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Professional paper

MODEL CLAUSES - AN EFFICIENT TOOL FOR CREATING PREDICTABILITY IN INTERNATIONAL BUSINESS CONTRACTING

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Abstract

A commercial contract refers to a legally binding agreement between parties in which they are obligated to do or restrain from doing particular things. This usually involves the movement of goods and rights or service delivery. Different terminologies, ambiguity or meaninglessness that may have certain provisions regulating concrete contractual issues resulting from differences that exist between the various legal systems of different countries have created situations of uncertainty of the contracting parties in the interstate business contracts. Solutions to get out of this situation were found in the so-called clause models that quickly came into use by being widely accepted by business entities around the world. For such admission, the promotion of the most weight organizations and institutions in the field of business contracting -International Institute for the Unification of Private Law (UNIDROIT), the International Chamber of Commerce (ICC), International Trade Center (ITC), and European Commission of the European Union-have also contributed. These model clauses serve as invaluable guide that clarifies the issues surrounding international contracts and help lawyers and business people avoid the most common pitfalls. By analyzing the most widely used examples of model clauses, particularly in the area of drafting and negotiating contracts, sales of goods or cases of force majeure, the author confirms the established hypothesis that the model clauses have a significant influence on the provision security between the contracting parties, and also in the strengthening of confidentiality between them.

Keywords: commercial contract, drafting, model clauses, business entities.

1. Introduction

Contracts are used almost in every industry, and many of the contract clauses that are used are applicable across sectors. In fact, there are certain contract clauses that are likely to make an appearance in just about any contract that is drafted. Commercial contracts, in particular, tend to contain a standard set of terms and conditions. Given the fact that national laws differ significantly in terms of the requirements they have for the content of contracts, the more so that such laws focus on contracts of a national rather than international character, while reaching a consensus by states on a unified law proved to be by no means easy, relevant international organizations and institutions have taken initiatives to find alternatives to facilitate international business contracting. Among them are particularly prominent: UNIDROIT, ICC, ITC, and the European Commission of the EU. Moreover, solutions provided by them are certainly more balanced than the choice of the law of the country of one of the two parties, since they will give neither of them the advantage of having recourse to its own law. In fact, both parties will be in the same condition, i.e. both will need to deal with a law with which they are not familiar.[1] In particular, this is a practice in international sales,

[1]*Developing Neutral Legal Standards for International Contracts: A National Rules as the Applicable Law in International Commercial Contracts with Particular Reference to the ICC Model Contracts*, International Chambers of Commerce, 4, https://iccwbo.org/content/uploads/sites/3/2017/01/Developing-Neutral-Legal-Standards-Int-Contracts.pdf [14.12.2020].

because the parties often do not know which law will apply in the event of a dispute, and thus want to avoid the application of any national law - decide in a contractual manner to regulate the circumstances with interest.[2]

Practice provides data on the greatest use of some of the contractual clauses: confidentiality, force majeure, termination triggers, jurisdiction, dispute resolution, and damages. In deciding which of the four categories of Model Clauses to choose parties should be aware of the advantages and disadvantages of each? Where appropriate, for each Model Clause two versions are proposed, one for inclusion in the contract ("pre dispute use") and one for use after a dispute has arisen ("post dispute use").[3]

1. International Institutional Commitment for drafting Model Clauses

(a) Model Clauses for the use of the UNIDROIT Principles of International Commercial Contracts

The UNIDROIT Principles of International Commercial Contracts (hereinafter "the UNIDROIT Principles"), first published in 1994, with a second edition in 2004, a third in 2010, fourth edition in 2016 and now in their fifth edition 2020, represent a non-binding codification or "restatement" of the general part of international contract law. Welcomed from their first appearance as "a significant step towards the globalization of legal thinking", over the years they have been well received not only by academics but also in practice, as demonstrated by the numerous court decisions and arbitral awards rendered world-wide that refer in one way or another to the UNIDROIT Principles.[4]

Unlike binding instruments, such as, e.g., the conventions, which are applicable whenever the contract at hand falls within their scope and the parties have not excluded their application, the UNIDROIT Principles, being a "soft law" instrument, offer a greater range of possibilities of which parties are not always fully aware. Hence the idea of preparing Model Clauses in which parties may wish to adopt in order to indicate more precisely in what way they wish the UNIDROIT Principles to be used during the performance of the contract or when a dispute arises.

The Model Clauses are divided into four categories according to whether their purpose is:

- to choose the UNIDROIT Principles as the rules of law governing the contract;
- to incorporate the UNIDROIT Principles as terms of the contract;
- to refer to the UNIDROIT Principles to interpret and supplement the CISG when the latter is chosen by the parties;
- to refer to the UNIDROIT Principles to interpret and supplement the applicable domestic law, including any international uniform law instrument incorporated into that law.

Parties should be aware that the purpose of the Model Clauses is merely to allow them to indicate more precisely the way they wish the UNIDROIT Principles to be used during the performance of the contract or when a dispute arises. Therefore, even if parties decide not to use these Model Clauses, judges and arbitrators may still apply the UNIDROIT Principles according to the circumstances of the case as they have been doing so far.[5]

[2]Faton Z. Shabani, *Pasojat juridike nga mospërmbushja e kontratës për shitjen ndërkombëtare të mallrave*, Tetovë: Universiteti i Tetovës, 2016, 311.

[3]*Model Clauses for the use of the UNIDROIT Principles of International Commercial Contracts*, Rome: UNIDROIT, 2013, 2-3.

[4] Ibid, 1.

[5]Ibid, 3.

(b) ICC Model Contracts and Clauses

The ICC Commission on Commercial Law and Practice (CLP) develops ICC model contracts and ICC model clauses which give parties a neutral framework for their contractual relationships. These contracts and clauses are carefully drafted by experts of the CLP Commission without expressing a bias for any one particular legal system. ICC model contracts and clauses aim to provide a sound legal basis upon which parties to international contracts can quickly establish an even-handed agreement acceptable to both sides. The contracts are the products of some of the finest legal minds in the field of international commercial law. They are constructed to protect the interests of all the parties, combining a single framework of rules with flexible provisions allowing the parties to insert their own requirements.[6]

The most outstanding feature of the ICC Model Contracts is that they are not drafted to be imposed by one of the parties to the other party in a manner to restrict the freedom of will principle - they adopt the rules that reflect the market place. Given such a feature, ICC Model Contracts are drafted with a purpose to replace the choice between differing national legislations, which are often not adapted to the needs of international trade, by a detailed set of contractual provisions.

The ICC Model Contracts include:

- Model Contract on Commercial Agency;
- Model Contract 'Consortium Agreement';
- Model Confidentiality Agreement;
- Model Contract on Distributorship;
- Force Majeure and Hardship Clause;
- Model International Franchising Contract;
- Model Mergers and Acquisitions Contract;
- Model Subcontract;
- Model Contract 'Occasional Intermediary (Non-circumvention and Non-disclosure)';
- Model International Transfer of Technology Contract;
- Model International Trademark License;
- Model International Turnkey Contract.

(c) ITC Model Contracts

Many small companies are now engaged in international trade, but don't have access to the necessary contract forms to protect them. ITC and leading legal experts developed eight generic contract templates that incorporate internationally recognized standards and laws for most small business situations. The contract templates provide practical ways to secure international business for small firms and bridge many legal and cultural traditions by harmonizing recurring legal provisions common to most international contracts.[7]

These templates are for key trade activities such as the sale of goods, distribution, services, joint ventures, and more. They were originally published in ITC's 2010 book: Model Contracts for Small Firms: Legal Guidance for Doing International Business.[8]

(d) European Union Model Clauses

[6] https://iccwbo.org/resources-for-business/model-contracts-clauses/ [20.12.2020].

[7] https://www.intracen.org/itc/exporters/model-contracts/ [20.12.2020].

[8] https://www.intracen.org/model-contracts-for-small-firms/ [20.12.2020].

European Union (EU) data protection law regulates the transfer of EU customer personal data to countries outside the European Economic Area (EEA), which includes all EU countries and Iceland, Liechtenstein, and Norway. The EU Model Clauses also known as "standard contractual clauses" are standardized contractual clauses used in agreements between service providers (such as Microsoft) and their customers to ensure that any personal data leaving the EEA will be transferred in compliance with EU data-protection law and meet the requirements of the EU Data Protection Directive 95/46/EC,[9] repealed by General Data Protection Regulation 2016/679.[10]

According to the European Commission Model Clauses offer sufficient safeguards on data protection for the data to be transferred internationally. It has so far issued two sets of standard contractual clauses for data transfers from data controllers in the EU to data controllers established outside the EU or European Economic Area (EEA).It has also issued one set of contractual clauses for data transfers from controllers in the EU to processors established outside the EU or EEA.[11]

On a practical level, compliance with EU data protection laws also means that customers need fewer approvals from individual authorities to transfer personal data outside of the EU, since most EU member states do not require additional authorization if the transfer is based on an agreement that complies with the Model Clauses. Furthermore a service provider that commits contractually to the Model Clauses gives its customer's assurance that personal data will be transferred and processed in compliance with EU data protection law.[12]

EC has issued three sets of model clauses:

(a) Decision 2001/497/EC[13] in which both parties enter into a joint and several liability for the data protection obligations;

(b) Decision 2004/915/EC,[14] developed in cooperation with different trade associations and providing for more flexibility for onward transfers by data importers;

(c) Decision 2010/87/EU[15] addressing data transfers from EU controllers to non-EU processors.

Given the existence of three forms of model clauses, it is important to understand the role of the recipient importing the personal data to make sure that the correct version is used. If the importer only uses the details on behalf of and as instructed by the "client" data exporter (e.g. a hosting service), the importer is a data processor and the data controller to data processor form of model clauses (2010) must be used. This scenario may arise where one group company acts as an internal service provider to other affiliates within a group of companies, as well as where an external vendor acts in that way. By contrast, if the importer acts as a data controller (e.g. a parent company receiving affiliate personal data for independent parental decision making and functions), a data controller to data controller form of model clauses must be used.

[9] Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data, ***OJ L 281 (1995).***

[10] Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC, ***OJ L 119 (2016).***

[11] https://ec.europa.eu/info/law/law-topic/data-protection/international-dimension-data-protection/standard-contractual-clauses-scc_en [20.12.2020].

[12] https://docs.microsoft.com/en-us/compliance/regulatory/offering-eu-model-clauses [20.12.2020].

[13] Commission Decision of 15 June 2001 on standard contractual clauses for the transfer of personal data to third countries, under Directive 95/46/EC, ***OJ L 181 (2001).***

[14] Commission Decision of 27 December 2004 amending Decision 2001/497/EC as regards the introduction of an alternative set of standard contractual clauses for the transfer of personal data to third countries, ***OJ L 385*** (2004).

[15] Commission Decision of 5 February 2010 on standard contractual clauses for the transfer of personal data to processors established in third countries under Directive 95/46/EC of the European Parliament and of the Council, ***OJ L 39,*** (2010).

This can be the original form (2001) or later form (2004). The 2004 version is recommended as it is more business friendly.[16]

2. Key Clauses found in Business Contracts

From the large number of contract models encountered today in business contracting practice seven of them stand out as the most representative.

(a) Model clause for inclusion in the contract

"This contract shall be governed by the […]".

Such a clause is in fact the first step of the contracting parties which decide to use certain models of clauses in their contract. On this case, if parties choose only certain rules as the rules of law governing their contract, the question arises as to deal with issues not covered by these rules. Issues outside the scope of these rules and, therefore, not covered by them at all will of necessity be governed by other legal sources.[17]

(b) Confidentiality

"The parties acknowledge that the existence and the terms of this contract and any oral or written information exchanged between the parties in connection with the preparation and performance this contract are regarded as confidential information".

Today, confidentiality clauses and secrecy agreements are widespread. It is no longer a matter of hiding ass's ears but technical processes, commercial methods, financial information. Exclusive information has economic value that is often substantial for the person holding it.[18]When two or more persons enter into a contract, there will no doubt be a significant exchange of information in order for both sides to perform their contractually stipulated obligations. In light of the need to furnish certain information about each side's financial and business practices, it is imperative for the contract to contain a strongly worded confidentiality clause. The higher the level of confidentiality, the greater the need to establish a consistent practice of the parties in the long run, a practice which is so very important especially in business contracts. This clause should preclude both sides from divulging any and all information that is shared during the course of the transaction. Of course, this is particularly important when there is valuable intellectual property at stake.[19] However, the exception to this principle is the information that: (1) is or will be in the public domain; (2) is under the obligation to be disclosed pursuant to the applicable laws or regulations, in order to protect the legal order or morality of the society; or (3) is required to be disclosed by any party to its shareholders, or the creditors from the principal transaction. Finally, there is often a close connection between the Obligation of confidentiality and the permitted use. It certainly happens that the information finds its way to persons who have no right to use it, for example to an expert appointed to judge the value of a formula and to report on it, but more frequently the information is provided so that it may be used, and the confidentiality clause often contains provisions as to how the information can be used.[20]

(c) Jurisdiction

[16]https://www.eversheds-sutherland.com/global/en/what/articles/index.page?ArticleID=en/Data-Protection/model-clauses-data-transfers-summary261015 [20.12.2020].

[17]*Model Clauses for the use of the UNIDROIT Principles of International Commercial Contracts*, 7.

[18] Marcel Fontaine, Filip De Ly, *Drafting International Contracts: An Analysis of Contract Clauses*, New York: Transnational Publishers Inc., 2006, 231.

[19]https://www.contractworks.com/blog/6-key-clauses-found-in-commercial-contracts [16.12.2020].

[20] Marcel Fontaine, Filip De Ly, op. cit., 232-233.

"Any suit, action or proceeding seeking to enforce any provision of, or based on any matter arising out of or in connection with, this Agreement or the transactions contemplated hereby may be brought in any federal or state court located in the […], and each of the parties hereby consents to the jurisdiction of such courts".

These days, cross-border transactions are fairly routine, both in the domestic and international sense. When the parties to a contract are located in more than one state, or perhaps more than one country, it may not be clear which state's laws govern the arrangement. Therefore, business contracts should always specify the state that will have jurisdiction over the agreement, so that it is perfectly clear which laws are applicable.[21]

(d) Dispute resolution

"The Parties agree to attempt initially to solve all claims, disputes or controversies arising under, out of or in connection with this Agreement by conducting good faith negotiations. If the Parties are unable to settle the matter between them, the matter shall thereafter be resolved by […]".

In many contracts, it is now common practice for firms to include an alternative dispute resolution clause (ADR Clause), requiring the parties to submit primarily to arbitration or mediation prior to or in lieu of seeking a remedy via litigation. This is generally a faster, cheaper way to solve contract-related problems, although some contracts still allow for traditional legal recourse.

(e) Penalty clause

"Any violation of the provisions stipulated in Articles […] above shall be sanctioned by the payment of an indemnity at least equal to the remuneration received by the […] during the last six (6) months of the existence of this contract, although the […] reserves the right to prove a greater prejudice and to obtain the cessation of the violation and due compensation by all legal means".

Penalty clauses are extremely common in international contracts. A penalty clause is an express provision in a contract. It places an obligation upon the party who has breached the contract to provide compensation to the aggrieved party affected by the breach. *A priori*, a penalty clause can be defined as one stipulating payment of a sum of money in the event of non-performance of a contractual obligation, with a purpose either of pure indemnification or of deterrence.[22]

(f) Force Majeure and hardship

"In the event either party is unable to perform its obligations under the terms of this contract because of acts, circumstances and events that fall within the scope Force Majeure and hardship, which are in fact beyond the control of the contracting party, such party shall not be liable for damages to the other for any damages resulting from such failure to perform or otherwise from such causes".

Commercial contracts often include Force Majeure or hardship clauses setting out requirements for establishing the existence of a Force Majeure or hardship event that prevents or impedes a party's performance of its contractual duties. These clauses combines the predictability of listed force majeure events with a general force majeure formula which is intended to catch circumstances which fall outside the listed events, i.e. provides several options for amendment or termination of the contract when circumstances make performance of a contract untenable.[23]When preparing the list of such actions, circumstances and events, it

[21]https://www.contractworks.com/blog/6-key-clauses-found-in-commercial-contracts[16.12.2020].

[22] Marcel Fontaine, Filip De Ly, op. cit., 300.

[23]https://iccwbo.org/publication/icc-force-majeure-and-hardship-clauses/ [20.12.2020].

is advisable for the contracting parties to always take into account what is provided by the legislation and case law and that of the arbitration.[24]

(g) Damages

"Because of the difficulty of measuring economic losses as a result of the breach of the foregoing covenants in sections […], and because of the immediate and irreparable damage that would be caused for which they would have no other adequate remedy, the parties hereto agree that, in the event of a breach by any of them of the foregoing covenants, the covenant may be enforced against the other parties by injunctions and restraining orders".

In light of the frequency of contract breaches in an effort to deter them, it is also standard practice for business contracts to contain clauses related to damages. In general, liquidated damages will be included, which is usually a predetermined amount that will be owed if one side fails to perform. Of course, a court may award other types of damages beyond that amount depending on the nature and impact of the breach.[25]

3. Conclusion

When choosing the applicable law, parties may wish to agree on neutral solutions, instead of submitting the contract to the domestic law of one of the parties. When this is the case they may opt for the law of a third country or they may decide to submit their contract to a-national rules of law, such as "principles of law generally recognized in international trade". The determination of such rules may be made through contractual clauses. Their number is considerable, while the author has decided to focus the research on seven of them and their ranking in this article is by no means coincidental.

In the first place is the clause by which the parties decide that their contract is subject to the relevant model clause. It is followed by the confidentiality clause that constitutes the trust and the keeping of secrets between the parties as the cornerstone of a sustainable business. The inclusion of such a confidentiality clause is imperative in the situations where the parties' confidential information will be exposed to the other. In business contracts there is often a foreign element involved and it is essential to ensure the jurisdiction selected best suits the context from a practical perspective. In these cases the clauses on jurisdiction come into play. It is important for the contracting parties to know in advance that in case of a dispute regarding the fulfillment of their contractual obligations, which procedure will be followed in order to resolve the disputed issue (dispute resolution clause). Once the contract is concluded, it has to be performed. Given the eventual possibility of non-fulfillment of contractual obligations, the parties anticipate such a situation by providing punitive clauses. Non-performance, however, is not always the fault of the other contracting parties, but may also occur due to actions or events beyond the control of the contracting parties, so it is important that the parties anticipate situations by providing for force majeure and hardship clauses. Finally, but not the last in importance, are the damages clauses. The parties will often attempt to determine in advance the amount of the damages due by the other party in case of breach, with an adequate liquidated damages clause.

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[24]Faton Z. Shabani, op. cit., 311.

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