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CONTRACT LAW HARMONIZATION AND NON-CONTRACTING STATES: THE CASE OF THE CISG

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I. INTRODUCTION

The United Nations Convention on Contracts for the International Sale of Goods (hereinafter referred to as the “CISG”) is one of the most successful instruments of contract law harmonization. After 27 years of its adoption, and 19 years after its coming into force, the number of Contracting States has reached 70. Those states share a common contract law of sales which is often characterized as a *lingua franca* of international trade. The CISG removes legal barriers to cross-border trading through the reduction of legal costs, and the Contracting States are enjoying the benefit of harmonization. This poses the question of what the rest of the world is doing. Africa and Asia are rather slow in becoming members of the club. Perhaps, each country and region has its own reason. I will avoid making any hasty generalization and will take Japan as an example in order to answer two related questions.

The first is a question that any Japanese attending a colloquium dealing with contract law harmonization or the CISG cannot avoid. Namely, why has Japan not become a member of the CISG, and will Japan remain a Non-Contracting State? After making some excuses for the past, I will make some optimistic remarks about the future.

The second question is whether the CISG is irrelevant in Non-Contracting States. I ask this question in order to describe the creeping influence of the CISG witnessed even among Non-Contracting States.

II. JAPAN AS A NON-CONTRACTING STATE

Japan, as of today, is a Non-Contracting State. Given the extent to which it is involved in export/import trade, this makes one wonder why.

It is not that any decision to reject the CISG has been made. There was a time in the early 1990s

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when it seemed that Japan was almost going to join the CISG community. In 1989, soon after the CISG came into force, the Ministry of Justice (hereinafter referred to as the “MOJ”) organized an informal study group to examine the CISG. It was expected that upon the recommendation of this study group, the MOJ would commence the official process of acceding to the CISG. This did not happen. The study group continued with its mandate until 1993 when their work was suspended before reaching any conclusion.

The most direct reason for the suspension was this¹: in the early 1990s, the Japanese economy was struggling with the aftermath of the burst of the bubble economy. The legislative agenda became full of urgent legislations directed toward economic recovery. These included laws on secured transactions, insolvency laws, corporation laws, and so on which required full attention of the MOJ. The MOJ could no longer afford to continue with its work on the CISG.

But that answers only half the question. There still is the question of why the MOJ gave priority to those legislations over the CISG. True, of course, economic recovery was a more urgent matter with more direct impact on the economy than the CISG. However, just giving a go to the CISG would not have taken up much manpower since the study group had been already examining the CISG. I suspect that there was also some hesitation, though not a concern, about the CISG.

First of all, it was still in the early 1990s when the number of Contracting States was around 30. It was not clear whether the use of the CISG will become prevalent. There was also some uncertainty as to how the CISG will be applied in other Contracting States.

Secondly, the major Japanese trading companies (the “*sogoshosha*”) did not really feel the need at that time for the CISG, and was not particularly enthusiastic about it. Rather they were reluctant to take on the costs of learning the CISG², and have repeated that they will opt-out of the CISG anyway. Standard terms opting out of the CISG became so common that you will find them even in contracts which do not involve any element of sale of goods.

This lack of support discouraged the MOJ to continue its work on the accession to the CISG under the economic condition of the time.

III. TOWARD A CONTRACTING STATE

Will Japan remain a Non-Contracting State? I am happy to report to you that, most likely, Japan will join the club soon. In October last year [2006], the MOJ resumed its work toward accession to the CISG. The plan is to get approval from the Diet which is a constitutional requirement as early as in 2008.

What made this change happen? The most direct reason is that the congested legislative agenda have cleared somewhat and the MOJ is now able to devote their manpower to this task again. A more indirect reason, but an equally important one, is the phenomenal success of the CISG.

All of the dismal predictions which were sources of reluctance in acceding to the CISG in the early 1990s turned out to be wrong. The number of Contracting States has more than doubled. With the

¹ For another account of the story, see Yoshihisa Nomi, “The CISG from the Asian Perspective”, in *Celebrating Success: 25 Years United Nations Convention on Contracts for the International Sale of Goods* (Singapore International Arbitration Centre, 2005), also available at <http://cisgw3.law.pace.edu/cisg/biblio/nomi.html>.

² Luke Nottage, “Who’s Afraid of the Vienna Sales Convention (CISG)? A New Zealander’s View from Australia and Japan” 2005 *Victoria University of Wellington Law Review* 815, 829-840 also available at <http://www.austlii.edu.au/nz/journals/VUWLR/2005/39.html> and <http://cisgw3.law.pace.edu/cisg/biblio/nottage.html>.

emergence of the vast array of court and arbitral decisions, and the enormous amount of scholarly writings, doubts about the predictability of the CISG have diminished as well.

Also, small and medium-sized enterprises which are not particularly prepared to face the legal technicalities are engaging in international trade more than ever. Arguably, they may become the largest beneficiary of the CISG when Japan becomes a Contracting State. This factor adds to the reason to accede to the CISG.

The major trading companies are also beginning to change their attitude toward the CISG, now that they have discovered that the CISG is being used in a large part of the world. They are finding out that the CISG can curtail costs of dealing with diverse domestic laws, as well as transactions costs associated with negotiating choice-of-law clauses.

This sudden awareness is in large part due to the growth of the Asian market³. Most symbolic is the rapid increase of Japan's trade with China. In the year 1990, China's share in Japan's export/import trade was less than 4%. Today it is close to 20%. This is equal to Japan's trade with the United States, which used to be Japan's largest trading partner for years. The U.S. and China combined accounts for nearly 40% of Japan's international trade. More importantly, it seems that Chinese traders are not shy to use the CISG. More on this later.

The same applies to other East Asian countries. Japan's trade with this region, even excluding China, amounts to more than 20% of Japan's export/import. This surpasses Japan's trade with the U.S. or China. Given the diversity of legal systems among these countries, and given that many of these countries are either transition economies or economies in the process of developing their legal infrastructure, the advantage of having one common contract law is becoming attractive than ever. Of course, at present, China, Singapore, and Korea are the only East Asian States parties to the CISG. However, joining the CISG would be a big step for Japan toward dealing with the Asian diversity.

IV. THE CREEPING INFLUENCE OF THE CISG IN A NON-CONTRACTING STATE

At present, Japan, as a Non-Contracting State, is involved in very limited CISG practice, but nonetheless, the success of the CISG does have some ripple effect.

1. The CISG in Japanese Courts

First of all, it is always possible that the CISG may be applied in a Non-Contracting State as foreign law. There was one close call in 1998. In a case of an import of a classic Porsche from the United States to Japan, the Tokyo District Court considered applying the CISG⁴. In that case, the Japanese rules of private international law led to the application of U.S. law (or California law) and the court considered that U.S. law would mean the CISG. There are obvious flaws in this reasoning⁵, but that did not affect the

³ The following analysis is based on trade statistics available from the Japan External Trade Organization (JETRO) website <http://www.jetro.go.jp/jpn/stats/trade/>.

⁴ Japan 19 March 1998 Tokyo District Court (Nippon Systemware Kabushikigaisha v. O.), 997 Hanrei Taimuzu 281. For a brief account, see <http://cisgw3.law.pace.edu/cases/980319j1.html>. On appeal, the Tokyo High Court (Japan 24 March 1999 Tokyo High Court, 1700 Hanrei Jiho 41, translation unavailable) reversed the district court's decision on jurisdiction and rendered judgment applying Japanese law.

⁵ First, the court apparently overlooked that Article 1(1)(b) should be fulfilled pursuant to the Californian rules of private international law in order to apply the CISG to this case. No such analysis is given. Second, the court further overlooked that the United States has declared an Article 95 reservation.

outcome of the case: the court, after its discussion of the CISG, denied its own jurisdiction over this case. Effectively, every reference in this case to the CISG is in the *obiter dictum*.

However, the point here is that the court did consider the CISG in length. It is unusual that a court would do so and overturn it later by denying its own jurisdiction. What caught my attention is the judge. The decision was rendered by Judge Toshifumi Minami, who was involved in several UNCITRAL deliberations of the CISG in the late 1970s and also at the 1980 diplomatic conference as a Japanese delegate. This decision may have been a part of his crusade to raise awareness about the CISG in Japan.

2. CISG Cases involving Japanese Parties

Other than the above, a quick research of the Pace CISG database⁶ revealed nine cases where CISG was applied to international sales involving a Japanese seller or buyer. One of them is an Australian court decision, and the other eight are cases from China: three court decisions and five arbitration cases. The arbitration cases are all from the China International Economic and Trade Arbitration Commission (hereinafter referred to as “CIETAC”). The cases identified are probably only a tip of the iceberg, and this is indicative of where the gravity of the CISG practice in Japan will lie. [Three of the cases do not make it clear on what basis the CISG was applied⁷, and the following examination will concentrate on the other six which makes the reason clear.]

(1) Article 1(1)(a)

One would not expect the CISG to be applied to cases involving Japanese parties on the basis of Article 1(1)(a). However, three of the CIETAC cases applied the CISG, surprisingly, on the basis of Article 1(1)(a). The cases involved parties whose places of business were in China and Japan, and the tribunal applied the CISG pointing out that China and Japan are both parties to the CISG⁸. This is clearly wrong. However, it does sound so natural that Japan is a Contracting State and it reinforces the view that it is about time that Japan live up to the expectations of other CISG states.

Besides, we also have to take into account the operation of Japanese companies through their overseas subsidiaries. Although the subsidiaries are not Japanese parties in the technical sense, it is no secret that they are controlled by their Japanese headquarters. Many subsidiaries will have their place of business in a Contracting State, and as such, they will be subject to the CISG through Article 1(1)(a). For example, a sale of goods between a subsidiary of a Japanese company in Germany and a French buyer will

⁶ A “Google” search by the combination of the terms “cisc case presentation” and “country: japan” will result in a list of cases in the Pace database involving a Japanese seller or buyer.

⁷ China 19 February 2001 Jiangsu Higher People’s Court [Appellate Court] (Tai Hei v. Shun Tian), translation available at <http://cisgw3.law.pace.edu/cases/010219c1.html>; China 27 November 2002 Higher People’s Court of Ningxia Hui (Xinsheng Trade Company v. Shougang Nihong Metallurgic Products), translation available at <http://cisgw3.law.pace.edu/cases/021127c1.html>; China 20 July 1993 CIETAC Arbitration proceeding (Shaping machine case), translation available at <http://cisgw3.law.pace.edu/cases/930720c1.html>.

⁸ China 7 November 1996 CIETAC Arbitration proceeding (Stone products case), translation available at <http://cisgw3.law.pace.edu/cases/961107c1.html>; China 2 April 1997 CIETAC Arbitration proceeding (Wakame case), translation available at <http://cisgw3.law.pace.edu/cases/970402c1.html>; China 21 October 2005 CIETAC Arbitration proceeding (Sheet metal producing system case), translation available at <http://cisgw3.law.pace.edu/cases/051021c1.html> (last visited on July 17, 2007). See also Dong Wu, “CIETAC’s Practice on the CISG” 2005/2 *Nordic Journal of Commercial Law*, http://www.njcl.fi/2_2005/article2.pdf, at 9-10 and Fan Yang, “The Application of the CISG in the Current PRC Law and CIETAC Arbitration Practice” 2006/2 *Nordic Journal of Commercial Law*, http://www.njcl.utu.fi/2_2006/article4.pdf, at 25.

be governed by the CISG⁹.

(2) Article 1(1)(b), including Opting-In

Next, there is an application of the CISG on the basis of Article 1(1)(b). In 2003, the Supreme Court of Victoria, Australia applied the CISG to a dispute involving a Japanese seller and an Australian buyer¹⁰. In that case, the private international law of the forum led to the application of Victorian law, and the CISG was applied on the basis of Article 1(1)(b). This is a straightforward CISG case.

What is more interesting for our purposes, however, are the cases where the parties “opted-in” to the CISG¹¹. There is a Chinese case in which the parties chose the law of People’s Republic of China as the governing law¹². The court interpreted correctly that the law of PRC includes the CISG. If the parties have chosen the law of a Contracting State, without expressly excluding the CISG, the prevailing view is that the CISG would apply on the basis of Article 1(1)(b)¹³.

There are also some cases that applied the CISG because the parties based their arguments before the tribunal on the CISG. For example, one CIETAC tribunal ruled that “[b]oth the [Buyer] and the [Seller] analyzed the rights and responsibilities based on the law of People's Republic of China and the CISG. Accordingly, the Arbitration Tribunal holds that the law of People's Republic of China as well as the CISG shall be the applicable law to this case.”¹⁴

As can be seen from these examples, it seems that Japanese business is starting to appreciate the merits of CISG, especially in the context of trading with China, and likely in the context of trading with the diverse legal systems of Asia.

3. Assimilation of the CISG into Japanese Law

Other than the practice described above, the CISG is gradually becoming assimilated into Japanese law. First of all, the CISG is starting to influence the interpretation of the Japanese Civil Code. For example, CISG’s limitation of avoidance of contracts to cases of “fundamental breach” was first considered

⁹ One early example is France 22 April 1992 Appellate Court Paris (Fauba France FDIS GC Electronique v. Fujitsu Microelectronik GmbH), translation available at <http://cisgw3.law.pace.edu/cases/920422f1.html>. The German seller was a subsidiary of Fujitsu Ltd., a Japanese company.

¹⁰ Australia 24 April 2003 Supreme Court of Victoria (Playcorp Pty Ltd v Taiyo Kogyo Limited) (Toys case), available at <http://www.austlii.edu.au/au/cases/vic/VSC/2003/108.html> and <http://cisgw3.law.pace.edu/cisg/text/030424a2english.html>. A brief account is also available at <http://cisgw3.law.pace.edu/cases/030424a2.html>.

¹¹ Another interesting phenomenon is the application of the CISG as *lex mercatoria* independent of the requirements of Article 1. Although I could not find any case involving a Japanese party applying the CISG as *lex mercatoria*, there was one that came close. It is a case from New Zealand (New Zealand 27 November 2000 Court of Appeal Wellington (Hideo Yoshimoto v. Canterbury Golf International Ltd), CLOUT no.702, also available at <http://cisgw3.law.pace.edu/cases/001127n6.html>), which involved a contract between a Japanese seller and a New Zealand buyer for the sale of “shares” of a company. This case is clearly outside the scope of the CISG because Article 2(d) explicitly excludes the sale of shares from the application of the CISG. Nonetheless, the court considered the application of Article 8 of the CISG (together with Article 4.3 of the UNIDROIT Principles of International Commercial Contracts 1994). At the end, the court decided not to do so, because such decision will only be overturned by the Privy Council in England. However, the court gives the impression that otherwise it would have applied the CISG.

¹² China December 1994 Fujian Higher People’s Court (San Ming v. Zhanzhou Metallic Minerals), translation available at <http://cisgw3.law.pace.edu/cases/941200c1.html>. For a brief account of the lower court decision (China August 1994 Xiamen Intermediate People’s Court (San Ming v. Zhanzhou Metallic Minerals)), see <http://cisgw3.law.pace.edu/cases/940800c1.html>.

¹³ On the other hand, in Italy 19 April 1994 Florence Arbitration proceeding (Leather/textile wear case), CLOUT no.92, translation available at <http://cisgw3.law.pace.edu/cases/940419i3.html>, a case involving a dispute between an Italian seller and a Japanese buyer, the parties chose “Italian law” as governing law. The majority of the tribunal decided to apply not the CISG but domestic Italian law, although one of the three arbitrators dissented.

¹⁴ China 23 July 1997 CIETAC Arbitration proceeding (Polypropylene case), translation available at <http://cisgw3.law.pace.edu/cases/970723c1.html>. For other similar CIETAC cases, see Wu, supra note 8, at 5-6.

to be an alien concept in Japan. It was traditionally understood under Japanese law that, as a general rule, the injured party may avoid the contract after giving the breaching party a *Nachfrist* period, no matter how trivial the breach may be (although it was also understood that fault on the part of the breaching party was necessary). There were, however, exceptions scattered around the Code which allowed avoidance of contracts only when the purpose of the contract can no longer be achieved. A reconfiguration of the interpretation of the Japanese Civil Code now attempts to turn these exceptions into the norm, which will put the Civil Code in line with the CISG. According to this view, the limitation of avoidance to cases of fundamental breach is nothing new and it has always been a part of the Japanese Civil Code.

And then further, the MOJ has now started working on the revision of the Obligations Law of the Civil Code¹⁵. That decision was made in order to adapt the Code to the social and economic change that took place since its enactment more than a century ago. However, this decision was also stimulated either directly or indirectly in part by the success of the CISG. It is only natural that the CISG will have impact on this upcoming revision.

V. CONCLUSION

I have stressed that the most direct allure of the CISG for a Non-Contracting State contemplating to join it lies in its success and the benefit that it brings¹⁶.

However, we must also not forget what made it successful. It was the wisdom of its founders in creating a fair, reasonable, and a practical contract law, as well as those whose efforts went into the continuous development of the CISG through its interpretation and application.

It is my hope that Japan, as well as other Non-Contracting States, will soon take part in this endless project toward harmonization.

¹⁵ See the website of the “Japanese Civil Code (Law of Obligations) Reform Commission” at <http://www.shojihomu.or.jp/saikenhou/>. Nomi, supra note 1, suspects that one reason that held back Japan from acceding to the CISG in the early 1990s was the misconception that a revision of the Civil Code would be required to accommodate the CISG. As Nomi points out correctly, this is a fallacy. However, the government’s willingness today to consider revising the Civil Code certainly helps to remove this (false) barrier.

¹⁶ For a similar “realist” argument regarding a slightly different context, see Souichirou Kozuka, “Contract Law in East Asia at the turn of the Century: Lawyers and Globalisation”, in Shinya Imaizumi et al eds., *Globalization and Economic Law Reforms: Perspectives from India, Mexico, Thailand and East Asia*, JRP Series No. 136, (Chiba: Institute of Developing Economies, 2005) and Souichirou Kozuka, “Economic Implications of Uniformity of Law” in Jürgen Basedow & Toshiyuki Kono eds., *An Economic Analysis of Private International Law* (Mohr Siebeck, 2006).