I. Introduction

CISG is considered one of the most successful international uniform laws.

Fifty six out of the current seventy eight Contracting States – has chosen to accede to the CISG without any reservations. It has been signed
by most countries in the world,¹ but not from others, some of them major commodities trade players like Brazil, Venezuela, Malaysia, and United Kingdom. The reason why those countries have not ratified CISG are not clear, very likely because CISG is not within a political agenda of the decision makers. Some speculations in UK have been around for a while, (in italics my comments):

- The Convention would be good news for lawyers but bad news for clients. (false, there are very few CISG cases in CLOUT in relation with the amount of international trade figures published by the World Trade Organization).

- Implementation would involve a greater number of disputes (It has not happened in the countries who have ratified CISG)

- There was a danger that The City of London would lose its edge in international arbitration and litigation. (Agreed. Why pay London barristers and solicitors when same quality of services can be provided by others?).

- The rules of arbitration on international associations based in London, works well without CISG see GAFTA (grain, animal feed materials, pulses and rice) or FOSFA (The Federation of Oils, Seeds and Fats Associations). Works well for FOSFA and GAFTA arbitrators, most of them based in London. However members of these commodities associations include producers and processors, shippers, dealers, traders, brokers and agents, superintendents, analysts, shipowners, and others services providers who are located all over the world.

This paper wishes to demystify the role of usages in doing international business transactions. On one hand, proof a usage is not easy and burden of the proof is for who invokes a particular usage. (Up to now the author has not seen one single arbitrator or judge procedural order requiring to provide further information on a particular trade sector or usage). Evidence on usages should cover (among others),

a) Its existence as a fact (not law).

b) Its validity under the applicable law,

c) It was known or ought to be known

d) It was widely accepted in the trade sector (not only in a particular chamber of commerce or a reduced group whose membership is not mandatory and/or from a group where parties were no members),

e) It existed at the time contract was signed and at the time it was performed

f) It was not only municipal usage, and if so, it was not an established practice between the parties,

g) It not was against public order

h) It is relevant to the controversy between the parties.

i) If it leads or not to a substantial breach of the contract

On another, we will show in this paper the high risk of the application of “usages” widely known by the parties and the trade sector, but their formation was manipulated by few interested players in the financial sector for their own profit.

II. The Usages

Let’s start our presentation with one example, as illustration, let’s focus on how the same product (Diesel D2), may have a different price according with the city where is located and not necessarily reflect the logistic costs. Prices in US Dollars. Using the same Platts index (Information of 29, November 2011).

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Platts is a company, subsidiary of Mc Graw Hills. Platts is a provider of energy and metals information and a source of benchmark price assessments in the physical energy markets. Platts was founded in Cleveland, Ohio more than 100 years ago: in 1909 by Warren C. Platt (1883-1963) to provide “reliable market-based price information” on the oil industry. From an original focus on the oil industry, Platts gradually expanded its purview to include metals, shipping, and all energy-related markets: oil, coal, natural gas, electricity, nuclear power, petrochemicals, renewables, and emissions.

The crude oil and diesel Platts index information is used throughout the energy valued chain (Platts has 10,000 customers, in 150 countries). The index is used by core energy supply chain, consultants, financial services, lawyers, governments, retail, commercial associations, suppliers, manufacturers all over the world. Furthermore Platts prices are used as benchmarks for contract settlements. (Note: Only spot sales are under CISG scope unless it is expressly excluded)

Please keep in mind that according with Art. 2 (d) CISG does not apply to sales investment securities or negotiable instruments.

Platts price is the London 4:30 p.m. time.
In the previous illustration, can be seen how physical crude oil is traded in the eWindow of Platts. On the right column is the name of the participants who are offering crude oil. And the orange cube in the graphic is the moment in which it is accepted by a buyer. Note that very
few companies are selling and buying, and from them the PLATTS index is formed (with great transparency: is open for all the participants to read the yahoo chat on the negotiations), but only 13 companies where active in fixing the Platt index that day, from the 240 companies registered and from the 10,000 subscribers. If one participant offers the product at significant discount is invited by Platts to bring its product at a much more higher price, so it does not distort the price of product offered.

In 2010 the difference in between the Brent (other index), and the WTI the index used for the West Texas Intermediaries was between +/-3 USD/bbl compared to West TI and OPEC Basket, however since the autumn of 2010 there has been a significant divergence in price compared to WTI, reaching over $11 a barrel by the end of February 2011 (WTI: 104 USD/bbl, LCO: 116 USD/bbl). Many reasons have been given for this widening divergence ranging from a speculative change away from WTI trading (although not supported by trading volumes, Dollar currency movements, regional demand variations, and even politics). In February 2011 the divergence reached $16 during a supply glut, record stockpiles, at Cushing, Oklahoma and is currently above $23.

In other words: Depending the index selected to fix the price of the crude oil, could be the difference (in a big vessel of 150,000 metric tons, since 7 barrels are equal to one metric ton, would be USD$ 24,150,000) just for the difference in the index selected!!!

Other than the price based on premium or discount over the index is very important to have the specifications certified as agreed by the parties due to the fact that quality is different from one crude oil to another.²

Who is taking advantage of the difference on price in the different regions? Other than the large trading companies, mostly the investment banks who are authorized by the US Federal Reserve not only to trade on

² For a full description of the qualities of crude oil and their regions can be seen TOTAL tests at: http://www.totsa.com/pub/crude/index2.php?expand=5&iback=5&rub=11 &image=middle_east. In practice is very frequently to use the services of SGS (http://www.fr.sgs.com) the world’s leading testing, inspection, certification and verification company who provides independent buy expensive services to the industry.
physical commodities but also to own tanks and other assets in Europe and Asia (not in North America). (See Below, Section IX). Note in the list of participants in the eWindow that most of them are also hedging their risk using financial derivatives.

III. The CISG

CISG Article 9

(1) The parties are bound by any usage to which they have agreed and by any practices which they have established between themselves.

(2) The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.

ARTICLE 9 The Hague Convention

1.- The parties shall be bound by any usage which agreed and by any practices which they have established between themselves.

2.- They shall also be bound by usages which reasonable persons in the same situation as the parties usually consider to be applicable to their contract. In the event of conflict with the present Law, the usages shall prevail unless otherwise agreed by the parties.

3.- Where expressions, provisions or forms of contract commonly used in commercial practice are employed, they shall be interpreted according to the meaning usually given to them in the trade concerned.

ARTICLE 12

For the purposes of the present Law, the expression “current price” means a price based upon an official market quotation, or, in the absence of such quotation, upon those factors which, according to the usage of the market, serve to determine the price.

Usages to which the parties have “agreed”, along with practices that the parties have established, are covered by article 9 (1); usages that the parties “have impliedly made applicable to their contract” are addressed in article 9 (2). In any case, according to Turku Court, “any applicable practice or usage has the same effect as a contract. (Finland, 12 April 2002).
Obviously the validity of usages is outside the Convention’s scope; the Convention addresses only their applicability. As a consequence, the validity of usages is governed by applicable domestic law. If a usage is valid, it prevails over the provisions of the Convention, regardless of whether the usage is governed by article 9 (1) or by article 9 (2). (UNCITRAL DIGEST 2012)

**Reasonableness**

Reasonable person is a prudent individual, but not an specialized one. During the drafting of the CISG, Chinese delegates unsuccessfully proposed that only “reasonable” usages would be binding on the parties. While some delegates responded that any usage that attracted the requisite international status would necessarily be reasonable.

Mc Doughlad, Lasswell and Chen proposed test for *opinion juris* is that of “*reasonableness*”. In our opinion would be useless to enter into the discussion if an usage is reasonable or not, since it was intentionally removed at CISG. The criteria is if the parties “knew or ought to have known”. Obviously we are facing *a time limitation*: should be knew or ought to have known at the time in which the contract was concluded. In other words: the usage should be previous to the contract and parties should not agree on contrary on it.

A second test is the *opinion iuris*: Some scholars have endorsed a revised definition of *opinio juris*, without *inveterata consuetudo*, Thirlway has identified the possibility that *opinio juris* includes not only a belief that a norm is already law, but a belief that it should become law. Jean Charpentier has likewise that the *opinion juris* consist of a sentiment that of the principles is useful, and not the conviction of their mandatory role. (*un sentiment de l’utilité des principes et non pas une conviction de leur valeur obligatoire*). Before a rule has come into being «*any shared ‘belief’ will be in respect of how the rule could arise, of the legal relevance of different instances of behaviour, and perhaps of the desirability of the rule arising*”. (LEPARD 2010).
The underlying idea on the test of “knew or ought to have known” is that of “expectations” where parties doing international business expect future behaviour in conformity with what is familiar to them from previous trading experiences. A behavioural regularity that results from business parties engaged in international sale of goods pursuing their interests.

As can be seen: The knew or ought to have known test is a problem of evidence, burden of proof, cost, and time.

Article 9(1), as opposed to Article 9 (2) does not require to be “widely known“. Usages and practices of the parties or the industry are automatically incorporated into any agreement governed by the Convention, unless expressly excluded by the parties. Usages not only supplements’ parties will in contracts but also take precedence over conflicting positive provisions of CISG (oberster Gerichtshof, Austria 21 March 2000). This Austrian decision not only delineates the requisite extent of parties’ familiarity with a trade usage in order for them to be bound by such custom; at the same time, it touches on the spatial and geographical considerations of the provision (WALKER 2005).

Note that no definition of usages, or practices. Usages (Art 9-2) should be widely known and (*not or*) regularly observed. Therefore only those usages who are both known and regularly observed can be binding. It is not only international trade usages which can bind parties, While the provision mandates that usages be widely known in the international trade of the relevant industry, it requires neither that all parties know about the usage (ULRICH 1999, WALKER 2005) nor that the usages be known worldwide (BONELL 1987, WALKER 2005). In fact, parties may even be bound by a local usage if such custom is common to local commodity exchanges or fairs and trade exhibitions. The Austrian decision:

One can still presume an exception for usages which are in force at certain stock markets, trade fairs or deposit sites, as long as the usage is also regularly observed there in the trade with foreigners. Furthermore, the possibility does not seem to be excluded that a
foreign tradesman, who is constantly active in another country and has already formed a number of transactions there, is bound by possible national usages.

IV. Usages as Applicable Law Used in Arbitration

The usages also play a subsidiary and secondary role in Arbitration. Arbitrators have to take into account the usages (Since the time of the Geneva Convention (1962) UNCITRAL Model Law Art 28, UNCITRAL rules Art 33(3), ICC Rules 2012 (Art 21 (2). Maritime arbitration rules at the Chamber of Commerce and Industry of the Russian Federation Art 20.2; The Stockholm Chamber of Commerce rather prefer to use “rules of law (Art 22), and the LCIA rather prefer to use “rules of law”.

In 1987 the UK courts declared null and void an award based on Lex mercatoria. (DST v. Rakoil, 2. LLOYD’S REP. 246, 251 (1987)

V. Advantages of the Incorporation of Usages

1.- Establish reasonable parameters: For example what would be a reasonable “time” according with the circumstances if one party requested “urgently” a spare part for a car.

2.- Allocation of responsibility for the delivery of goods.- As would be the ICC- Incoterms.

3.- To determine if the package and/or logistics for the goods. For example if bags of 50kg of cement inside of plastic bags for 2 metric tons, instead of the use of containers was or not a substantial breach of the contract. The plastic bags are fully used for cement and sugar trade, but not for wines.

4.- In determining the coverage of an insurance policy.- There are broad practice among insurance and re-insurance companies on who has the burden of proof.

5.- To establish the quality of the goods. For example scope of the quality certificates if not used SGS services
6.- To determine the scope of guarantees such as:

- UCP 600 (Uniform Customs and Practice for Documentary Credits).  
- ISBP (International Standby Practices),
- URUCB (Uniform Rules for Contract Bonds),
- URUCG (Uniform Rules for Contract Guarantees),
- URDG (Uniform Rules for Demand Guarantees) y
- URR (Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits).

7.- To be used to fix a price (the price is an essential element for the validity of a sale/purchase agreements under most of jurisdictions). As

3 UCP 600 (2006). See BAKER Walter and DOLAN John “Users Handbook for Documentary Credit Under UCP 600” Paris. ICC. 2007 the issuing bank chooses to follow the ‘independent’ principle of UCP by not enquiring into the nature of the underlying transaction. As stated in Article 3(a), UCP500:
The main burden of preventing fraud lies with the buyer. His failure to take adequate measures, misplaced confidence, short-sightedness, trust in conmen, naivety and trading with unknown companies and individuals without investigating their credentials were to blame for his loss. According to Mr Bernard Wheble:
‘Yet even if the main burden of preventing fraud should, and does, lie with the buyer, he could surely do with all the help he could get, and so far as the banks are concerned I feel they can usefully adopt an ‘educational’ role ... it would be of assistance to all, and especially to the trading areas referred to in Ellen and Campbell’s book [International Maritime Fraud, Sweet and Maxwell, 1981], i.e. trading areas which have gained operational autonomy before they have learned the basic principles of international trade, for they are all too often the victims of the fraudsters. Documentary credit operations into a highly litigious area of banking.


7 ICC, “Uniform Rules for Demand Gurantees” ICC Publication NO 458, 1994

illustration the above mentioned Platts index, but also it can be the Lon-
don Metal Exchange which does not sale or purchase physical commodi-
ties, LME offers financial futures and options contracts, but its price is
used to sale at discount or premium for aluminium, copper, tin, nickel,
zinc, lead, steel billet, cobalt (non PVC and plastics anymore due to lack
of transparency in the sector)

VI. If Usages are so Important Why Only Few Cases in
Courts?

Relatively very few international sale of goods contracts end up in
dispute resolution. UNILEX only refers to 902 cases since 1988 for the
trillions of transactions done in the world. Business practices are taking
place in a world in which the use of law and lawyers is not free and may,
even for parties to a sale of goods transaction be prohibitively expensive.
Just as an illustration, FOSFA arbitration rules 2005 states:

No person wholly or principally engaged in legal practice shall
be eligible to act as an arbitrator or empire” “Either party...
may not have presented or be represented by any member of
the legal profession wholly or principally engaged in legal prac-
tice”

Buyers and sellers frequently use standard forms, templates copied
from internet or obtained from chambers of commerce, industry as-
sociations etc. Buyers/Sellers do not see the contract as a governance
structure which can offer arrangements of differing flexibility and for-
mality depending on the choices made by the parties. International sale
of goods contracts very frequently does not include a clear description of
the transaction. When dispute arises its too expensive and takes to long
to recover damages from the counterpart.

From the very few CLOUT decisions published, -most of them
related to non-conformity of the goods- is reflected that usages are not
frequently invoke by lawyers/arbitrators/judges,. Why? The burden of
the proof of a particular usage is too high? The incorporation of usages
into the contract makes sense only where third parties can, at reasonable cost, verify compliance with the custom and apply it with accuracy?

What we have found is that only one Austrian case regarded to sector trade usages, the rest where issues more or less within a legal framework, (confirmation letters, interest paid or the INCOTERMS). The most relevant cases,

- Argentinean Court CLOUT 21.- Payment of interest in a sale agreement is an usage.
- Swiss Court (CLOUT 95).- Confirmation letter tantamount an usage Art 9(1) and was a binding practice between the parties Art 9 (2).
- German Court (CLOUT 276). The seller sent a letter of confirmation to which the buyer failed to reply. Court found that a contract already had been concluded between the parties prior to the letter of confirmation.
- Austrian Graz Court of Appeal (CLOUT 175) a seller who has been engaging in business in a country for many years and has repeatedly concluded contracts of the type involved in the particular trade concerned is obliged to take national usage into consideration.
- Swiss Court (CLOUT 221) On a purchase on credit, the court dismissed the plaintiff’s allegation that a usage existed and was known to the parties (article 9 (2) CISG), pursuant to which bank transfers have to be made to the seller’s account in the import trade.
- Austrian Supreme Court (CLOUT 240) held in athat the court of first instance should examine whether the conditions have met, in particular whether the usages were widely known and regularly observed in the trade.
- USA Court (CLOUT 447) Incoterm CIF is an usage (other cases deals also with INCOTERMS as usages, with more or less limitations, for a brief description on the discussions see UNCITRAL DIGEST 2012).
Austrian case (CLOUT 477). The frozen fish was not allowed to be imported into Latvia for human consumption as it was older than six months, and was therefore sent back to the buyer by its customer.

UNILEX has recorded the ICC award No 93333 (Switzerland 1998), Considering UNIDROIT Principles “usages”. Interesting because it was rendered just 4 years after the first edition of the UNIDROIT Principles were published.

Under Article 9(2) the prerequisites for incorporation of a usage are its actual or imputed knowledge by the parties, its international character, and its observation by parties to similar contracts in the trade. If those conditions are satisfied, there is no basis for rejecting the custom on the grounds that it arose other than from a bargain from few market participants.

There may be instance in which a member of the group would self-interestedly violate the custom, and thus undermine its conventional benefits, unless there is some deterrent. During the period of evolution, the primary enforcement mechanism will be extralegal, such as shunning within or dismissal from the group. Reputational enforcement may continue after the practice has become entrenched, but may be displaced or augmented by legal enforcement if the legal regime permits recognition of the custom, as under the incorporation strategy. If reputation sanctions are unavailable, legal enforcement becomes more important to induce compliance with the usage.

The basic critique made by contemporary formalistic scholars (Katz 2004) in the fields of contracts and commercial law is that trade usage, even when it exits, is considerable more complex, subtle, and heterogeneous than mainstream scholars and commentators have appreciated. The formalists argue that much regularly observed behaviour reflects not compliance with what the parties regard as customary legal obligation, but rather a conscious departure form those obligations for purposes of business goodwill or an implicit settlement of a potential contractual dispute. Generalist courts deciding disputed cases ex post, on this view, are unlikely to be able to determine if an usages was or not widely known by the parties at the time in which contract was formed.
VII. Usages are Confused With Other Legal Institutions

The importance of the trade usages is not limited to the will of the parties. For example if buyer and seller agree in using a lower quality of cement for a construction project, the usage may have also an integrative role in the interpretation of the contract, where the common good, in society plays also a role. However if the application of the standard (usage) is for a extra-contractual obligations, first the judge/arbitral tribunal shall enter to the issue of its own competence to decide on it.

An usage should not be confused with foreign law or with criteria of the reasonable person. (The CISG refers in other articles to the “reasonable person” (a prudent but not specialized individual). In Art 9(2) the standard is higher it requires to have the the knowledge of those who trade in that particular sector. Art (3) refers to a criteria for the interpretation of the contract. Neither is the same to customary international law (obligations between States) nor, an usage the General Principles of Law mentioned in the ICJ Statute Art 3 (1) (c).

The usages are not a synonymous of the romantic\textsuperscript{9} \textit{lex mercatoria}. In the same way that a part cannot be the whole. \textit{Lex mercatoria} includes aspects of public international law, uniform law, general principles of law, works from intergovernmental organizations, as the UNIDROIT Principles of International Commercial Contracts, customs not codified, usages published for a specific commercial association, model contracts, arbitral awards.\textsuperscript{10}

As Muthucumaraswamy Sornarajah (2011) states on lex mercatoria:

“lex mercatoria does not have any principles that are clearly identifiable and the ones that have been stated as principles of the system are so obvious that they could have been used without

\textsuperscript{9} BEWES, Wyndham Anstos, \textit{The Romance of the Law Merchant}. London: Sweet & Maxwell 1923

\textsuperscript{10} LANDO, Ole, \textit{The Lex Mercatoria in International Commercial Arbitration} (1985) 34 ICCQ 747
any resort to such nebulous theory.”\textsuperscript{11} “The attempt to create an international law on investment protection through purely private means did succeed to a large extent, despite the fact that its theoretical foundations were slim.”\textsuperscript{12}

VIII. Usages Under CISG Have a Very Clear Orientation Pathway

A) They need to be known or ought to be known. Its irrelevant the requirement of time and space. \textit{inveterata consuetudo}, is not a question of time but the knowledge an application in the trade sector. It is not needed to be universally known.

B) Should not be against mandatory rules. An usage cannot be against the local or national law. Also in order to be valid, under the applicable law, should comply with the relevant criteria of formation of contracts, including what in Civil Law countries is known as “vices of the will” such as the error when entering into a contract.

C) Burden of the proof. Under most jurisdictions what is not a law is a fact, and as a fact it should be proved. If the usage is not proved, the arbitral award will have a error in law. “A party asserting any fact has the burden of proving it by adducing appropriate evidence before the tribunal. Finding of fact are which an award is based can be challenged as errors of law if they are not based in evidence”.

If a usage is a “fact” (In Austria the question of whether a specific trade usage exits is a factual question)\textsuperscript{13}. The burden of the

\textsuperscript{11} Sornarajah, Muthucumaraswamy, “The International Law on Foreign Investment», 3a edición. UK Cambridge University Press 2011. p. 303

\textsuperscript{12} “It indicates not only the power of multinational corporations to create law but also, the existence of avenues through vehicle into law can be used as an instrument of private power through weak sources of law such as the awards of arbitral tribunals and the writings of highly qualified publicists. The role of later who are but individuals with partialities to certain views either because they believe firmly in them or because it is lucrative to do so, requires a view of international law not as scientifically neutral discipline but as a manipulable device which serves the interest of power”. Sornarajah, Muthucumaraswamy, Ibid. p. 305

\textsuperscript{13} www.cisg.at/10_34499g.htm
proof is to the party who benefits from it. The basic rule is actore incumebit probatio, In an Italian court decision rendered on November 26, 2002 reported by FERRARI (2005) “the party that alleges the existence of any binding usage has to prove it, at least in those legal systems that consider the issue as being one of fact or in which for other reasons the court is not obliged to gain proof of the usage itself”. Where the party that carries the burden of proof does not succeed in proving it, the alleged trade usage will not be binding upon the parties.

D) Cost/time assessment: If the time to know the usage and assess its impact into the contract of sale of goods is higher than the value of the contract, it would be not reasonable to spend in expert witnesses, analysis, etc.

E) Source. Its not enough that the usage is published by a chamber of commerce if join such chamber or association is not mandatory.

CISG does not define usages or practices. UCC does, but according with CISG Art 7, the construction of the contract has to be done taking into account the international character and the uniform interpretation (from which a reference to foreign law using comparative law technics, may not be mandatory to the tribunal, who for the procedure has to follow its own rules of procedure and accept or not the foreign law as an indirect evidence to the case).

The United States Uniform Commercial Code

UCC § 1-205. Course of Dealing and Usage of Trade.

(2) A usage of trade is any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question. The existence and scope of such a usage are to be proved as facts. If it is established that such a usage is embodied in a written trade code or similar writing the interpretation of the writing is for the court.
(5) An applicable usage of trade in the place where any part of performance is to occur shall be used in interpreting the agreement as to that part of the performance.

**IX. Empirical Approach**

CISG APPLIES TO ALL KIND OF GOODS, NOT ONLY PHYSICAL COMMODITIES. (SECURITIES AND NEGOTIATBLE INSTRUMENTS SUCH AS FINANCIAL DERIVATIVES ON COMMODITIES ARE EXPRESSLY EXCLUDED FROM CISG).

The key to economic growth is developing institutions that reduce transaction cost and facilitate trade. Today, companies divide their operations across the world, from the design of the product and manufacturing of components to assembly and marketing, creating international production chains. More and more goods are “Made in the World” rather than “Made in the UK” or “Made in France”. However market access is not easy, in author’s opinion most of the benefits are for those large multinational companies and its suppliers who can work together with governments to remove the non-tariff barriers on international. Barriers in certain sectors such as Agriculture are very well known, also the use of environmental, sanitary and phytosanitary measures. Lawyers and international consultants offers services on “trade engineering” helping big clients in dealing with customs valuations, subsidies, safeguards, countervailing measures, dumping practices etc. If a particular sanitary or phytosanitary label, package or procedure is requested by a buyer it may be argued that its an “usage” in the trade sector. However is noted that some countries protect its national producers imposing “safety” requirements to imports. For example United States imposes labels on free dolphins for all tuna imported into USA. Countries (not individual sellers) can go to the WTO dispute settlement body, but in most of the cases the seller has very limited legal resources to defend its interest.
The economy of Turkey, as one of the world’s newly industrialized countries is nowadays among the world’s leading producers of agricultural products, textiles, motor vehicles, ships, transportation equipment; construction materials, consumer electronics and home appliances, etc. CISG applies to all kind of goods, not only commodities. As a matter of fact, in most of the commodities trade CISG is surprisingly not invoked.

While the former industrialized countries are shifting their production to lower man-power cost countries, their economy is based mostly in services, and financial services is not the exception.

X. Specialization: It’s Not Enough Be Good at Detail, if the Forest Can’t be Seen For the Trees.

In a world where specialization is seen as the only way in which an individual or a country can get a competitive advantage the risk/cost of this specialization is the myopia in seeing what is happening since 1980 (year in which the CISG has been open for signature).
Competitive advantage is defined as the strategic advantage one country, business or individual has over its rivals. The term competitive advantage is the ability gained through attributes and resources to perform at a higher level than others in the same industry or market, implementing a value rating strategy not simultaneously being implemented by any current or potential player. Superior performance outcomes and superiority in production resources reflects competitive advantage. There are so many economy theories on competitive advantages, but as a fact we see in one hand that very few companies take the most part of the market share in the global economy. Just an illustration: for everybody is known the audit firms, “big four”, few automotive manufacturers, but also in raw materials, and food. For example 3 companies control the 66% of the global market of bananas and only 5 companies control 87% of the global market.

In other words. If a banana grower wants to sell directly to supermarkets he will be requested to provide Cavendish quality, 8 inches, in boxes of 44 pounds. His bananas must be transported over long distances from the tropics. To obtain maximum shelf life, harvest should come before the fruit is mature. The fruit requires careful handling, rapid transport to ports, cooling, and refrigerated shipping. The only way in which can be prevented the bananas from producing their natural ripening agent, ethylene. This technology allows storage and transport for 3–4 weeks at 13°C (55°F). On arrival, bananas should be held at about 17°C (63°F) and treated with a low concentration of ethylene. After a few days, the fruit begins to ripen and is distributed for final sale.

### World market shares of banana companies

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The competitive advantage of the three or five global banana companies is the same as most of the mining companies in Brazil, they own the ports, the vessels, the refrigerators... the cost for new comers is too high to compete. Who purchase bananas on CIF basis understands that it has to be shipped in refrigerated containers. Or who purchase coal for the metallurgic industry understand that the size of the stones I should be larger that if the coal would be used for the power industry.

While the share of industrial countries has shifted to emerging markets, countries that in the 80s were industrialized nowadays, rely in services for their economy. In the case of cities as New York and London in “financial services”. The “competitive advantage” theory is too easy to confirm and defend in economic terms, but very difficult to defend under a political science approach. If fact the so called banana republic is a pejorative political description of a politically unstable country that economically depends upon the exports of a limited resource (e.g. fruits, minerals), which usually has an impoverished working class are ruled by a wealthy elite. In practice, a banana republic is a country operated as a commercial enterprise for private profit, effected by the collusion between the State and favoured monopolies, whereby the profits derived from private exploitation of public lands is private property, and the debts incurred are public responsibility.

Such an imbalanced economy reduces the national currency to devalued paper-money, hence, the country is ineligible for international development credit and remains limited by the uneven economic development of town and country. Kleptocracy features influential government employees exploiting their posts for personal gain (embezzlement, fraud, bribery, etc.), with the resultant deficit repaid by the native working people who “earn money”, rather than “make money”. Because of foreign (corporate) manipulation, the government is unaccountable to its nation, the country’s private sector–public sector corruption operates the banana republic, thus, the national legislature usually are for sale, and function mostly as ceremonia government.
The competitive advantage relies in “speciality” companies and individuals require to be more and more familiar with small but very sophisticated area of knowledge and experience to do in less time and cost what others can accomplish. To have a competitive advantage in the financial sector, is necessary local approach but global solutions, bringing from every corner of the world business opportunities for the company/firm/individual.

Trillions of dollars is the amount of international trade every year, most of those transactions are among multinational corporations and their supply chains. The CISG is a success instrument not only for the number of ratifications but also because it has permitted a framework in which international sale of goods can be done under the same uniform legal umbrella. Since 1988 UNILEX (Edited by Michael Joachim Bonell) reports only 904 cases in which CISG has been applied. CLOUT (Case Law on UNCITRAL text) all UNCITRAL cases reported on all UNICTRAL instruments are 1191. UNILEX report 902 on CISG.

From those cases very few are on commodities. As mentioned CISG only applies to physical commodities, does not apply to securities, or financial instruments. The fact is that most of international commodities are trade through digital (not paper anymore) financial instruments and its derivatives not in physical commodities for several reasons. The reasons why nowadays are so much more securities trade than physical commodity trade are among others:

- Lack of reliable price references for certain products
- Lack of reliable price reference for certain locations
- Existing clients increasingly want price risk management in physically settled contracts
- Simplified accounting
- Board level familiarity
- Performance/credit concerns around fixed-price contracts with physical suppliers
- Derivative policy limitations, either for regulatory or governance reasons
- Credit considerations in certain jurisdictions, and with certain counterparts
- Increasing emerging market commodity focus
- Physical market participants are interested and provide liquidity
- Lenders support it with their corporate clients

That spontaneous law is a « fact » and its value as source of law depends of several factors, among others the interest of certain groups in its formation in Henri Battifol words: sa valeur comme droit depend d’autres facteurs... ces règles ne seraient qu’un moyen de domination des certains groupes, (Henri Batiffol 1973 p. 323). For the purposes of conflicts law the objective of security seeks to maximize uniformity in defining the legal and socio-economic consequences of transactions and eventually the selection an duplication of the corresponding law.

XI. Can Everybody be an International Trader?

The author considers relevant to highlight a very big risk: The specialists in London and New York care so much about what came out of their computers and so little about what came out of the real world, most of the traders on crude oil are more concern about futures than oil production. It is easy to find physical crude oil at discount or sugar (in Brazil no more than 5 companies are integrated and listed companies, the rest rely in the services of cooperatives of its members or use trading houses).

Whoever is out of the intimate circle of large physical commodities who play with the “financiers” is considered a “corrupt”, or “not serious”. In the last years was difficult to find corn, aluminium and other commodities because the price continued to increase. On copper cathodes, mining companies from Chile had their vessels in international waters waiting for the expiration of financial instruments, so after the clearing at the London Metal Exchange they can be re-directed to final destina-
tion. They use the vessels as warehouses and is practically impossible to purchase physical copper cathodes on spot basis.

Time ago, when CISG was drafted, traders on iron, copper cathodes controlled most of the market, nowadays, thanks to technology, communications, and the possibility to enter into direct agreements most of the international trade is done directly with the large multinational corporations, who sale at discount of what is the “index” price, that is fixed through the action of very small number of participants.

The fact that indexes such as LME (London Metal Exchange), ICE are used to determine the price of the physical goods (-selling with discount or premium to the index-) and that some of them as ICE Clear Europe guarantees contract performance by acting as an independent central counterparty to every futures and options contract traded on ICE Futures Europe. Safety, security and market integrity are vital to the exchange trading process. As mentioned, our experience shows that quality and price can be find in the real world cheaper than through the financial circles. Having access to the physical markets is about optimization and knowledge - it gives you the visibility of the market to make far more successful proprietary trading decisions in both physical and financial markets. However to do that its necessary be familiar with both the trade sector (specific and specialized industry) and be enough capitalized and specialized to take part in the financial markets.

This is known by the biggest investment banks, as Goldman Sachs, Citi, JP Morgan, Credit Suisse, among others, are also dealing with physical sugar, oil, diesel. The Holding of the investment banks owns tanks, warehouses, and other assets related to physical trade. Investment banks say in public that they do not want to be a trade house, but recognize physical transactions as a way to access price risk opportunities i.e. non-derivative vehicle to manage price. The documents made public by the Federal Reserve site reflect otherwise

14 http://search.newyorkfed.org/board_public/search?text=physical+commodities&Search.x=21&Search.y=5
“In last year’s second-quarter Securities and Exchange Commission filing, Morgan Stanley added the following new text to its lengthy Supervision and Regulation disclaimer:

“The company is engaged in discussions with the Federal Reserve regarding its commodities activities. If the Federal Reserve were to determine that any of the company’s commodities activities did not qualify for the BHC (Bank Holding Company) Act grandfather exemption, then the company would likely be required to divest any such activities.”

Since trading metal is covered by the 2008 USA Federal Reserve regulations, RBS trades with financial products backed by gold, silver, copper but also RBS trades with a liquid “concentrates directly from the mine” the liquid includes percentage of gold, silver, copper and other ore and is sold to refineries. Concentrate is not under the definition of metal Concentrates are not within the scope of regulations of the Federal Reserve.

Goldman Sacks has come under fierce criticism from companies such as Coca-Cola, which has accused it of inflating aluminium prices, Or also Sicilian orange juice producers accused Coca-Cola of the low price paid. So low that they prefer not to harvest the oranges. So much is said that JP Morgan, Goldman Sachs and Credit Suisse have loses in their physical commodities operations. However the same banks get profits from the warehouses of the physical commodities: “ As surplus metal stocks accumulated during the recession, profits at the UK-based Henry Bath (JPMorgan’s ownership of its global metals warehousing business) surged to more than $110 million in 2009 and near $80 million in 2010, about $1 million per employee per year, according to annual reports filed to UK Companies House in November 2011. These units could, in theory, be run as “merchant banking” investments, as with Metro, but

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15 REUTERS March 2, 2012
http://www.reuters.com/article/2012/03/02/us-fed-banks-commodities-idUSTRE8211CC20120302

16 Ibidem

17 Ibidem
that requires they be kept at arm’s length and divested within 10 years. In the authorization to Credit Suisse the Federal reserve of the US stated “As a condition of this order, to limit the potential safety and soundness risks of Commodity Trading Activities, the market value of commodities held by Société Générale as a result of Commodity Trading Activities must not exceed 5 percent of Société Générale’s consolidated

**Urgent Need For a Suitable Solution For Transactions Too Small and Too Big.**

The financial crisis was in certain way mitigated, making the problem bigger. According with US Bank Holding Company Act, a holding company who controls one or more banks is not a bank because it does not engage in banking itself. Therefore not subject to the legal restrictions.

Due to capital requirement, and experience in the trade sector it’s difficult to have the success of the big players, such as the investment banks or gigantic traders as Glencore or Trasfigura. The entry barrier is high. If a small or medium enterprise wishes to enter into international sale of goods, very likely sooner or later will have bad experiences with electronic business to business sites. Such as Alibaba Group, that although operates China’s largest B2B online marketplace and largest online shopping site and its worth $17 billion dollars. But attention, ALIBABA Group, (with its holding company in Cayman Island, who is not a signatory of CISG) does not take responsibility for being the electronic trade vehicle (not an agent?) by whom buyer met a fake seller although Alibaba granted him its golden status. (Alibaba just fired one of their executives for not taking the due diligence).

In November 15, 2008 the FBI, ICC, CIA, Federal Reserve, the European Central Bank, and Interpol had a meeting in which they point out


that there are so many false offers in the digital world. The ICC published a letter trying to scare parties saying that who sends a false Non Circumvention non Disclosure Agreement (NCNDA), International Master Fee Paymaster Agreement (IMFA), Letter of Intend (LOI), Ready, Willing and Able letters (RWA), Bank Comfort Letter (BCL) or sends false Proof of Product (POP), or false Proof of Funds (POF) will be charged with a crime. However goes without saying than a letter is not enough to typify as a crime a specific conduct.. Since Nullum crimen, nulla poena sine previa lege poenali (No crime, no punishment without a previous penal law” –national law-, not a letter from ICC, FBI, CIA, INTERPOL, or European Central Bank. An usage never will be a way in which a crime may be typified. It would be also against due process, and the international conventions on human rights.

The International Chamber of Commerce has built a network of lawyers to act in cases of fraud (NETFraud) but up to now, nothing can stop the amount of fake offers, buyers in the B2B world. So much time, and money is lost due to the lack of security in dealing in the B2B world. Pursue a CISG case against a Chinese seller may be very difficult, in most of the cases seller disappear, or the cost of CIETAC arbitration would be so high considering the amount in dispute. This trillion of dollars lost every year, has on another hand Alibaba earning 17 billions in less than 5 years. Tencent and the use of social media will trigger exponentially the international sale of goods. Every single individual will be a potential trader of sale of goods. Therefore CISG is of outmost importance, and its best times are to come.

The legal framework is not the only aspect to take into consideration: Empirical evidence on the marketing factors shows that there are other major aspects to take into consideration: high-consistent product quality, price, company reputation, after sale service support, terms of delivery, matching customer specifications, negotiations skills, export market research, consistent development of New Products, discounts to distributors/agents, promotion directed to middle men, warranties, invitation to trade shows, export government initiatives among others.
CISG as the leading uniform treaty which govern contracts for the international sale of goods is an outstanding instrument that contribute to the removal of legal barriers in international trade and promote the development of international trade. However from our point of view, and due to the fact that the usages may not be reasonable, its advisable to assess the risk of volatility and change of circumstances, not only bringing to a new equilibrium the contract, but drafting clear and enforceable contracts in time, excluding the use of any usage that may affect the contract equilibrium.

Last but not least, UNCITRAL has done an outstanding job with the uniform law for international sale of goods. However the two extremes: the transactions too small and too big crave for a suitable solution.

UNCITRAL should pay attention not only to arbitral awards and courts decisions (which are greatly appreciated), but also gather information from companies, chambers of commerce, professional and trade associations worldwide in order to be more familiar with the problems that international trade is facing. This is particularly important in international sale of goods, due to the fact that because of the amount in controversy in many cases is not high, the controversies are not reaching national courts or international commercial arbitration tribunals. Also UNCITRAL is invited to form an interdisciplinary group of experts in both physical and financial commodities trading to work in a proposal of international rules for clearing houses due to the fact that major investment banks are doing physical commodities trading and their clients, major multinational corporations, have the power to control indexes and impose usages at their will.
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