view of the possible inclusion in the work programme of subjects of this nature.

Co-ordination of work of other organizations

2. General Assembly resolution 2205 (XXI) states that the Commission shall further the progressive harmonization and unification of the law of international trade by, *inter alia*,

(i) Co-ordinating the work of organizations active in this field and encouraging co-operation among them;

(ii) Establishing and maintaining a close collaboration with the United Nations Conference on Trade and Development;

(iii) Maintaining liaison with other United Nations organs and specialized agencies concerned with international trade.[32]

3. The object of these provisions appears to be to make the Commission the body responsible for organizing and directing all work connected with the unification of international trade law. However, up to the present stage of the Commission's work this object has not been fully realized. While the work of some organizations is to some extent carried on in collaboration with the Commission, other organizations both within the United Nations family and outside it sometimes work in areas of international trade law without any reference to the Commission. Several factors may have contributed to this. In some instances, the programme of work of other organizations was established at about the same time the Commission was established, and accordingly there was no proper opportunity for co-ordination. Again, certain organizations do not appear readily to acccept the pre-eminence of the Commission in the field of international trade law. Furthermore, the Commission has been mainly concerned with working on its priority subjects, and has directed less attention to co-ordination. It would, however, be appropriate at this stage to examine the question of co-ordination, not only because it has been stressed by some Governments,[33] but because a lack of assertion by the Commission of its proper role could have unfortunate consequences: duplication of work, and a gradual erosion of the area of competence of the Commission. The Commission may therefore wish to consider the methods by which a better co-ordination of work can be achieved.

Methods of work

4. In carrying forward its work, the Commission has adopted a variety of working methods, i.e. established working groups or study groups, entrusted work to a Special Rapporteur, authorized the engaging of consultants, and requested studies to be made by the Secretariat. These working methods have proved adequate in relation to the current programme of work where the method of work most appropriate to the subject in question has been selected. The Commission may wish to consider whether any modifications to these working methods are desirable, with particular reference to the future programme of work.

Possible scope of the future work programme

(i) *Period of projection of the future work programme*

5. In its comments on the future work programme, the United States notes that it is undesirable to include in the future work programme projects that would take many years to complete, since the current rapid growth and change in international trade might result in the projects when completed being of little utility. Certain proposals, however, such as the drafting of a Trade Code, involve work extending over many years. The Commission may wish to consider this issue.

(ii) *Establishment of working groups*

6. Owing to financial restrictions, the Commission is not free to establish more than three working groups at any one time. At present, the working group on negotiable instruments has yet to complete its work. It is expected that this work in so far as it relates to the preparation of a draft convention on international bills of exchange and international promissory notes, will be completed in 1979.

[32] Para. 8, subparas. (*a*), (*f*) and (*g*) of the resolution.

[33] Czechoslovakia and the German Democratic Republic, in their comments on the future work programme, note the need for closer co-ordination. Czechoslovakia stresses the need for close co-ordination with other United Nations bodies, in particular with UNCTAD and the International Law Commission, and notes the possibility of collaborating with UNCTAD in its work on charter-parties and marine insurance. It also notes the desirability of co-ordination with UNIDROIT and the Hague Conference on Private International Law. The importance of co-ordination was also stressed during the deliberations leading to the establishment of the first work programme of the Commission (A/7216, paras. 25-28).

ANNEX I*

Note by the Secretariat: liquidated damages and penalty clauses

1. The United Nations Commission on International Trade Law at its tenth session requested the Secretary-General

> "to consider, as part of the study on the future long-term programme of work of the Commission which is to be presented at the eleventh session of the Commission, the feasibility and desirability of establishing a uniform régime governing liquidated damage clauses in international contracts".[a]

This report is written in response to that request.

2. The request by the Commission arose out of a proposal submitted during the course of the tenth session that the draft Convention on the International Sale of Goods include a provision on liquidated damages and penalty clauses[b] in contracts for the international sale of goods. During the ensuing discussion, it became apparent that there was considerable support for the idea behind the proposal, i.e. that uniform rules regulating liquidated damages and penalty clauses would be an important contribution to the facilitation of international

* Originally issued as A/CN.9/149/Add.1 on 1 May 1978.

[a] UNCITRAL; report on the tenth session A/32/17, annex I, para. 513 (Yearbook . . . 1977, part one, II, A).

[b] A significant difficulty in terminology exists which goes to the substance of the subject-matter of this report. In the French, Russian and Spanish languages the technical name for the type of clauses under discussion is "penalty clause". Common law countries distinguish "penalty clauses" from "liquidated damages clauses" for purposes of determining the validity of such clauses. Other legal systems which recognize the validity of clauses which serve as a means of encouraging performance of the contract we well as of those intended as an estimate of damages nevertheless use different terms to describe such clauses and differentiate between them in regard to their legal consequences. Since the choice of terminology in a given legal system sometimes leads to expectations as to the consequences arising out of the use of such a clause, it was thought best, at this stage of the Commission's consideration, to use terminology which minimized these expectations.

trade and commerce. However, it was generally considered that establishing a unified régime was a complex problem which warranted more attention than could be given at that stage of the deliberations in respect of the draft Convention. Furthermore, liquidated damages and penalty clauses were also important in many types of contracts which were outside the scope of the draft Convention. For all these reasons, it was suggested that it would be preferable to deal with liquidated damages and penalty clauses in a separate instrument which could be applied to a wider range of international contracts and not be restricted to contracts for the international sale of goods.[c]

Desirability of unification

3. Clauses or stipulations providing for the payment of damages or of a penalty on default are in wide use in commercial contracts. Their purpose is to determine in advance the amount of damages in the event of a breach of contract or, by imposing a penalty for such breach, to encourage performance of the obligations under the contract. Frequently such clauses or stipulations are intended to serve both purposes.

4. Such clauses are attractive to merchants and their lawyers. If the sum stipulated in the clause is high enough, it increases the likelihood that the other party will perform his obligations at the time and in the manner agreed. If the other party does not perform in conformity with the contract, the clause gives an easy, rapid and clear calculation of the compensation for that breach. This is true whether the clause was intended to make an accurate estimate of the actual damages, to encourage performance by stipulating by way of penalty a sum higher than the estimated damages, or to limit damages by stipulating a sum less than the estimated damages. As a result, the likelihood of controversy between the two parties is reduced, along with the costs directly involved in settling any dispute and the danger of rupturing the business relationship between the parties.

5. These advantages of the clauses would seem to be even more significant in a contract between parties from two different countries. The possibilities for delay or failure of performance are greater, the informal pressures which can be exerted to encourage performance by the other party are less effective, and access to a foreign legal system—which would be necessary for at least one of the parties in case of litigation—is more difficult and expensive than when the contract is between two parties from the same country.

6. Nevertheless, various restrictions are placed by different legal systems on the use of such clauses. In some jurisdictions, a court will not enforce a clause in a contract unless it is construed as providing for liquidated damages rather than as providing for a penalty. In some other jurisdictions, a court may revise a clause which sets the compensation either substantially higher or substantially lower than the estimated damages. This result may reflect the view that the dominant purpose of such clauses is a pre-estimate of future damages in cases of breach or may reflect the view that the clause might have been imposed by the economically stronger party. As a result most legal systems appear to authorize the courts either to disregard such a clause or to lower the amount stipulated in it if the amount stipulated appears to be excessively high, and, in some legal systems, to raise the amount stipulated in the clause if that amount appears to be excessively low.

7. Even within legal systems which have the same underlying philosophy towards the use of these clauses there are often important differences in the law in respect of such questions as to whether damages may be awarded in addition to the stipulated sum, whether the sum may be stipulated in terms other than money, and whether a party who is not liable for damages for failure to perform his obligations because that failure was due to an impediment beyond his control is also by that impediment absolved from liability to pay the sum stipulated.

8. Since some legal systems restrict the freedom of the parties to contract in respect of liquidated damages and penalty clauses, the merchant community cannot overcome the diversity of legal régime by agreement amongst themselves. It is therefore submitted that, if unification is to be achieved, it must be by international legislation.

[c] A/32/17, annex I, paras. 510-512.

Feasibility of unification

9. Although there are important differences in public policy which lie behind the rules in respect of liquidated damages and penalty clauses in the various countries, it would appear that these differences can either be minimized or avoided. This is particularly true in respect of the rules which have developed in some countries to protect consumers from the abusive use of such clauses. The elimination of all consumer transactions from the eventual unified régime should reduce the difficulties of introducing rules which may be different from those which have been developed in the national legal systems to govern consumer as well as non-consumer contracts.

10. In addition, less opposition is to be expected to a change in the law where the clause is stipulated in a contract between parties from different States. In such a case, and in the absence of uniform legislation, rules of private international law come into operation to determine whether and to what extent a liquidated damages or penalty clause will be enforced by the foreign court that is seized of the suit. It is thus possible that, in a case before a foreign court, a party will have a penalty clause enforced against him though under the domestic law of that party's State such a clause would have been held invalid or would have been modified by reducing the damages stipulated. Conversely, a party may not be able to obtain enforcement of such a clause even though in the court of his own State adjudication would have led to a recognition of the rights stipulated in that clause.

11. It is not possible within the scope of this report to analyse the kinds of contract for which a unified régime in respect of liquidated damages and penalty clauses might be adopted. Nevertheless, in view of the fact that the common law systems and the civil law systems are in agreement that such clauses can serve a useful function but that they can be utilized to take unfair advantage of the other party, it seems reasonable to conclude that agreement could be reached on rules in respect of liquidated damages and penalty clauses for use in a wide range of contracts used in international trade.

ANNEX II*

Note by the Secretariat: international barter or exchange

1. In the course of consultations with international organizations on the future programme of work of the Commission, attention was drawn to the growing importance of transactions by barter or exchange. Such transactions can be distinguished from sale transactions in that the goods sold are not to be paid for by money, but by other goods or some other valuable consideration.

2. Legal systems approach the contract of barter or exchange in different ways. In general, civil law systems provide expressly that the provisions on sale apply, by analogy, also to barter,[a] and specify that each of the parties to a contract of barter is considered the seller of the goods which he transfers and the buyer of the goods which he receives. A similar approach is found in the Uniform Commercial Code of the United States of America which, in section 2-304, provides that "the price can be made payable in money or otherwise. If it is payable in whole or in part in goods each party is a seller of the goods which he is to transfer."

3. The approach of common law countries that follow the English Sale of Goods Act, 1893 is different. Section 1 of that Act restricts the meaning of a contract of sale to a contract "whereby the seller transfers or agrees to transfer the property of goods for money consideration". Where the consideration for the transfer of goods is not money, there is a contract of exchange that is distinguished from a contract of sale, and the Sale of Goods Act has no direct application to such a contract.[b] Apparently, the common law principles applicable to sales of goods are ordinarily applicable to exchanges.[c]

* Originally issued as A/CN.9/149/Add.2 on 12 May 1978.

[a] E.g. Brazil, Codiglio Civil, art. 1164; Ethiopia, Civil Code, art. 2409; France, Code civil, art. 1707; Germany, Federal Republic of, BGB1. art. 515; Hungary, Civil Code, art. 386; Italy, Codice Civile, art. 1552-1555; Netherlands, Civil Code, art. 1582; Russian Soviet Federated Socialist Republic, Civil Code, art. 255; Switzerland, Code des obligations, art. 237. See also International Trade Code of Czechoslovakia, art 425.

[b] Benjamin; *Sale of Goods*, 1st ed. (1974), p. 29; Cheshire and