

Party Autonomy – A New Paradigm without a Foundation?

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I. I. Introduction

A. Party Autonomy – The New Paradigm of Private International Law?

The rise of party autonomy in choice of law has been swift and massive. Party autonomy has become the unquestioned primary tool to determine the applicable law in contract law. The new Japanese Private international law Act is only one of many examples. Party autonomy is being used more and more in other areas of private law like tort, family, succession. Its principal justification is no longer questioned.

And some scholars and regulators want to go even further. Some scholars of regulatory law suggest party autonomy as a helpful tool for areas like bankruptcy or securities law. Law and economics scholars even suggest that party determination should be the starting point for the determination of the applicable law in every area of the law where this is possible. Scholars of contract law suggest that non-state law like the UNIDROIT Principles of International Commercial Contracts should qualify as a law that parties can choose. European law scholars suggest that party autonomy is required by EU law. Others even propose a human right to one's own choice of a legal order.

B. The Incompatibility with Traditional Methods

All of this is somewhat surprising given that party autonomy does not fit well within traditional methods of private international law. Party autonomy cannot be justified in a statist theory because party autonomy cares little about a law's own intended scope of application. It cannot be justified in a theory of acquired or vested rights, because when and whether rights are acquired is, in this theory, determined by states, not by the parties. Importantly, party autonomy runs counter to a theory of closest relationship, because parties are free to designate a law largely irrespective of such a relationship. And it is incompatible with a focus on governmental interests,

because governmental interests cannot be determined by private parties. In short, party autonomy is nothing less than a new paradigm of private international law.

This leaves only two possibilities. Either, party autonomy is a makeshift solution to an insoluble problem—Kegel’s famous suggestion that has not found much support. Or, it is a new paradigm. As such, then, it requires a foundation.

C. The Poverty of Theoretical Discussions

Given the radical character of party autonomy, it is surprising how little theoretical discussion there is on its theoretical foundations. Jürgen Basedow has recently pointed out that we rarely find more theoretical discussion than vague references to freedom. Horatia Muir Watt even speaks of party autonomy as the “foundational myth of private economic law.” Indeed, most presentations suggest that it does not matter that we have no justifying theory for party autonomy, because party autonomy has become so important that we must deal with it anyway. And it does not matter how we justify limitations to party autonomy, because those are within the realm of each state. But that must be wrong. If we want to understand the role of party autonomy, we need to develop a theory that underlies it. Moreover, if we want to determine the scope that party autonomy should have, we cannot do so without a theory.

Today I want to suggest that we do not have such a theory. Instead, we have two paradigms—and internationalist one, and a substantive law one—and no basis on which to choose between the two. My suggestion is that we should not choose between the two, but instead develop a different paradigm that I call a transnationalist one. Today, in the brief time I have, I can offer no more than preliminary thoughts towards such a paradigm. And I leave for another day development of the underlying theory of transnational law.

II. Two Paradigms

A. The existing paradigm: party Autonomy as a quasi-connecting Factor

Presentations of party autonomy in recent textbooks typically proceed in two steps. The first of these is to present party autonomy—that is, party designation of the applicable law—as a quasi-connecting factor, and to discuss in what areas of the law party autonomy is available. In the second step, the, so-called limits to party autonomy are discussed. Such limits can concern the types of contracts, for example employment contracts. They can concern the legal systems that can be chosen, for example non-state laws. And they can concern the types of rules that remain applicable despite a choice of law by the parties, in particular so-called mandatory laws.

This structure is reflected in most codifications of private international law. For example, in the regulations on “juridical acts” in the new Japanese Act, party autonomy is presented as the starting point in Article 7; Article 8 provides for an exception for situations in which no party determination has taken place. These rules are then followed by the exceptions for specific contracts (consumer contracts (Art. 11 paras. 1, 4), labor contracts (Art. 12 para. 1). Further restrictions through internationally mandatory norms are not even mentioned, though it is understood that they remain applicable at least when they are Japanese.

With this structure, party autonomy is placed squarely within an internationalist paradigm. Here, party choice functions just like any other connecting factor—it designates an applicable law at large.

1. Rule and Exception

We should note from the start that this presentation implies certain biases. The first of these is that of *rule over exception*. In the classical presentation, party determination of the applicable law is the rule, limitations are the exceptions. In this scheme, once party autonomy has in principle been established, the burden of

argument lies with those who suggest limitations. This is how the debate is usually presented.

But it is not at all clear why this relation between rule and exception should always be the case. To take just one example, why should the impossibility to choose non-state law be viewed as a limitation to party autonomy in need of justification? There may of course be good arguments in favor of such a choice. But it seems that the burden of argument should lie with those who favor it, not those who oppose it. If party autonomy serves as just another connecting factor, it would be *prima facie* surprising if it could designate a law as applicable that cannot be applicable on the basis of any objective connecting factor. This suggests that the choice of non-state law is a matter of scope, not of limitations. And this suggests, further, that the rule/exception relation more generally needs to be questioned.

2. Selection and Deselection

A second bias implied is that of *selection over deselection*. We often overlook that party choice does two things simultaneously: it designates a law as applicable that would normally be inapplicable, and it designates a law as inapplicable that would normally (that is: absent party determination) be applicable. This latter part, deselection is, for some purposes, even more important than selection. After all, what mainly distinguishes party autonomy from mere freedom of contract is the ability of parties to deselect laws that are, in substantive law, mandatory and could therefore not be derogated through freedom of contract. Nonetheless, we rarely speak, normally, of deselection of applicable law (or *Rechtsabwahl*). But arguably, what is in need of justification is not the ability to select a law, but the ability to deselect a law that would normally be applicable.

B. Party Autonomy as Freedom of Contract and its Extension

It is worth remembering that this internationalist paradigm of party autonomy as a quasi-connecting factor is an accident of history. When party autonomy was first

proposed in the 19th century it was viewed, in principle, as a mere extension of contractual freedom. (Of course, contractual freedom was by then a relatively recent invention, too.) Parties could choose a foreign law on the basis of, and in principle within the limits of, party autonomy as granted by the objectively applicable law. Such party autonomy was confined by the *ordre public*, but what exactly this was and how it differed from mandatory rules was not clear.

1. Rule and Exceptions

Viewing party autonomy as an extension of freedom of contract also creates biases. Remarkably, these are opposites of the internationalist model. The first bias concerns, again, *rule and exception*. Now, however, the rule is that party autonomy remains within the limits of freedom of contract under domestic law. That a mandatory law of domestic law should be inapplicable because of the international fact pattern is the exception. This means that now the burden of argument lies with those who argue for the *inapplicability* of a mandatory rule in the international context.

2. Selection and Deselection

And a second bias concerns again the relation between selection and deselection. In this paradigm, however, the whole emphasis is on *deselection*—the question to what extent freedom of contract allows the parties to avoid mandatory laws. This is so because domestic law serves as the starting point. Selection, by contrast, is largely ignored in this paradigm. This is so because, when foreign law applies merely on the basis of freedom of contracts, its selection is no different from the incorporation of any random set of rules. As concerns selection, in other words, there is no difference between law and non-law. In other words, it is not clear in what way selection is something other than mere contractual freedom, or: in what way what is selected is actually a law, and not just a number of rules.

C. Shortcomings

We can see, I think, that both paradigms have mutual blind spots. What is the rule for one is the exception for the other, and vice versa. Where one of them focuses on selection and ignores deselection, the other focuses on deselection and has no clear understanding of selection.

But both paradigms also suffer from common shortcomings, and these are perhaps more important. Most importantly, both paradigms rest within the methodological nationalism that defines, in general, the dualism of private international law and substantive law. Substantive law remains nationalist insofar as it treats party choice of law as though it were just another example of domestic contract making. Private international law by contrast locates facts within one legal order, and thus domesticates them. Together, they suggest that one legal order alone can apply.

Now, already in cases of freedom of contract, we never have only one law that applies. We always deal with a combination of at least two laws. These are the official law of the state, and the privately made law of the parties—regardless of whether we consider the contract as law (as does, famously, the French Code civil in its Article 1134), or not.

What gets interesting in the private international law realm is how the relation between law and contract plays out. In the domestic realm, the contract is clearly subordinate to the law. That is, freedom of contract is granted by the state, and at the same time exists only within the limits given by the state.

Arguably, for international transactions, party autonomy reverses this order. Now, the state's law is subordinate to the contract. This is so because state law applies only due to a grant by the parties, and at the same time only within the limits of the parties' choice of law clause.

Where we have actual theories of party autonomies, this reversal of hierarchies is openly acknowledged. One example can be found in the literature on regulatory competition, or on "law as a product." Here, the idea is that lawmakers compete, in a "law market", for attention by parties. Parties, like consumers, pick the law that they

like best. There are many problems with the idea of regulatory competition, but one is especially relevant here: Markets (insofar like contracts) require a framework within which they can function. Typically, this framework is provided by the state. But obviously, when states are market participants they cannot, at the same time, be the ones to provide the framework.

Another example of such subordination has recently been proposed by Basedow. He suggests that party autonomy follows from the principle of personal freedom, which, as a human right, is prior to the state. And he strengthens this argument with his suggestion that even sovereignty itself is based in autonomy, namely in a social contract. Again, there are several problems with this argument. The most important one for this context, however, may be that it is unclear why such a choice by the parties should be binding—not just states and adjudicators, but even the parties themselves. Basedow suggests that, whereas natural freedom cannot justify a binding force of a contract for a future, it can justify the effectively dispositive character of the choice of law. Yet what is at stake, in party choice of law, is not effective (physical) disposition but rather its legal recognition, and here the same problem emerges for dispositions as does for obligations.

III. Structure of a new theory

A. Towards a transnationalist paradigm

If we want to develop a theory of party autonomy, we should, I believe, first reassess the hierarchical relation between state and parties. I want to suggest that a hierarchical relation does not grasp the complexity of this relation. Take the example of commercial agency law in the European Union. Parties tried to avoid its application through a choice-of-law clause choosing Californian law. The state responded by declaring the internationally mandatory character of EU law. Parties in turn tried to avoid this through choice-of-court agreements, but the state again responded by refusing to enforce such agreements. When parties tried to avoid state

courts altogether by going to arbitration (which might ignore those mandatory rules), the state responded by denying validity to arbitration agreements, too.

We could read this story as one in which parties always manage to find new ways to escape the regulatory scope of the state. Or we can read it as a story in which the state retains its dominance, by enforcing its mandatory rules ever more aggressively. But neither does not seem to grasp the back and forth involved in this story. In reality, parties can set themselves above the state through choosing the applicable law; states, by contrast, can set themselves above the parties through determining the scope of party autonomy. It seems more fruitful to see both, *prima facie*, on an equal level—if only, at first, for hermeneutical purposes, to avoid the respective biases discussed before.

If we take seriously this hypothesis that state and parties are coequals, what follows? We find, then, a different kind of relation between contract and state. The contract, on the one hand, is truly transnationalized; it exists detached from the state. This is true for both its substantive part and its choice-of-law part. However, in order to achieve meaning and enforceability, it requires linking to one state order. We should not understand this linking as a relation of subordination, however: neither is the state subordinate to the parties, nor vice versa are the parties subordinate to the state. Or: each is both at the same time, dominant and subordinate.

B. Starting point: mandatory rules as the field of contention.

What are consequences of these findings for a theory of party autonomy? First, we see that what makes party autonomy contentious is not the ability for parties to determine what rules apply in their relation. This is a freedom they already have under freedom of contract. This implies that the scope of party autonomy can never be narrower than that of freedom of contract under the applicable law. What changes is merely the nature of this contractual freedom which has now become transnational: it is no longer freedom of contract as granted by one state law or

another (and thus tied to a legal order) but instead one of transnational freedom of contract.

Nor is an issue contentious that has occupied private international lawyers for considerable time, namely the issue of so-called internationally mandatory rules. Although this is an issue for private international law theory in general, it is not a problem for the paradigm of party autonomy. This is so because these rules apply regardless of whether we follow an internationalist or a freedom of contract paradigm. In fact, this is again an area well-known from state law, namely state regulation. Again, regulation changes its nature once it becomes transnational. Here, through internationally mandatory rules, the state actively regulates and designates the outer boundaries of freedom of contract. This regulation is transnational, too—it consists of the sum of such mandatory rules from all interested states.

What is contentious is merely whether, and to what extent, party autonomy can go further than freedom of contract. This is the third space of transnational contracts, a space that does not exist in domestic law. Notably, the boundaries of this space are always contested: parties try to extend it, states try to limit it. This is the space that needs to be explained by a theory. In other words, we need not explain freedom as such; we need to explain the existence of a space between domestic and transnational freedom.

This is a central insight. It is of course not a new insight, but it is quite important. Many theorists suggest that party autonomy follows, somehow, from individual freedom. They invoke liberal philosophers like Kant, Hayek, Rawls and Nozick (and ignore, conveniently, others like Hegel.) But now we see clearly that it is not enough to show that these philosophers can support freedom of contract. Nor would it suffice, even, to demonstrate that a certain philosophy, like libertarianism, could support unlimited freedom of contract. Instead, what we would need is a conception of personal freedom that supports a difference between freedom of contract within the state and freedom to choose the applicable law in transnational contracts. None of the philosophers usually cited has such a theory.

Note, however, that this third space is not a constant. Without being able to prove it I think we can see it becoming smaller and smaller. On the one hand, a general trend towards liberalization means that contractual freedom is on the rise. On the other hand, we see that more and more rules that used to be mandatory merely in a domestic sense are now becoming internationally mandatory. Instead of a constant space, then, we have a dynamic contention of both boundaries of this third space.

C. Selection and Deselection

We can look at this space more specifically. Instead of treating party autonomy as a whole, we should focus on its two aspects separately—that of selection, and that of deselection.

1. Selection

Selection is the simpler part. By and large, we need no new theory to explain why parties can choose rules that apply to them. We can derive such a theory from general theories of freedom of contract. The only thing that we need to explain is whether parties are bound by the mandatory rules of the law they choose, or whether they can deviate from it. In freedom of contract, such binding force is quite limited. Of course, parties can lay down meta-rules that limit the ways in which future contract changes can happen, but any such meta-rules can of course be ultimately overcome by contractual agreement.

For party autonomy, the question is trickier. If party autonomy functioned like an ordinary choice of law rule, it would designate a governing contract law, together with its binding rules. In principle, that is what the doctrine requires, but of course this result is somewhat strange: Although applicability of that law would follow from the parties' choice alone, that law would nonetheless limit the parties' freedom. Indeed, some have suggested to ignore a party choice if it leads to a law that would invalidate the contract. Such a result seems to strengthen autonomy, but in some ways it weakens it: it means that parties are unable to choose a law completely, including its binding rules.

2. Deselection

I want to leave this open for now because I want to focus on the more important aspect—deselection. The crucial question is why parties should be able to deselect laws that would normally be applicable. Of course, putting it like this is somehow question-begging: if the applicable law is determined by party choice, there is no other applicable law whose rules would need to be deselected in the first place.

Let me start, first, with what is relatively unproblematic. What is unproblematic are the negative *ordre public*, and so-called internationally mandatory rules. Although both of these issues are often discussed as limits to party autonomy, both are really general problems of private international law—both determine the applicability of certain rules regardless of the normally applicable law.

The most interesting area is the area of ordinary mandatory rules—the rules that are binding in domestic contract law but can be deselected through a choice of law. Sometimes it is argued that such deselection is unproblematic because it merely leads to another set of applicable mandatory rules, those of the chosen law. But this is unconvincing for two reasons. First, as we have seen, it is not always clear that the rules of the chosen law are actually mandatory in fact. Second, the argument assumes the equivalence of legal orders. Such equivalence may or may not be an axiom of traditional private international law. But it cannot apply to party autonomy, where parties can choose the applicable law based on the precise content of the mandatory rules. This is so especially where parties can select different laws to govern different parts of their contract.

How can we justify the deselection of rules that would otherwise be applicable? Maybe the best way is to start from the situations in which such deselection is impossible. This is so in two cases. The first is that of so-called internationally mandatory rules—rules, in other words, that are considered especially important. This suggests that other mandatory rules are considered less important the more international the contract in question is. In this sense, freedom of contract becomes bigger the more the contract is detached from a legal system.

The second is in special types of contract, like consumer or employment contracts. In these areas, boundaries of substantive contractual freedom are effectively expanded into private international law. Effectively, consumer contracts and employment contracts are governed by (at least) two sets of legal rules: those of the chosen law, and those of the law determined by objective criteria. But the scope of the chosen law does not go beyond that of freedom of contract.

D. Implications for the choice of non-state law

(If time allows) Let me discuss some implications for the choice of non-state law, though I suppose these are quite obvious by now. First, the problem with such choice is largely not selection but deselection. Much ink has been wasted on this obvious point. In other words, it is uncontroversial that the UNIDROIT Principles can be chosen. What is problematic perhaps is whether the parties can derogate from the Principles' own mandatory rules (Art. 1.5). But this may be a more theoretical problem. What the Principles declare mandatory is, essentially, a principle of good faith. Such a principle permeates the whole text. Parties unwilling to submit their contract to such a principle are unlikely to find the UNIDROIT Principles to be an attractive law anyway, regardless of whether some of their rules are mandatory or not.

The other question is whether, and to what extent, such choice leads to the deselection of state laws that would otherwise apply. The Principles themselves are famously unclear on this point. Their Art. 1.4 suggests that mandatory rules remain applicable and leaves open, deliberately, the question whether this means internationally mandatory rules or any rules. The question has also not been of much practical relevance.

So far, the UNIDROIT Principles are rarely chosen in practice, although such a choice would be possible in practice. This could change with the new Hague Principles, on which Prof. Nishitani will report, but I doubt it. The Hague Principles strike me as unclear on this point. On the one hand they suggest that non-state law like the UNIDROIT Principles can be chosen instead of state laws. On the other hand, the

very fact that they are referred to as “rules of law” seems to imply that what is at stake is more the selection aspect than the deselection aspect. In the end, the important problems are not resolved.

As a doctrinal matter, the issue is unproblematic: although states have traditionally allowed only state law to be eligible by the parties, there is no reason why they should not extend electibility to non-state laws (as the Rome I Regulation in its draft version did.) As a theoretical matter, selection of the Principles is unproblematic. Deselection of otherwise applicable law, by contrast, seems unwarranted. If the UNIDROIT Principles explicitly present themselves as an expression of contractual freedom, then no reason is apparent why countervailing regulatory interests should be less relevant.

E. Towards a Theory?

As I said in the beginning, I cannot develop a full theory of party autonomy here. But I can, in lieu of a summary, at least sketch its conditions.

- A theory of party autonomy need not explain freedom of contract at large. Instead, it needs to explain why there exists a difference between substantive freedom of contract and party autonomy. In other words, a theory of party autonomy needs to be, first and foremost, a theory of rules that are mandatory domestically but can be deselected through a choice of law clause.
- A theory of party autonomy is not a theory merely of selection but also of deselection. It must therefore, in the first place, be a theory not merely of a chosen law, but of the relation between the chosen law and the law that applies in the absence of a choice.
- In view of the practice of party autonomy, we can see two coordinates of the scope of party autonomy for international contracts. The first concerns their *international* character: the more international, detached from states, a contract is, the more justification there is for deselection. The second concerns their *contractual* character: the more a contract results from free

and equal bargaining (as opposed to a consumer of employee contract), the more justification there is for deselection.

- Finally, the ongoing transnational competition between parties and states means that a theory cannot be static but must be dynamic. It must account, in particular, for the shift of rules between a domestically mandatory and an internationally mandatory character.