As a result states have been more willing to participate in the creation of international conventions and model laws unifying substantive rules of commercial law.
(c) *Dispute Settlement.* During the third phase the norm is the settlement of commercial disputes in both national courts and private arbitrations. The adjudication principle and the arbitration principle are both influential. However, the growing importance accorded the latter is evident in the trend toward increasing reliance upon arbitration. Indeed, many now regard dispute settlement through arbitration to be the norm today.\(^{170}\)

For many years it was fashionable to say that international commercial arbitration had come of age. That is no longer an appropriate observation. By now it has entered a mature and sophisticated middle age. Both the crises and illusions of youth are past, and in the eyes of businessmen (although not necessarily their lawyers) the creature has developed an identity and ability to solve problems that match the needs of the critical role it plays in world commerce today.\(^{171}\)

The trend towards increased recourse to private arbitration is being encouraged by states which are participating in creating uniform and mandatory rules that provide for the recognition and enforcement of foreign arbitral awards. States are adopting legislation that curtails the power of


national courts to intervene in private arbitrations and that limits the ability of judicial authorities to set aside arbitration awards.

The reassertion of arbitration as the preferred method for settling commercial disputes reflects the growing importance attached to the principles of merchant autonomy, freedom of contract, informality, and the facilitation of exchange. "The party autonomy principle that underlies arbitration gives the contracting parties the power to fashion a remedial process tailored to their specific needs, limited only by fundamental public policy concerns."\(^{172}\) The parties to an arbitration agreement are free to choose the law to be applied and the procedures to be adopted in the settlement of disputes and to designate the arbitrator.\(^{173}\) "Arbitration is almost exclusively a creature of contract. The parties determine the content of the contractual agreement, and any requirement to arbitrate is dependent upon and subject to the will of the parties in almost all

\(^{172}\) Carbonneau, "Arbitral Adjudication," p. 36.

\(^{173}\) In a survey conducted by the American Arbitration Association in 1981 respondents indicated that the identity of the arbitrator was the most important factor in arbitration. The integrity, impartiality, linguistic ability and technical knowledge of the arbitrator were regarded as critical considerations in the choice of arbitrators. See Robert Coulson, "A New Look at International Commercial Arbitration," Case Western Reserve Journal of International Law 14 (1982): 359-71 for a report by the President of the association on the survey.
Informality in the procedures adopted by arbitrations contribute to more expeditious and less expensive dispute settlement, and thus produce greater efficiencies. Arbitrations are generally less time consuming than are court proceedings and, consequently, less expensive. In addition they are more efficient in resolving disputes involving technical issues, for arbitrators with specialized knowledge and expertise are regularly chosen. Furthermore, exchange relations are facilitated through more efficacious enforcement. As agreements to arbitrate are based on the consent of the parties, they are more likely to be recognized and enforced than are judgments rendered by national courts. Merchants who have agreed to binding arbitration are unlikely to refuse to accept the arbitral award.

In addition to compelling practical reasons, the development of an institutional context for arbitration is contributing to the strength of the arbitration norm.


Three elements converge to provide the structural reason for choosing arbitration as the method for settling transnational business disputes: (a) major multilateral treaties make arbitral awards rendered in one country enforceable in others... (b) established institutions exist to administer arbitration in an expeditious, economical and neutral fashion, and (c) official rules of procedure have been developed for the conduct of arbitral proceedings that parties to contracts can adopt or that will be applicable through simple designation by the parties of an administering institution. ¹⁷⁷

This institutional context is a product of efforts undertaken to develop and to unify arbitration law so as to address the uncertainty, inefficiency, and parochialism produced by national adjudication in the second phase of the regime.

In addition, unification efforts were spurred on by the proliferation in the early part of the twentieth century of private associations that engaged in international arbitration and developed their own arbitration rules. Graving observes that today there are "literally hundreds of institutions" engaged in commercial arbitration throughout the world.¹⁷⁸ The International Chamber of Commerce Court of Arbitration, created in 1923 is today the most successful of the arbitration associations, in terms of the volume of cases it hears and its use by states of different legal


traditions, various levels of development, and with market and non-market economies.\textsuperscript{179} It developed from a predominantly Western institution in the 1920s to one of worldwide scope.\textsuperscript{180} The American Arbitration Association, formed in 1926, is the second most heavily utilized institution for international arbitration and it utilizes a number of rules governing different types of commercial transaction.\textsuperscript{181} The London Court of Arbitration, originally the London Chamber of Arbitration, was founded in the late nineteenth century and operates under its own set of rules. Though it was once a popular venue for arbitration, it declined in popularity in the 1970s as a result of the imposition by the courts of procedural obstacles to arbitration. Legislative reforms increased its popularity and today hears about one-half the cases heard by the American Arbitration Association and about one-tenth those

\footnotesize{\begin{itemize}
\item \textsuperscript{180} In 1987 one-third of ICC arbitrations involved developing states while one-sixth were state-controlled entities. Graving, "The International Commercial Arbitration Institutions," p. 331.
\item \textsuperscript{181} Ibid., pp. 336-42.
\end{itemize}}
heard by the ICC Court of Arbitration. Significant differences in the rules applied by these and other arbitration institutions generated efforts to unify arbitration law.

Intergovernmental efforts to unify arbitration law began under the League of Nations, producing two largely unsuccessful conventions. These conventions did not attract much support outside Europe for it was felt that they were too limited in aim and objective. The ICC produced a draft convention on arbitration in 1954, but work was subsequently taken over by the Economic and Social Council of the United Nations which produced the New York

182. Ibid., p. 344.

183. These are not the only arbitration institutions, but the most significant ones in terms of international usage. The Stockholm Chamber of Commerce provides the venue for the settlement of East-West commercial disputes, and Switzerland provides the locale for many arbitrations. Other institutions that engage in international arbitration under their own rules include the International Centre for Settlement of Investment Disputes, the Indian Council of Arbitrators, the Japanese Commercial Arbitration Association, the CMEA, the ECE and the Inter-American Commercial Arbitration Commission. See P. Saunders, "Procedures and Practices under the UNCITRAL Rules," *American Journal of Comparative and International Law* 27 (1979), p. 453 for a more extensive list of arbitration institutions.

184. The Protocol on Arbitration Clauses, September 24, 1923, 27 *League of Nations Treaty Series*, 158 was limited in aim to the recognition of the validity of arbitration clauses, while the Convention on the Execution of Foreign Arbitral Awards, September 26, 1927, 92 *League of Nations Treaty Series*, 301 provided conditions governing the enforcement of awards.

Convention of 1958.\textsuperscript{186} The New York Convention imposes on states party to the convention the mandatory obligations of enforcing arbitral agreements and recognizing and enforcing foreign awards, subject to national public policy limitations. It is in force in some seventy-eight countries, including the major trading states.\textsuperscript{187}

The New York Convention assists in the enforcement of commercial agreements by placing mandatory enforcement obligations on states. The mandatory nature of a state's obligations to recognize and to enforce foreign arbitral awards is another exception to the predominantly permissive regime. However, states do retain ultimate control over the arbitration process for they can affect procedures and substantive law through the imposition of public policy considerations.\textsuperscript{188} While such state control can potentially limit merchant autonomy and freedom of contract and


\textsuperscript{187} As of January, 1989. See Graving, "The International Commercial Arbitration Institutions," p. 326. Its adherents include the United States, Japan, Great Britain, Germany, Canada and the former Soviet Union.

\textsuperscript{188} Buchanan, "Public Policy and International Commercial Arbitration," p. 513 notes that public policy "is the final parameter of the law that, while it is reflected in and often expressed by statutory and constitutional statements of law, also dictates either consent or constraint, permission or prohibition, when statutes are silent on a given matter." Public policy considerations may include matters of morality, conscionability, economic policy, and professional conduct.
interfere with efficient exchange, many states have adopted liberal approaches to the application of the public policy limitation.

While public policy provides states with a tool for external constraint upon the relative freedom of the members of the international business community to determine relationships as they see fit, it can also provide the mechanism for freeing international commercial transactions from the stringent requirements of the domestic law of the forum state or foreign states.189

There has been a decline in judicial hostility to arbitration, reflecting domestic policy concerns that reliable enforcement procedures are necessary to encourage international economic exchange.

In the United States a shift in the courts’ attitude towards arbitration occurred after the enactment of domestic arbitration law in the 1920s, which marked a change in public policy concerning arbitration. The courts came to differentiate between domestic and international arbitrations, applying considerably more restraint in intervening in the latter.190 In the United Kingdom

189. Ibid.

190. See ibid. Buchanan reviews the domestic treatment of international arbitration in a number of countries and finds a liberal approach to the recognition and enforcement of international arbitral awards in the U.S.A., Argentina and France. This is less so for Egypt where traditional values and legal rules provide obstacles to arbitration. Brazil is not party to the New York Convention and has not been a hospitable forum for enforcing awards. Buchanan was unable to assess the situation for the Soviet Union, which though party to the convention, had entertained no judicial proceedings to enforce foreign awards. For a contrary view regarding Egypt’s domestic attitudes towards
judicial attitudes also shifted in response to domestic legislation that imposed limits to judicial intervention in arbitral proceedings, however there is still resistance to the complete acceptance of arbitration. Similar developments occurred in France, although the policy shift was initiated by the courts and not the legislature. Subsequent legislative enactments have rendered France one of the most hospitable forums for enforcing arbitration awards.

Developments in the legal systems of England, the United States, and France evidence a clear 'rehabilitation' of arbitration as a parallel process of resolving domestic disputes. The redefinition of the judicial role in arbitration was central to the reevaluation in each country. Rather than a competitive relationship, the various domestic arbitration laws mandated collaboration between the judicial arbitral processes, with the public process lending the assistance of its coercive jurisdictional authority where necessary. In England, this phenomenon principally involved a lessening of judicial review powers.... In the United States and France, the legislation expressly established a cooperative interrelationship between the courts and arbitral tribunals.


192. Ibid., pp. 53-7.


A number of other countries are showing a greater willingness to recognize and enforce foreign arbitral awards. The New York Convention was brought into force in the People’s Republic of China in 1987, in Algeria in 1989, and in Canada in 1986. Many other states modernized their arbitration laws in the 1980s, creating legal environments more hospitable to arbitration.

The shifts in domestic policies concerning arbitration were a response to the tremendous growth in commercial transactions and the unprecedented expansion in commercial litigation. Domestic courts were simply unable to respond adequately to the increased volume of commercial cases and to the increasing complexity of commercial transactions. In addition, most states recognized the economic benefits that would flow from reducing the transaction costs of enforcement and from encouraging stability in the enforcement of property rights. Finally,


196. Canada, France, Italy, Belgium, the Netherlands, Switzerland, Australia, Nigeria, Cyprus, Djibouti and Spain. See ibid., p. 579.

197. See Carbonneau, "Arbitral Adjudication," for a discussion of many of these factors in reference to shifts in the domestic policies of the United States, Great Britain, and France.
it was generally felt that commercial disputes seldom raised issues of public policy and when they did, the public policy limitation could be invoked by a domestic court.

For many states modernization was also prompted by unification initiatives undertaken by UNCITRAL. The unification of arbitration law was made part of UNCITRAL's programme of work when the Commission was initially created. The Commission adopted UNCITRAL Arbitration Rules in 1976 after "extensive consultation with arbitral institutions and centres of international arbitration."²⁰⁰

The special contribution of the UNCITRAL Arbitration Rules is their appropriateness for worldwide use. They offer a well balanced and modern set of arbitration rules, prepared with the assistance of arbitration experts from all parts of the world. They may also be particularly welcomed by developing countries who were vigorously represented in the drafting and strongly supported the preparation of such rules by an organ of the United Nations.²⁰⁰

The UNCITRAL Arbitration Rules have achieved "world-wide recognition and application, primarily due to the text's reliance upon the principle of party autonomy and purposeful consideration and incorporation of international consensus and opinion."²⁰⁰ The rules may be invoked in arbitrations

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held by the ICC Court of Arbitration, the London Court of Arbitration, and the American Arbitration Association. They are used widely and have attracted the support of the developing countries.\footnote{201} UNCITRAL also produced uniform rules on conciliation\footnote{202} after consulting with the ICC and the International Council for Commercial Arbitration (ICCA), which is a private association of arbitration experts from thirty countries.\footnote{203} Like the arbitration rules, the conciliation rules are of voluntary application. However, conciliation, unlike arbitration does not involve adversarial procedures or produce binding awards.

UNCITRAL's most ambitious undertaking in the area of arbitration, however, is the Model Law on International

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\footnote{201. Derains, "New Trends in the Practical Application of the ICC Rules of Arbitration," p. 43. The author notes that the growing support of developing countries for arbitration is evident in the creation of arbitration centers in Kuala Lumpur and Cairo. See also, Enein, "Arbitration Under the Auspices of the Cairo Regional Centre for Commercial Arbitration." The rules are also being reviewed by CMEA countries. See V. S. Pozdnjakov, "Commercial Arbitration in CMEA Member Countries," \textit{International Tax and Business Lawyer} 4 (Fall 1986): 272-9.}


Commercial Arbitration, adopted in 1985. The model law "is intended to serve as a model of domestic arbitration legislation, harmonizing and making more uniform the practice and procedure of international commercial arbitration while freeing commercial arbitration from the parochial law of any given adopting state." The model law embodies the merchant autonomy principle in the freedom it accords parties "to tailor the 'rules of the game' to their specific needs." For example, the parties are free to specify arbitrable subject matter and to choose institutionalized arbitration and rules, the procedures governing the conduct of arbitrations, and the applicable law. Party autonomy is also reflected in the strict limits placed on judicial intervention into the arbitration process. The "approach of the model law, which allows limited prompt recourse to the court during arbitral proceedings, but simultaneously permits the arbitration to go forward, represents a balance between the potential for delay through dilatory tactics of a recalcitrant party, and the futility and high costs of arbitral proceedings in which


206. Ibid., p. 329
the award is ultimately set aside by the court."\(^{207}\) The informality principle is reflected in the wide powers over procedural matters given to the arbitration tribunal. In tandem with the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, the model law provides a comprehensive and a voluntary regime for informal, expeditious, and impartial dispute resolution and enforcement.

Many states are considering the adoption of the UNCITRAL Arbitration Rules and Model Law. Canadian jurisdictions have enacted legislation bringing the rules and model law into effect,\(^{208}\) while the United States, which participated in the drafting of the model law and was satisfied with the final product, is considering its implementation.\(^{209}\) Bulgaria, Cyprus, Egypt, Hong Kong, Hungary, India, Singapore, Great Britain, and Germany are also considering acceptance of the model law, while the Netherlands has enacted legislation based upon the model law.

\(^{207}\) Ibid., p. 331.


It is believed that the flexibility resulting from the adoption of a model law rather than a convention, will facilitate its broad acceptance. Indeed, the lack of support sufficient to bring the European Convention on International Commercial Arbitration of 1966 into force is attributed to the inflexibility it accorded states in its implementation. However, the drawback of the model law approach is that uniformity may be compromised by the enactment of modifications to the model law. This has in fact occurred in Canada where various jurisdictions have enacted implementing legislation modifying the model law.

The strengthening of the arbitration norm in the third phase of the regime is thus evident in increased reliance on arbitration as the preferred method for settling commercial disputes and in the proliferation of arbitration institutions and rules providing an institutional context for dispute settlement. The norm of state control has weakened as the ability of national courts to intervene in arbitration proceedings and to set aside arbitration awards has been curtailed by legislation.


211. See ibid., for a discussion of the convention versus model law approach and the pitfalls of the mandatory language used in the European Convention.

The growing trend among states, including the major commercial states, to accept limits on the abilities of national courts to intervene in the arbitration of commercial disputes reflects significant pragmatic considerations. The inability of national judicial systems to deal with the qualitative and quantitative expansion of commercial relations and litigation in a cost-effective manner has been significant in reordering domestic attitudes towards arbitration. In addition, the general value that all states placed upon commercial prosperity and their belief that arbitration produces greater wealth through reducing transaction costs and ensuring the stability of exchange provided common foundations for the generation of the arbitration norm.

B. Summary

This review of the third phase in the evolution of the regime discloses considerable strengthening in the universality of the law merchant. While states continue to exercise significant control over international commercial transactions, their influence is being tempered by a commitment to unify standards, recreating the notion of a *jus commune*. Moreover, in some areas states are contributing to the creation of a permissive, facilitative regime. The unification movement began as a predominantly European exercise, but has now attracted global
participation. Most states support the movement, though not all are in agreement as to the weight to be given to competing regime principles. Efforts by developing states and other states to assert the primacy of the equity principle have been unsuccessful in changing the fundamental principles of the regime and only modestly successful in changing regime norms and rules. Developed, predominantly Western states, have succeeded in strengthening rules and norms reflecting liberal, capitalist values. These values place priority on the principles of merchant autonomy, freedom of contract, informality, and the facilitative nature of the exchange relationship. Moreover, while states have managed to overcome obstacles posed by tensions between the common law and civil law, these tensions have not generally involved conflict over fundamental principles.

With regard to the substantive dimension, the norm of state control has remained particularly strong in the area of liability for defective goods. In this area there has been little support for the creation of international regulatory standards. States have simply been unwilling to relinquish control over products liability, and thus the regime embodies rather limited standards governing liability for nonconforming goods. In the case of insurance, it would appear that the norm of merchant control and not state control is blocking the emergence of international insurance standards. Insurance companies enjoy considerable independence in regulating insurance matters.
The norm of contractual and market prices remains strong. States asserting the primacy of equity concerns have succeeded in blocking the entrenchment of an open price rule that they believe strengthens the norm of price setting by sellers when prices are underspecified. However, it is unlikely that they have succeeded in articulating a new norm given the ambiguity of the rule and its lack of support in jurisdictions like the United States. Developing states have succeeded in effecting a rule change regarding notice periods for defective goods claims and limitations periods. However, both concessions were made within the context of conventions of voluntary application.

The regime exhibits moderate strength in the regulation of transport costs and liabilities. The rules regulating the passage of risk have been unified and, with the exception of the rule governing the passing of risk for goods sold in transit, attract broad support. The ICC's Incoterms have been unified and modernized in response to advances in transport techniques and documentation and are widely used in regulating transport costs and liabilities. Significant weakness, however, is evident in the liability rules governing bills of lading. States have been unable to agree upon uniform rules, reflecting the lack of a normative consensus concerning the allocation of risks between cargo and carriers. The major carrier states continue to support the traditional regime standards limiting carrier liability under the Hague and Hague-Visby Rules. The Hamburg Rules,
more favourable to cargo, have attracted insufficient support to bring them into effect. In contrast, the norms governing financial and credit arrangements have strengthened considerably. Diverse national standards have been unified and merchants continue to develop new techniques and customary rules. The scope of the regime has broadened to address new forms of financial transactions, generating new norms and standards.

The procedural dimension exhibits considerable strengthening in regime norms. Secondary rules or rules of recognition have developed identifying legitimate agents of law creation and enforcement. A number of intergovernmental and non-governmental organizations capable of generating standards of broad application emerged in the third phase of the regime. There is widespread recognition among commercial actors of the legitimacy of these formulating agencies. Non-governmental organizations, most particularly the ICC, are able to generate rules of near universal application. Intergovernmental organizations, in particular UNCITRAL, are creating international positive law in the form of conventions and model laws that are attracting great interest and support. The creation of UNCITRAL was instrumental in expanding the unification movement beyond its predominantly European origins. The participation of developed, developing, socialist, common law, and civil law states in UNCITRAL has enabled unification efforts to bridge significant differences.
The most significant development, however, has been the participation of the United States. We noted earlier that significant limitations on the ability of the Hague Conference and UNIDROIT to generate standards of universal appeal was their essentially European and civil law orientation. The United States took little interest in their unification efforts in the late nineteenth and early twentieth centuries. A shift in U. S. policy occurred, however, as a result of domestic unification efforts and in response to the fear that their interests would be inadequately protected if they did not begin to take an active role in the unification movement. As a result, the United States took a leadership role in the drafting of the various UNCITRAL conventions and model laws. The United States supports the creation of a permissive, facilitative regime, embodying free market principles. The influence of the United States on the drafting of the Vienna Sales Convention is evident in the voluntary application of the Convention and in its fidelity to the principles of merchant autonomy, freedom of contract, and the facilitative nature of exchange.

Other states, like Canada, have increased their interest and participation in creating regime standards in response to the increased interest exhibited by the United States. Canada is now active in the unification movement as a result
of increased U. S. involvement. Canadian trade experts believe that Canada has no choice but to participate given that the United States as its major trading partner will draw Canada into the international regulatory framework. Canada, along with the United Kingdom and countries of Western Europe, shares in the commitment to the creation of regime norms and rules premised upon liberal, capitalist values.

The growing legitimacy of international legislation as a source of law evidences a strengthening of the procedures for creating uniform law. Furthermore, the predominantly voluntary and optional character of the conventions and model laws shows the influence that the Western developed states, which favour a permissive and suppletive regime, have had on developing regime standards. This is evident as well in the growing legitimacy of commercial custom as a source of law. Though regarded with suspicion by developing states and not welcomed by socialist states, commercial custom is being accorded greater force as a source of law.

Further strengthening in the procedural dimension is evident in the acceptance of the unification of substantive commercial law as a developing norm in the coordinative strategies adopted by states. Though states continue to

213. See Cutler, "Canada and the Private International Trade Law Regime."

coordinate their commercial relations through unifying conflicts of law rules, unification efforts have extended to include matters of substantive law, signalling a weakening in the norm of state control prevalent during the second phase of the regime. In addition, the growing legitimacy and efficacy of international arbitration in dispute settlement are significant developments. They signal a strengthening of the norm of international control as states relinquish the virtual monopoly over dispute resolution held in the second phase by submitting to mandatory limitations on their abilities to intervene in the arbitration process. Furthermore, states are now participating in the assertion of the arbitration principle as they submit to mandatory recognition and enforcement requirements.

We will next recapitulate the significant developments in the regime and assess the explanatory capabilities of different theoretical approaches.
CHAPTER VII

CONCLUSION: REGIME EVOLUTION AND ALTERNATE THEORETICAL PERSPECTIVES

The preceding chapters show that the private trade law regime has been in existence for a millennium. The regime originated in merchant customs and has endured changing patterns of political authority, different conceptualizations of the world, and transformations in international economic relations. While these developments have influenced the strength and normative structure of the regime, the regime exhibits considerable continuity in fundamental principles. This chapter will recapitulate the major trends in the development of the regime, identifying significant continuities and discontinuities that require explanation. It will then evaluate the explanatory capabilities of the theoretical perspectives selected for review.

A. Regime Origin, Strength, and Nature

The regime originated in merchant custom and was transmitted throughout the European trading world through merchant practices in the first phase of its development. At this time, the merchants operated with significant autonomy. Local political and religious authorities exerted minimal positive influence on the generation or the content of regime norms. This autonomy largely disappeared in the second phase as states absorbed the law merchant into
national systems of law. During the third phase, the autonomous influence of the law merchant is being reasserted, but through the agencies of states and international organizations, and subject to limitations imposed by concerns of national sovereignty and political autonomy.

The study shows that there is a significant distinction between the importance of the regime and its strength, in terms of the specificity and comprehensiveness of regime norms and rules. The private trade law regime is of great importance in the facilitation of commerce. However, regime norms and rules are formulated at a high degree of generality and allow considerable flexibility in their application. Indeed, the durability of the regime derives from its predominantly voluntary and permissive rules structures. In general, the regime has received the strongest support in areas subject to permissive, facilitative regulation and weakest in areas subject to mandatory controls. Support tends to be stronger when merchants exercise considerable autonomy and when merchant customs are dominant. Inversely, weakness is associated with state intervention and the development of national legal standards. Finally, the regime exhibits greater strength with the involvement of international organizations. As we shall see, however, there are significant discontinuities in these general trends.
During the first phase, the dualistic system of regulation, which differentiated between domestic and international commercial transactions, reflected the peculiarities of the medieval power structure, the influence of Christian conceptions of the world, and probably a modest volume of international economic transactions. While the regime exhibited considerable strength in both the substantive and the procedural dimensions, its strength was greater in areas where local authorities were unable or unwilling to intervene. Thus, greatest strength is evident in the substantive dimension in the areas of transport, insurance, and financial transactions. These transactions were subject to permissive rule structures, were associated with a high degree of merchant autonomy, and were regulated almost exclusively by merchant custom. In contrast, the norms governing prices, defective goods, and interest charges, which embodied Christian notions of morality and the interests of local political authorities, were weaker. In these areas local mandatory regulations served to temper merchant autonomy somewhat. In the procedural dimension, the strength of the norms governing the locus of regulation, the methodology of rule creation, and dispute settlement were associated with permissive rules, merchant autonomy, and reliance on merchant custom.

During the second phase, the disappearance of the dualistic system of regulation reflected the development of modern nation states and the extension of national control
to most international commercial transactions. States became more willing and more capable of controlling international transactions. This reflected an enhanced understanding of the political dimension of trade. This understanding was caused, in part by the increased volume in international economic transactions generated by colonial expansion and, in part by the advent of capitalist and mercantilist thought. These developments were accompanied by a general weakening in the regime. The regime weakened most in areas subject to mandatory state regulations and in areas where merchant autonomy and the influence of merchant customs were the most severely curtailed. Regime norms weakened most in the procedural dimension as merchant autonomy and the influence of merchant customs were subordinated to state control and national legislation. Less weakening is evident in the substantive areas of transport, insurance, and financial transactions where merchant customs remained influential and permissive rules remained the norm. In these areas, while national variations in rules emerged, the continuing influence of merchant custom and the adoption by states of the same fundamental principles served to maintain significant uniformity. The norms governing prices and products liability strengthened, as states adopted permissive rule structures governing sales contracts. In these areas, states did not limit merchant autonomy, but instead, encouraged it by entrenching the principles of freedom of
contract and the sanctity of contract in their national legal systems. These developments reflect changes in the nature of the regime as states came to adopt free market principles as the foundation for the regulation of commercial exchange.

In addition, in the second phase there was a differential weakening in regime norms among states. In general, common law jurisdictions experienced more weakening in the universality of standards and in the influence of merchant custom than did the European, civil law jurisdictions. This was particularly so in the procedural dimension where merchant autonomy and the influence of custom were severely curtailed by common law jurisdictions. In the substantive dimension, as well, peculiarities in the common law rules governing prices and products liability resulted in differential weakening in regime norms.

In the third phase, the development of international organizations engaged in the unification of commercial law and conceptions of a global economy, generated by an unprecedented quantitative and qualitative expansion of international economic relations, have accompanied an overall strengthening of the regime.

The regime continues to be strongest in areas where the rules are permissive, where merchant autonomy is strongest, and where merchant customs remain influential or have increased in influence. This is the case for the regulation of prices, financial transactions, and certain transport
issues. The regime tends to be weaker where states have intervened to establish mandatory national laws, as in the area of products liability and certain transport issues. In addition, the regime tends to be stronger in areas where international organizations are active in the development of regime standards. This is most evident in the procedural dimension. It is notable that the weakness in the norms governing insurance is accompanied by the general absence of international regulatory efforts in the area.

However, there are some significant discontinuities. In the area of dispute settlement, the arbitration norm is very strong, in spite of the existence of mandatory national laws. In fact, the arbitration norm derives its strength from the mandatory obligations undertaken by states to recognize and to enforce foreign arbitral awards. In addition, the norms governing coordinative strategies have strengthened with increased state involvement in the unification of substantive national commercial laws. These developments signal a significant decline in states' attachment to the political autonomy principle and important changes in their views regarding the purposes of commercial regulation.

We will turn now to consider the ability of the structural realist, functional, and sociological perspectives to account for the strength and nature of the regime and these important continuities and discontinuities.
B. Evaluating Theoretical Perspectives

1. Phase I

Structural realism is of limited assistance in explaining the origin of the regime. Its hypotheses are not really disproved, but then neither are they supported. There is no evidence that any state or group of states imposed or created the regime (Hypothesis A. 1). As we have seen the regime developed out of merchant custom and practice. The main locus of regulation was the merchant community, while the main source of law was merchant custom. Nor is there any evidence that the nature and scope of the regime reflected the interests of a hegemonic state or a group of states (Hypothesis A. 2) or that the regime changed in response to changes in the capabilities and preferences of a hegemon or a coalition of powerful states (Hypothesis A. 4). This should come as no surprise because structural realism assumes the existence of a system of sovereign states -- a system that was not yet in existence. The concept of the underlying power structure must therefore be adapted to reflect medieval conditions of authority. Political authorities, such as they existed in the medieval period, had limited influence on the regime. This was a result of both their inability and unwillingness to regulate the activities of merchants engaged in international trade. They lacked sufficient resources to regulate international transactions, but were also reluctant to do so for they received important economic benefits from the activities of
foreign merchants. Furthermore, international trade was relatively modest in volume and thus did not engage the attention of the local authorities significantly. There is little evidence that they were concerned about political autonomy or relative gains in relation to foreign trade in any major way. (Hypotheses 3 (a) and (b)).

There is evidence to suggest that the strength of the regime derived more from the absence of political authority and not from its presence. The strength of merchant autonomy, the efficacy of merchant custom, and the permissive character of the regime were made possible by the hands-off approach of local authorities.

Moreover, while there is evidence that the growth of towns and cities as autonomous political entities certainly facilitated the transmission and codification of regime norms, their origin lies elsewhere, in long established custom and usages. This touches upon another important limitation of structural realism that is of more generalized relevance to the regime. Keohane has shown that structural realist analysis is informed by rationalist and utilitarian assumptions.1 Structural analysis is rationalistic in its commitment to the utilitarian logic of rational choice theory, exchange theory, game theory, and microeconomics, which assume that cooperative or regime governed behavior can be accounted for by reference to states' rational

1. "International Institutions."
calculations of interests and utilities. Furthermore, it is positivistic in approach.\(^2\) The positivism derives from the \textit{a priori} assumption regarding the objective influence of system structure on the determination of state interests and the commitment to positivist epistemology. Ashley observes that structural realist theory "is theory of, by, and for positivists."\(^3\) It is positivistic in its reference to the "'received model' of natural science" and in its "naturalist bias" which holds that the "truth of discourse lies in the external object."\(^4\)

The realist image of international anarchy, when coupled with these rationalist, utilitarian, and positivist premises and orientations, inspires a particular way of thinking about and defining what constitutes authority and rule. It evokes the power or interest-based theory of law and organization embodied in legal positivism and command theories of law. Hart notes that while the term legal positivism, "like most terms which are used as missiles in intellectual battles, has come to stand for a baffling multitude of different sins," it is comprised of three distinct doctrines which constitute the "utilitarian


tradition in jurisprudence." These doctrines relate to the separation of law and morals, the value of analytical inquiry into legal concepts and the command theory of law. It is the third that is of immediate relevance to this discussion. The Austinian view of authority and rule as the command of a sovereign backed by force (the command theory of law) underlies the characterization of the international system as anarchic, or lacking centralized authorities for rule creation and enforcement. Reliance on the domestic analogy, wherein the binding source of law is said to emanate from the enforcement powers of the state, results in the characterization of the international system, which is said to lack such enforcement mechanisms, as anarchic. Simply put, there is no sovereign to issue or to enforce the


6. Hart identifies the following five different meanings of legal positivism: 1. the contention that laws are commands of human beings; 2. the contention that there is no necessary connection between law and morals or law as it is and ought to be; 3. the contention that the analysis of legal concepts is worth pursuing and is distinguishable from historical and sociological inquiries into law or critical appraisals of law; 4. the contention that the legal system is a closed logical system in which correct legal decisions can be deduced by logical means from predetermined legal rules without reference to social aims, policies or moral standards; and, 5. the contention that moral judgments cannot be established or defended as statements of facts can by rational argument, evidence or proof. Ibid., p. 601, note 25.

7. For discussion of the inappropriateness of reliance on the domestic analogy see Kratochwil, Rules, Norms, and Decisions, chap. 1.
law. Furthermore, the rationalistic and utilitarian premises of legal positivism, embodied in the command theory of law, limit the definition of law to rules that may be traced in origin to positive acts of will, as embodied in legislation.\(^8\) The positivist tenet that states are bound only by laws to which they have agreed, as evidenced by international treaties and conventions, reflects the operation of the will or consent-based theory of obligation which emphasizes formal authority structures. The tendency to equate rule with formal authority and with the command theory of law produces two unfortunate results. Firstly, it limits rules to commands, prohibitions, and injunctions, overlooking a host of other rule structures that operate not as constraints, but as permissive, commitment, facilitative, and empowering rule structures. Hart has shown that even in the context of domestic legal systems the command theory of law "omits some of the most characteristic elements of law," embodied in facilitative and secondary rules.\(^9\) Secondly, it obscures the operation of informal authority structures, as Onuf and Klink argue, conflating "formal and substantive definitions of anarchy."\(^10\) These limitations pose serious

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8. See von Wright, *Norm and Action* for a discussion of the "will theory of norms" as the classical theory of norms which underlies command theories of law and which traces the ontological status of prescriptive norms (or commands) to the will of the state.


drawbacks to the utility of structural explanations in accounting for the origin of the regime in merchant customs and practices and in accounting more generally for the evolution, nature and strength of the regime. As we have seen, permissive, and facilitative rules are the norm in private international trade law. While the trade regime does consist of some mandatory rules and injunctions, the majority of commercial regulations consist of model codes and laws designed for the optional use of parties in commercial transactions. Furthermore, the critical roles that commercial custom and the practices of private actors have played in the origin, evolution, and strength of regime standards are simply not captured by the notion of acts of positive law creation. Customary law and informal commercial practices that have evolved over time simply cannot be traced in origin to an act of will or to formal sources of law.

The explanatory capability of structural realism is further undermined by the longevity of the regime. The regime exhibits considerable longevity, in spite of significant changes that occurred in the authority structures of the medieval phase with the growth of cities and towns and the establishment of centralized political authorities (Hypothesis A. 5).

The sociological approach best captures the genesis of the regime in commercial custom and the critical role played
by private actors. There is evidence that the regime was premised upon a transnational consensus amongst merchants regarding the desirability of the regime, its purposes, and the procedures for implementing it (Hypotheses C. 1 and 2). Merchants shared a commitment to legal regulation, but of a particular sort, which in turn reflected shared values and knowledge about the world. By developing permissive and facilitative norms that gave maximum play to merchant autonomy, and at the same time reduced the costs of exchange and produced greater certainty, merchants showed a commitment to the values of certainty and efficiency in exchange. International merchants were able to operate with significant autonomy from the restraints imposed by the local, religious morality.

In addition, the belief that the interests of merchants (i.e., certainty and efficiency) could be best achieved through rules that imposed minimal formal requirements, that encouraged the expeditious conclusion and enforcement of agreements, and that permitted great flexibility evidences both ideological and epistemological consensuses. It is historically incorrect to interpret these consensuses in the context of modern liberal and neo-liberal theory. Such theory emphasizes the value of markets in producing the efficient allocation of resources and limits human intervention on ideological, normative, and epistemological
grounds to the correction of market failures.\textsuperscript{11} However, the symmetry in approach and rationale is undeniable and leads directly into the relevance of the functional approach to regimes.

Functional analysis shares with structural analysis a commitment to positivism and to rationalist and utilitarian premises.\textsuperscript{12} As such, the former is subject to the criticisms made above regarding the inability of positivist methodology and rationalist and utilitarian assumptions to account for the origin of customary norms. Commercial practices that have evolved over time cannot be easily reduced to acts of choice or design contemplated by the model of the rational, utility maximizing actor. However, commercial actors have supported reliance on commercial customs and practices on the grounds that such practices respond to commercial needs and efficiency concerns.

There is evidence to support the hypothesis that the regime developed in response to transaction costs that confront traders irrespective of the historical context or period (Hypothesis B. 1). The possibility of cooperating to achieve joint gains from the correction of market failures does not require the existence of liberal or neo-liberal

\begin{itemize}
  \item \textsuperscript{11} For the clearest statement of the virtues of a liberal, free market approach to economic regulation see Hayek, \textit{Law, Legislation and Liberty}.
  \item \textsuperscript{12} Keohane, "International Institutions" and Kratochwil and Ruggie," International organization."
\end{itemize}
ideology and epistemology. Nor need it be premised upon the existence of any particular political structure. Indeed, economic theories of law utilize transaction cost analysis to explain the generation of the legal institutions of private property and contract in primitive societies.\textsuperscript{13} Such theory posits that customary law emerges to address the market failures accompanying commercial exchange.

The adoption of uniform standards and limited liability in the areas of transportation, finance, and insurance were believed by merchants to facilitate transactions by lowering transaction costs, in spite of the absence of liberal and neo-liberal economic theories. Furthermore, the development of a private enforcement system facilitated the expansion of commerce by providing merchants with the security that their agreements would be honoured and by reducing the transaction costs of enforcement.

There is also evidence to support the hypothesis that organizations facilitated the conclusion and monitoring of agreements (Hypothesis B. 1 (c)), although as we have seen, the law merchant institutions were transnational and not international. The network of merchant courts and the activities of consuls and notaries, who accompanied merchants in their travels, provided a transnational institutional context for regulating commercial relations.

Further evidence shows that the regime developed in response to increases in the volume of commerce and that regime norms evolved in response to changing commercial practices (Hypothesis B. 2). New techniques were developed to facilitate the transport, financing, and insurance of goods as commerce expanded in scope and in volume.

Finally, the regime exhibits considerable normative continuity during the medieval phase, in spite of significant changes brought about by the emergence of centralized political authorities and the growth of towns and cities (Hypothesis B. 3). The primacy accorded the principles of merchant autonomy, the sanctity of contract, the facilitation of exchange, and the efficacy of merchant custom and arbitration provided uniformity in the normative structure. The efficiencies generated by custom-based regulation and by the merchants' private enforcement system go a long way in accounting for the origin and the strength of the regime in the medieval phase.

2. Phase II

Structural analysis assists somewhat in explaining the nature of the regime in the second phase and important changes from the first to second phases. The decline of the dualistic system of regulation and the extension of state control to all areas of commercial activity are generally reflective of the growth of the states system and concerns of state building. They also reflects the declining power
of the church in commercial matters. There is evidence that
the advent of the states system, premised on sovereignty and
political autonomy as the fundamental constitutive
principles governing international relations, weakened the
regime and proved resistant to the generation of
international standards. The emphasis of states on the
creation of positive law undermined the universalizing role
of commercial custom, while the development of national
systems of regulation in the form of national conflicts of
laws rules resulted in the application of national laws to
international commercial transactions. Both developments
reflect the operation of the political autonomy barrier
(Hypothesis A. 3 (a)).

However, the power structure alone is inadequate for
capturing the complexity of the regime in the second phase.
Dominant values and ideas had a key role in changing the
attitude of political authorities. The development of
capitalist business techniques and mercantilist theory
highlighted the importance of economic sources of national
power. In addition, the increasing volume of international
commercial transactions probably heightened awareness of the
political dimension of international trade. While there is
no evidence that a hegemon or a group of states imposed the
regime on others, we saw that the United Kingdom was
instrumental in the birth and transmission of the values
associated with liberal political economy. These values
were of critical importance in establishing the nature of
state controls and in strengthening the permissive and facilitative nature of commercial law.

Enhanced recognition of the role of international commerce in the determination of national power and in the achievement of political autonomy and the development of liberal political economy as the normative and theoretical foundation for state regulation suggest that the sociological approach is also instructive. The coupling of the transnational value of sovereignty with the transnational commercial values embodied in liberal political economy produced what Ruggie refers to as a fusion of power and social purpose.\textsuperscript{14} States, as the legitimate agents of law creation, embraced liberal, capitalist values as the ideological, normative, and epistemological premises for commercial law.

The functional approach declines somewhat in explanatory force, but is still of considerable value. The movement in the second phase toward the development of national commercial rules reflected a desire for more clearly defined standards governing the exchange relationship. We saw that the law merchant was incorporated into the common law in part to address the need for an officially developed legal system and in part as an effort to facilitate exchange by generating more clearly defined standards.

\textsuperscript{14} "International regimes, transactions, and change," p. 198.
standards governing contracting and a more efficacious dispute settlement system. States became involved in dispute settlement and enforcement in order to generate greater economic welfare by lowering the transaction costs of enforcement (Hypothesis B. 1 (a)). However, uniformity in rules declined and the regime weakened as states narrowed the influence of commercial custom and adopted national systems of conflicts rules. In spite of the continuity in commercial need concerning the desirability of correcting market failures, differences in rules emerged causing a weakening in the regime. This raises an important limitation posed by the causal weakness of functional theories. Functional theories are unable to explain why regime standards originate in some areas but not in others or why the regime weakened differentially.

The overall weakness of the regime might be explained in terms of the colonial patterns of trade. It is possible that critical market failures did not arise when trade was conducted within colonial spheres under similar legal systems. Furthermore, considerable continuity in the underlying principles of the sanctity of contract, freedom of contract, and the facilitation of exchange probably served to address the most significant market failures. The

15. For these and other criticisms see Haggard and Simmons, "Theories of International Regimes," and Keohane, "International Institutions." For a rejoinder to criticisms of functional theories see Zacher, "Toward a Theory of International Regimes."
adoption of the will theory of contract, premised upon free
market philosophy, provided the foundation for a consensus
regarding the virtues of liberal political and economic
values and shows the intimate relationship between the
insights afforded by the functional and the sociological
perspectives.

Differential weakening was evident as uniformity
decided more in the United States and in England than on
the Continent. While legal theorists who believe that the
common law system is inherently more efficient than a
statute-based system would probably argue that Anglo-
American law developed adequate responses to commercial
needs and thus obviated the need for the development of
further standards, we have seen that this was not the case.
Indeed, the emergence of different national rules generated
a movement to unify commercial laws and practices. It is
more likely that peculiarities in the development of the
common law, associated with the incremental development of
law through judicial decision, allowed more scope for the
generation of local particularisms. In comparison, the more
rationalized and comprehensive approach involved in the
codification initiatives of the civil law tradition probably
left less room for the emergence of local differences.

16. See for example Posner, "The Ethical and Political
Basis of the Efficiency Norm in Common Law
and P. H. Robin, "Why is the Common Law Efficient?"
3. Phase III

Developments in the third phase of the regime provide partial support for structural realism. There is some evidence that the United States was able to influence the regime disproportionately. We saw that once the United States began to participate in the unification movement, it played a leadership role in development of regime standards. This is most evident in the development of the rules governing international sales transactions. As was noted in Chapter VI, the Vienna Sales Convention is considered to bear the greatest likeness to U. S. commercial law (Hypothesis A. 2). The preference of the United States for a permissive, voluntary regime is shared by the major Western commercial states and forms the foundation for regime standards in most areas. However, there is no evidence of explicit imposition or coercion. In instances where the United States came into conflict with other states the matters were resolved through accommodating the divergent views or developing ambiguous rules. In some cases, differences were left unresolved. Accommodation occurred in most disagreements between the United States, as a common law jurisdiction and European states, as a civil law jurisdictions. Many significant differences between the common law and civil law were resolved through the development of rules that blended the two systems. This occurred in the rules governing sales law and limitation
periods. Accommodation also occurred in the dispute over the status of commercial custom as a source of law. Other disputes between the LDCs and countries with planned economies were not resolved so smoothly. The inability to develop a normative consensus resulted in significant ambiguity in the rules governing open price contracts and goods sold in transit. In the case of the liability of transport carriers, disputes between carrier and cargo states were not resolved at all, resulting in the existence of three different sets of rules. However, the fact that the United States could not dictate or impose its position on open price contracts or enforce strict notice periods for the exercise of legal claims arising out of sales transactions shows that there are limitations to its influence. In addition, there is evidence that the United States is moving towards the position adopted by European states in reference to the terms of trade in transport agreements.

There is evidence to support the view that the political autonomy and the relative gains barriers have inhibited the development of regime norms (Hypotheses A. 3 (a) and (b)). Concerns of political autonomy blocked the development of significant products liability rules, while the relative gains problem posed obstacles to agreement regarding the various transport conventions and the development of unambiguous rules governing open price contracts and the passage of risk for goods sold in transit.
In addition, concerns of political autonomy have had an impact on the procedural dimension. The norms governing the locus of regulation indicate that states retain considerable legitimacy as agents for the creation of commercial law. Moreover, while states now participate in efforts to unify their national substantive laws, the preference of many developed states for rules of optional application has inhibited the development of mandatory obligations. In general, Western developed states have been most resistant to the development of mandatory standards, in the belief that such standards pose unnecessary limitations on their autonomy.

The norms governing dispute settlement constitute a major exception to the largely voluntary nature of the regime and pose difficulties for structural realism. The view that the institutional barrier inhibits cooperation in the development of regime norms (Hypothesis A. 2 (c)) is refuted by the existence of institutional arrangements which have facilitated the development of mandatory obligations governing international arbitration. States have traded off significant autonomy over the resolution and enforcement of commercial disputes in order to achieve other goals. These include greater economic welfare generated by a more efficient and efficacious enforcement system.

There is some evidence that changes in the regime were accompanied by changes in the preferences of the United States (Hypothesis A. 4). The movement toward a global
regime and the increased strength in the regime were accompanied by the increased interest, participation, and support of the United States. The unification movement was once a regional and an European movement, but became a global undertaking with U. S. participation in UNCITRAL. However, it is difficult to determine whether U. S. support alone has resulted in the strengthening and universalizing of regime standards or whether institutional factors are also significant.

There is only partial support for the position that international regimes are transitory and temporary (Hypothesis A. 5). The private trade regime exhibits considerable longevity, but its strength has varied over the three phases in its evolution. The increased support of the United States for the unification movement no doubt contributed to a strengthening in uniformity of rules. However, uniformity of regime principles preexisted both the unification movement and the participation of the United States in the movement.

Finally, the critical role that private actors have played in the development of the regime in the third phase and the important influence that domestic political considerations have had on the nature of the regime undermine the explanatory capabilities of structural realism. We have seen that private merchant associations today play a key role in developing and determining the nature of regime norms. Moreover, the enhanced recognition
of custom as a source of law gives further weight to the influence of private merchant associations in the articulation of regime norms. Finally, it is evident that domestic political considerations have often constrained states' abilities and willingness to submit to regime discipline.

The sociological approach assists in explaining the continuity in regime principles and the role played by private actors. Continuity in the primacy of the principles of freedom of contract, merchant autonomy, the sanctity of contract, and the facilitation of exchange may be attributed to the unity provided by shared values of economic liberalism. This is particularly so for the Western, developed states. This consensus is embedded in Western theories of contract law and forms the normative, ideological, and epistemological foundations for the modern regime. Private actors have been instrumental in transmitting these principles throughout the world in their contractual practices. This consensus is gaining strength with a heightened consciousness of the need to address new management problems generated by the globalization of commercial relations. Contemporary regime norms are responding to these problems by affirming the primacy of free market values and are proving resilient in warding off attempts to infuse commercial relations with equitable purposes.
The sociological perspective also assists in explaining the largely voluntary nature of the regime. The influence of sovereignty as a consensual value continues to be reflected in regime norms. However, states' commitment to national sovereignty and to political autonomy have been tempered by what Ruggie refers to as the development of "embedded liberalism." States have affirmed the regime values of economic liberalism, but of a sort that accommodates domestic intervention. Hence they support a voluntary regime that contributes to uniformity without severely curtailing their political/legal autonomy.

The functional approach provides a good explanation of developments in the third phase. There is considerable evidence that states have traded off political autonomy to achieve gains from correcting market failures (Hypothesis B. 1 (a)). This is most evident in area of dispute resolution, where states have submitted to mandatory obligations to recognize and to enforce foreign arbitral awards which severely curtail the abilities of their national courts to intervene. The unification movement itself was spawned by concerns of correcting market failures. Commercial actors and states have developed uniform standards in transport, insurance, and finance to facilitate exchange by reducing their transaction costs. Furthermore, international

17. "International regimes, transactions, and change."
organizations have assisted in facilitating the conclusion and the monitoring of agreements (Hypothesis B. 1 (c)). Indeed, the advent of international organizations engaged in the unification of commercial law is one of the most significant developments in the modern regime. UNCITRAL, in particular, has played a critical role in expanding the unification movement beyond its regional, European origins. The creation of UNCITRAL marked the first institutional context for the development of a regime of global application.

Phase three provides much evidence to support the view that regimes develop and strengthen with increases in interdependence (Hypothesis B. 2). The regime expanded and adapted to accommodate quantitative and qualitative developments in international commerce. Moreover, the participation of the United States, which contributed to regime strength, was motivated by the quantitative expansion of trade. New standards developed in transport, insurance, and finance to address market failures generated by new transactions and technological developments, while the arbitration norm strengthened in response to market failures in the national adjudication of commercial disputes. National legal systems were simply unable to adequately address the demands posed by quantitative and qualitative developments in international commercial transactions.

The hypothesis that strong regimes are likely to develop in instances where actors are able to identify joint
gains in cooperating to correct market failures is strongly supported by developments in phase three of the regime. Common commercial interests in ensuring predictability of costs and certainty and transparency in laws regulating exchange, regarded as essential to the facilitation of exchange, form the foundation for the development of regime standards. However, the assumptions of mutual interests and joint gains require probing. It has been suggested that functional analysis of regimes exhibits a 'liberal bias' that poses limits to its explanatory capabilities. Haggard and Simmons note that "[F]unctional theories emphasize how the facilitating role of regimes helps them realize common interests" and the assumption of highly convergent interests leads to a minimization of divergent interests. Thus, the possibility that regimes may "institutionalize inequalities" is neglected.\textsuperscript{18} The potential for regimes to embody particularist or less-than-universal values and interests is evident in the notion of imposed or biased regimes that "distribute rewards to the advantage of some and the disadvantage of others, and in so doing they buttress, legitimize, and sometimes institutionalize patterns of dominance, subordination, accumulation, and exploitation."\textsuperscript{19} While functional analysis may have the appearance of being

\textsuperscript{18} "Theories of International Regimes," p. 509.

value neutral in that it contemplates symmetrical benefits flowing from regulation, it may obscure clear value preferences, evident in an asymmetric distribution of benefits. This objection is of particular concern to the private trade law regime. As we have seen, the underlying assumptions of modern contract law derive from liberal economic premises and were strongly influenced by British utilitarian thought. It is thus not surprising that the assumption of free exchange between parties of equal bargaining power underlies the obligatory nature of promissory or contractual obligations. While functional analysis focuses on the facilitative role of rules and thus accommodates permissive rule structures, it obscures the possibility that rights and entitlements may be distributed asymmetrically. Arguably, exact symmetry of benefits is not necessary to establish common interests. As Zacher notes:

No student of international regimes could challenge the fact that some potentially mutually beneficial regimes are rejected because of their distributional consequences or that some are adopted in part or largely because of distributional implications and the power of certain states. However, there are quite a few areas in which regimes have been established because almost all states achieved some gains. Those who gain less than others accept the regime because they do benefit, and because the larger gains of others are not seen as threatening to them.

Functional analysis assists in explaining why all states engaging in international commerce identify benefits in rendering exchange relations more efficient, certain, and secure. However, it does not capture important tensions between states over distributional concerns or explain why some states have been more successful than others in fashioning rules to their benefit.

Nor does functional analysis account for variations in the normative structure and the strength of the regime over time. Functional logic suggests that there should be reasonable continuity in the normative structure and the strength of the regime despite major changes in the distribution of capabilities among states (Hypothesis B.3). While there has been considerable continuity in regime principles over the three phases, there has also been considerable variation in rules. The regime is characterized by an enduring tension between the facilitative and distributional functions of commercial regulation. Furthermore, this tension has most often been resolved in favour of the former. Functional theory assists in understanding the continuity in regime principles in terms of the efficiencies and welfare generated by facilitative norms, but it does not explain why these norms emerged victorious over distributional norms. In order to explain the victory of free market principles reference must also be made to factors raised by structural realist and sociological analyses. The critical roles played by England
and the United States in originating and transmitting liberal political, economic, and legal values must also be considered. Furthermore, while the general strengthening of in the regime in the third phase would seem to support the efficacy of functional theory, we have seen that the United States has been instrumental in supporting and shaping regime norms.

The private international trade regime has evolved over time from an informal, collection of customs and practices, many of which derive from ancient commercial customs, to more formalized and positivistic rule structures. Changes in the normative structure, scope, and strength of the regime reflect the influence factors too numerous and complex to be accommodated by any single perspective. Each perspective offers valuable insights, but none is singularly capable of capturing the richness of the regime's history. A synthesis of perspectives is required in order to adequately account for the origin of the regime and its nature and strength over time.

Structural realism highlights the significance of barriers to cooperation posed by states' concerns of political autonomy and relative gains. It affords important insights into the influence that powerful states have on the determination of the normative structure and the strength of the regime. Structural realism is most useful in explaining the influence that the United Kingdom and the United States
have had on the modern regime. However, it is of limited value in accounting for the customary origins of the regime and for explaining the efficacy of voluntary norms.

The sociological approach provides some assistance in emphasizing the critical role played by shared values, consensual knowledge, and historical experiences in the genesis of norms. It thus accounts for the origin of historically conditioned customs and practices. However, the sociological approach does not provide a theory of cooperation. It does not address the circumstances generating consensual normative, ideological, and epistemological structures. For this, we must resort to the power-based analysis of structural realism or to functional analysis.

Overall, the functional perspective is the most useful in understanding the regime. It provides a theoretical rationale for cooperation and a reasonably good account of the origin and evolution of the regime. However, the account is not comprehensive. While concerns of economic efficiency have most certainly provided the foundation and dominant guidelines for regime standards, considerations of equity and fairness have also figured, though to a lesser extent. Functional analysis cannot account for challenges posed by equity concerns or answer why equity concerns have been subordinated to efficiency concerns. For this, reference must be made to the dominant ideology, norms, knowledge, and actions of the most powerful states.
This study of the private international trade law regime shows that the regime has provided the foundation for international commercial exchange for centuries. It has derived its character and strength through a variety of agencies, including private commercial actors, states, and international organizations. While uniformity in rules has waxed and waned at different times, considerable uniformity in the principles underlying the regulation of commercial relations render it the most durable and pervasive of international economic regimes. The private international trade law regime provides the foundation for global commercial exchange and there is every reason to believe that its influence will endure into the future. While the law merchant has certainly changed and developed since its medieval beginnings, continuity will persist as long as merchants and states remain committed to the protection of private property, freedom of contract, and the sanctity of agreements.
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APPENDIX A

PRINCIPLES INFORMING THE PRIVATE INTERNATIONAL TRADE LAW REGIME

Principles relating to the purposes of regime:

Facilitation of Exchange Principle: Commercial regulation, national and international, should facilitate the expansion of commercial exchange by enhancing the efficiency of commercial transactions. This is best achieved by reducing the costs and uncertainties of commercial transactions and enforcing promissory obligations without imposing unnecessary constraints on commercial flexibility.

Political Autonomy Principle: Commercial regulation should enhance political autonomy by promoting the achievement of local or national goals and policy concerns.

Equity Principle: Commercial regulation, national and international, should promote fairness and equality in exchange relations. Weaker parties should be protected and attempts to equalize the impact of commercial law should be made.

Principles relating to the Substantive and Procedural Dimensions of the regime:

Market Allocation Principle: The facilitation of exchange and expansion of commerce can best be achieved by allowing market forces to determine the most efficient allocation of resources.

Merchant Autonomy Principle: Merchants are the legitimate agents for creating binding obligations and should be free to regulate their own affairs. The procedures required to create contractual obligations, the substantive content of contracts, and the settlement of contractual disputes are best left to merchants to determine.

Freedom of Contract Principle: The most efficient allocation of resources is achieved by according broad scope for merchants to determine the nature of their contractual obligations. Commercial actors are assumed to be rational agents capable of creating binding contractual obligations.

State or Local Intervention Principle: States and local authorities are the legitimate agents for creating commercial law. Broad scope should be accorded to such authorities to regulate the creation, content, and enforcement of contractual obligations so that commercial activities reflect important national policy concerns (i.e., concerns of equity, morality, and public policy).
International Intervention Principle: International organizations are legitimate agents for the creation of commercial law. The intervention of international authorities is required to facilitate exchange through unifying commercial laws and to address certain equity concerns.

Sanctity of Contracts: Commercial actors may create promissory obligations that have the status of law and will be enforced as the law unto the parties, subject to public policy limitations.

Informality Principle: The most efficient allocation of resources may be achieved through avoiding the imposition of formalities on the creation and enforcement of commercial agreements.

Arbitration Principle: Arbitration is the most efficient and effective mechanism for dispute resolution. Merchants should be free to submit their disputes to international arbitration under the law chosen by the parties and states should be required to recognize and enforce international arbitral awards.

Adjudication Principle: National courts applying national law are the appropriate forums for dispute resolution and enforcement. States should be in control of the procedures and standards to be applied in dispute settlement and enforcement.