Legal Remedies in Breach of Contract by the Seller under CISG

o. Univ.-Prof. Dr. Rudolf Welser / Hon.-Prof Dr. Irene Welser[*]

I. Introduction

The **United Nations Convention** on Contracts for the **International Sale** of **Goods**, the CISG, has now been in effect for more than 25 years. It has been ratified by over 60 member states, including most European States, the United States of America, Russia and China. At the moment, it is at the Turkish Grand National Assembly for ratification. As a consequence of its wide applicability, the CISG has great influence on the reformation of the various national sales laws, especially in Europe and will be of great importance also for Turkey in the very near future. The Convention has originally – in 1980 – been concluded on a conference in Vienna, so two Viennese experts have been invited to give a short overview of legal remedies that the buyer may invoke, if the seller breaches the contract.

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[*] *Prof. Dr. Rudolf Welser* is University professor and Head of the Institute of Civil Law at the University of Vienna, Austria. He is author of more than 200 publications, amongst these the standard book on Austrian Civil Law, the *Koziol/Welser*. Contact address: rudolf.welser@univie.ac.at; www.univie.ac.at/zivilrecht

Dr. Irene Welser is honorary professor at the University of Vienna and partner at the Viennese law firm Cerha Hempel Spiegelfeld Hlawati, where she heads the contentious business department. Contact address: irene.welser@chsh.at; www.chsh.at

Both Rudolf Welser and Irene Welser have specialized in questions of CISG and often act as arbitrators in international sales disputes. This article is the extended version of a speech held by Prof. Dr. Rudolf Welser on November 10, 2006 at The Istanbul Chamber of Commerce.

II. Which Obligations and Responsibilities does the seller have?

1. General Provisions

To state whether there is a Breach of Contract caused by the seller, the first question to be answered is: Which duties does the seller, according to the Convention, actually have? Do these duties correspond with our "national" understanding of Breach of Contract? Art 30 of the Agreement reads:

"The seller must deliver the goods, hand over any documents relating to them and transfer the property in the goods, as required by the contract and this Convention".

The UN Sales Convention also contains determinations about the particular place of performance or delivery, about the time of performance and quite a few provisions about **conformity** of the performance. These do not in detail correspond with national Turkish or Austrian Law, therefore a closer look should be taken at them first.

2. Place and Time of Performance

a) Place of Delivery (Art 31)

The place of delivery is primarily determined by the **terms of the contract itself**. Often, international sales contracts refer to clauses such as Incoterms like "FOB" ("free on board"), "DES" ("delivered ex ship") or "DAF" ("delivered at frontier"). In this case, the delivery obligation and its fulfilment is fairly clear.

If the **contract does not contain any provision** where to deliver the goods, it has – as "step number one" - to be determined whether the contract is, nevertheless, to be considered as a "distance purchase agreement". This is the case, if, according to the other provisions of the contract, a transport of the goods from one place to another is necessary. The seller basically fulfils such a delivery obligation by **handing the goods**

over to the first carrier for transmission to the buyer, for example, to a qualified freight carrier or other handling agent.

In all other cases, the seller only has to make the goods available at the place where the goods **were stocked** at by the time of conclusion of the contract or were to be manufactured or completed at. It is sufficient to place the goods at the buyer's disposal there; there is no need to send or ship them.

If no such place exists or was taken into account by the parties, the place of delivery simply is the **place of business** of the **seller**. Again, the buyer needs to come and collect them.

If the seller does not deliver his goods at the right or correct place (or hold them at the buyer's disposal there), he breaches the contract, and the buyer can **reject** the goods. If, by such malperformance, the delivery date is exceeded – which is normally the case – the buyer has all remedies resulting out of breach of contract. However, the buyer may also accept the goods delivered to the wrong place. He is then, however, entitled to claim the occurred extra costs as damages.

b) Delivery Date (Art 33)

Of course, also the date of delivery is primarily determined by the content of the contract. If the contract states explicitly, or by means of interpretation, a period of time within which the seller can deliver, he is entitled to deliver **at any time within this period**, unless circumstances indicate that the buyer has the right to specify or choose a certain date.

In any other case, the goods have to be delivered "within a reasonable period of time after the conclusion of the contract". This provision is rather vague and may open room for discussion as to what is reasonable. It is clear that the interests of both parties need to be taken into account. The seller's interests are not of primary importance. Usually,

average production and delivery periods serve as a good yardstick to determine reasonableness of time.

The failure of timely delivery is – regardless of the seller's default – again a breach of contract, which entitles the buyer to remedies.

c) Documents (Art 34)

International sales contracts often include a duty of the seller to provide specific documents. If the seller is bound to hand over such documents relating to the goods, according to Art 34, he must hand them over at the time and place and in the form required by the contract. This fact is little surprising. Any documents that may have been handed out earlier, but have not been found sufficient by the buyer, may be adapted until the time of due delivery. The violation of the duty of transfer of sufficient documents is sanctioned in the same way as the delivery of non-conforming goods, which may seem rather strict. It is, however, a consequence of the fact that the Uniform Sales Law has, basically, the same legal remedies for all "breach of contract" cases. This fact will be reverted to later.

3. Conformity of the goods – no quality deficiencies

a) Criteria

The main obligation of the seller is to **deliver goods conforming** to the **contract**. Therefore, the seller must deliver goods which are of the quantity, quality and description required by the contract and which are contained or packaged in the manner required by the contract (Art 35 para 1). It is therefore up to the parties to define exactly what they want. Normally, international sales contracts contain clear provisions about the description of the goods and their quality.

If they have not stipulated anything, according to Art 35 para 2, the goods are to be regarded in conformity with the contract:

- if they are fit for "**ordinary use**";
- if they are fit for any **particular purpose** expressly or impliedly made known to the seller at the time of the conclusion of the contract;
- if they correspond to the **sample** or model that has been held out as standard for the contract;
- if they are **adequately packed** to protect them.

This basic definition of quality is very similar to the one that may be taken form a national law understanding. The same is true for a limitation of liability if the defect was known to the buyer:

b) Exclusion of liability in case of knowledge or potential awareness of the buyer (Art 35 para 3)

According to Art 35 para 3, the seller is not liable for any deficiency of the goods at the time of the conclusion of the contract that the buyer **actually knew** or could **not** have been **unaware** of. This provision covers any defectiveness that an average buyer finds out in the course of a regular inspection of the goods before the purchase. However, the buyer has no obligation of such inspection before conclusion of the contract.

c) The relevant time for assessing conformity of the goods (Art 36 para 1)

The seller is liable in accordance with the contract and the Convention for any lack of conformity which exists at the time when the **risk passes to the buyer**, that is, normally, the delivery point. It is basically irrelevant whether the deficiency was apparent at that time or could only be discovered later. Therefore, the seller is also liable for hidden or secret defects. He is, on the contrary, of course not liable for normal "wear and tear" defects unless he has guaranteed that for a period of time, the goods will

remain fit or will retain specified qualities or characteristics. Furthermore, the seller is not liable for defects that result from mishandling by the buyer.

d) Duty to examine and give notice (Art 38 to 40)

Like many national trade law provisions, the CISG contains an obligation for the buyer to check the conformity of the goods quickly and to promptly complain to the seller in case of deficiencies: The buyer must, according to Art 38, **examine** the goods within as **short a period** as is practicable in the circumstances. The period for such inspection is therefore not in any case "appropriate", but short. All undue delay must be avoided.

The provisions on the duty to examine and to give notice of non-conformity apply to all kinds of defects in quality and quantity. They also apply if goods altogether different from the order are delivered, a so-called "aliud".

In order to make a proper complaint, the buyer has to be aware of the fact that there are three different periods: There is one examination period, and after that, two notice periods: a relative and an absolute one.

First, it has to be recalled that the buyer has to examine the goods delivered in "as short a period as is practicable in the circumstances". This has already been pointed out. After such an examination has been made, a new period is running: the period for giving notice of the defects to the seller. Pursuant to Art 39 para 1, the buyer **loses the right** to rely on a lack of conformity of the goods if he does not give notice to the seller specifying the nature of the lack of conformity "within a **reasonable time** after he has discovered it or ought to have discovered it". In this respect, the Convention is not as strict as before: After a "short" period to examine, the complaint must only be made within "reasonable" time. According to various court rulings, normally, a **period of 14 days** is to be considered as "reasonable". It is interesting to remark that this provision has been a model for reforms of the trade law in Europe: For example, the new Austrian Business Law that came in force as of 1st January, 2007 changed the buyer's duty to

"promptly" complain about defects to a duty to complain "within reasonable time" according to the CISG.

In addition, there is an **absolute time-limit of two years** that starts with the actual handover of the goods to the buyer. It also covers hidden defects that are discovered later. In case a contractual guarantee period has been agreed upon, of course, this period applies.

But even an eventual failure of examination or notice does not hinder the buyer to bring in a claim for breach of contract, if the **seller himself** was **grossly negligent**. In that case, neither the relative nor the absolute period applies. Art 40 of the Convention reads:

"*The seller is not entitled to rely on the failure of examination or notice, if the lack of conformity relates to facts of which he knew or could not have been unaware and which he did not disclose to the buyer*".

And furthermore, there is still another chance for a buyer, who failed to complain about a deficiency: If he can prove that he has a "**reasonable excuse**" for his failure to give the required notice, he may – according to Art 44 – still reduce the price (in accordance with Art 50) or claim damages, except for loss of profit. Allowing this exception, CISG is quite tolerant in respect of busy buyers.

4. Absence of Third-Party Claims (Art 41 to 43)

The duty of the seller to deliver goods in contractual quality, free of defects or deficiencies, is, of course, not his only one. Naturally, the goods must also be free and clear from any security interests, liens, pledges or other encumbrances or third party rights and must not be subject to any transfer restrictions or pre-emption or similar acquisition rights. The freedom of such third party claims is regulated separately from the defects in quality in Art 41 to 43. The Convention distinguishes clearly between the – general – seller's liability for the "freedom from any right or claim of a third party" on

one hand and his liability for specific **industrial** or other **intellectual property infringements** on the other hand.

a) Freedom from any right or claim of a third party to the goods (Art 41)

Generally, the seller must deliver goods which are free from any right or claim of a third party, unless the buyer agreed to take the goods subject to that right or claim. "Any right or claim of a third party" is fairly extensive and comprises any and all claims which could negatively affect the buyer's use of the goods, regardless of their nature or their basis in private or public law. There is no exception for the seller's liability in respect of such general third-party claims.

b) Freedom of intellectual property rights (Art 42)

The seller's **liability** for **freedom from intellectual property** claims is somewhat more restrictive, taking into account that intellectual property laws may be different in various countries. Therefore, the seller only has to warrant freedom from third party claims based on industrial or other intellectual property, of which at the time of the conclusion of the contract the seller **knew** or **could not have been unaware**. As a further prerequisite, the right or claim must be based on industrial property or other intellectual property of either the state where the goods are to be resold or the state where the buyer has his ordinary place of business. Thus, **unforeseeable claims** based on intellectual property laws of other countries are excluded. Furthermore, the seller is not liable, if the buyer himself had or must have had knowledge of such an intellectual property claim, or if the intellectual property infringement results from the buyer's own drawings, designs or specifications that, according to the contract, the seller was obliged to use.

c) Duty to give notice (Art 43)

Again, both for general and for IP-based third party claims, there is a duty to give notice within a reasonable time after the seller has become aware or ought to have become

aware of the right or claim. Basically, the situation is very much the same that has been outlined before, concerning general deficiencies in quality.

III. Remedies of the Buyer for Breach of Contract by the Seller (Art 45 to 52)

1. General

Generally, most national laws clearly distinguish between the legal consequences in cases of different kinds of misperformance, such as default, deficiencies in quality or other breaches of contract. The legal consequences may be manifold: They reach from claims for specific performance, the right to withdraw or terminate the agreement, the right to challenge the agreement, the right of rescission, the right of avoidance, to claim damages and so on. Each of these legal remedies usually has a different prescription period.

The CISG has a totally different approach: The convention does not make a difference between the impossibility of performance, delay, subsequent impossibility by fault or by coincidence or positive violation of contractual duty, not even warranty or guarantee. **There is one uniform kind of malperformance only: the so-called "breach of contract"**. The legal ground for such breach of contract is totally irrelevant, and it is of no importance whether such breach concerns the primary or the secondary obligations. Consequently, in all of these cases, the buyer will basically have the same remedies. Still, for the legal consequences it is decisive, whether the breach of contract is **"fundamental"** or not.

According to Art 25, a breach of contract is fundamental, *"if it results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract, unless the party in breach did not foresee and a reasonable person of the same kind in the same circumstances would not have foreseen such a result."*

The concept of fundamental or, as we may also say, **material** breach of contract therefore takes into consideration two elements: One is the deviation from the contract as such, the other is foreseeability of its consequences for the seller, being a prudent and efficient businessman. For example, delay in a contract with **fixed time of delivery** has been considered as such a fundamental breach of contract.

The buyer's remedies for breach of contract are laid down in Art 45. He can basically require

- specific performance,
- avoidance of contract or
- price reduction and
- claim damages. The claim for damages can concur with other remedies.

If the seller is only partly in delay with his performance or if the delivery is only partially defective, the remedies of the buyer are limited to the missing part.

These remedies sanction all duties of the seller, thus primary and secondary obligations, defects in quality, late performance and third-party claims. Normally, all remedies can be alternatively exercised.

The Convention does not contain any prescription period for the exercise of the remedies in court, provided that notice has been timely given. The statute of limitation is governed by the national law that applies due to the conflict of laws provisions.

2. Specific Performance

It is now necessary to take a **closer look** at the **various remedies** in detail. We shall first revert to the claim for "specific performance", meaning that the buyer wishes the contract to stay fully in force and demands that the seller shall, finally, fulfil his obligations thereunder.

a) General (Art 46)

According to Art 46, "*the buyer may require performance by the Seller of his obligations unless he has resorted to a remedy which is inconsistent with this requirement*". Such **"inconsistent" legal remedies** are avoidance of the contract and price reduction. This is logical and goes without saying: In the first case, there is no more legal basis for performance, in the second case, the buyer decides to claim a different kind of compensation. Therefore, it is no longer possible to claim performance of the contract as such, as this would be contrary to each other and lead to the result that the buyer would be compensated for the same default twice and thereby be unduly enriched.

If the buyer decides to claim for performance of a contractual obligation, there is a certain implication of the national law: According to Art 28, a court is not bound to enter a judgement for specific performance **unless the court would do so under its own law** in respect of similar contracts of sale not covered by the Convention. Anglo-American jurisdictions tend to regard damage claims as primary remedy and only exceptionally permit claims for specific performance in cases where the buyer has a special interest, for example, if the goods are "unique" for him. The Convention wanted to take such a "local" approach into consideration, at least to a certain extent.

b) Repair and Delivery of Substitute Goods

Under the "specific performance" title, if the goods have already been delivered, the Convention provides for remedies that are **similar to warranty claims**. In case of a **defect in quality or quantity**, the buyer can require the seller to **repair** them, unless this is unreasonable having regard to all circumstances (Art 46 para 3). If the goods do not conform with the contract, the buyer may require delivery of **substitute goods** (Art 46 para 2). Such a demand requires, however, that the non-conformity is a fundamental breach of contract.

Let us recall: this means a "reasonably severe defect". If this is the case, the buyer is free to choose whether he prefers the delivered goods to be repaired or new substitute goods to be delivered. Both the demand to repair and the demand for delivery of substitute goods must be made **in conjunction with the notice of default** that has been mentioned earlier, or within a reasonable time thereafter.

If the breach of contract is not fundamental and if a repair is not possible or unreasonable, the buyer can only keep or retain the defective goods and claim for damages or price reduction.

c) Claim for Performance and Additional Period of Time (Art 47)

According to Art 47, the **buyer may fix an additional period of time** of reasonable length for performance of the seller's obligations. The buyer is, however, not obliged to do so, he can also demand performance without it. At first glance, fixing an additional period of time seems to be negative for the buyer, as he may not, during that period, resort to any other remedy. The seller may thus rely on this "last chance" given by the buyer.

It might now be asked, why should the buyer give such a last chance, if this has the negative effect that he is – for this period – bound by his declaration? The advantage of fixing an additional period of time turns out in case that the breach of contract is not fundamental: If the goods have not yet been delivered, the buyer – by fixing such additional period of time – gains the additional right to declare the contract avoided, **even** if the breach of contract is **not fundamental**. Without granting such a period, he would not have this right. Therefore, if the buyer cannot be sure that the breach of contract is fundamental, he should always consider fixing an **additional period of time** in cases of delay.

3. Avoidance of the contract (Art 49)

Let us now pass on to the most severe legal remedy of all, the so-called "avoidance of the contract". The CISG talks of avoidance of the contract when it means the total dissolution of a contract, that is its cancellation. Avoidance of the contract is, together with the right to claim damages, the main remedy of the buyer in case of breach of contract.

a) Prerequisites

The avoidance of the contract according to Art 49 includes **all cases that fall under the concept of resignation, withdrawal or rescission**. The Convention tends to restrict the right of avoidance of the contract to severe reasons in order to hinder the buyer to get rid of the contract too easily.

Art 49 para 1 provides for two cases only in which avoidance of contract can be declared:

- First, if the failure of the seller to perform his obligations under the contract or the Convention amounts to a **fundamental breach of contract**; or
- second, in case of **non-delivery**, if the seller does not deliver the goods within the additional period of time fixed by the buyer or declares that he will not deliver them within such a period.

In case of **fundamental breach of contract, no further prerequisites** have to be met. Not only defective performance, but also delay may as such be a fundamental breach of contract. Such a fundamental breach would for instance be affirmed, if the contract is a time purchase and therefore contains a fixed-date element. In this case, **avoidance of the contract can immediately be declared and, additionally, damages for non-performance can be claimed**. (As will be pointed out later, such damage claims

basically do not require any negligence or fault on the part of the seller, which comes as a surprise in comparison to many national laws.)

If the breach is not fundamental, there is a clear distinction between delay and other cases: In case of **non-delivery and delay**, there is the possibility to declare the contract avoided even if the breach is not fundamental, provided that an **additional period** of time has been fixed.

The situation is completely different, if we talk about deliveries that have not been delayed, but have simply been **effected in a defective** way. Here, only in case of a "fundamental" breach, the contract may be avoided. It is therefore completely irrelevant whether an additional period of time has been fixed or not: The demand for repair or for delivery of substitute goods even in conjunction with fixing an additional period of time cannot lead to avoidance of the contract, if the breach is not fundamental.

In this case, if the breach is not material, the seller basically only has the right of **price reduction** and **damages**, but has to keep the goods and pay the purchase price.

b) Exercise of legal remedies within reasonable time (Art 49 para 2)

In any case, the buyer must declare the contract avoided within reasonable time after he has or should have become **aware of the breach** of contract. If he fails to do so, he loses this right.

c) Effects of Avoidance

The effects of avoidance are regulated in Art 81 and the following of CISG. Avoidance of the contract releases both parties from their obligations, subject to any damages which may be due. If restitution of goods is necessary, the parties must do so **concurrently**. If the buyer is unable to effect such restitution because of his own acts or omissions, he loses the right to declare the contract avoided or to require substitute

goods. On the other hand, he does not lose these rights if the goods have deteriorated or **perished** as a result of the examination that was necessary in order to give proper notice of the defectiveness or if the goods have been **sold** in the normal course of business before discovering their defects.

If the buyer has, according to the aforesaid, lost his right to declare avoidance or to demand delivery of substitute goods, **he may still exercise the remaining remedies,** such as damage claims or a demand for reduction in price.

d) Form and content of declaring avoidance

There are **no formal requirements** for the declaration of avoidance. It may therefore also be declared orally unless the contract contains a specific provision that any declarations must be made in writing only. The wording is not essential, the buyer must only make it clear that he is **no longer willing** to perform his own contractual duties because of the seller's breach of contract. It is, however, important to remember that some kind of declaration is necessary. In any case, the contract does not dissolve by itself.

4. Reduction in Price (Art 50)

If the goods do not conform with the contract and whether or not the price has already been paid, the buyer may **reduce the price** in the **proportion** of the actual value of the goods at the time of delivery compared to the value of conforming goods.

A reduction in price is not permitted for every breach of contract, but **only** if the contract is fulfilled and the goods **do not conform** to the contract because of defects in **quality** or **quantity**. There is no claim for reduction in price for delayed deliveries. It is doubtful whether the reduction in price is available in cases of third-party claims.

5. Right of retention

If it becomes obvious even before the date of delivery, that one party will commit a fundamental breach of contract, the other party can avoid the contract. If the time permits – that means if there are no contrary obligatory interests of the other party – and it is reasonable according to the circumstances, the party that wants to avoid the contract has to give notice to the other party to give him a last possibility to fulfil his duties. The notice is not necessary, if the other party explicitly declares that he will not perform his duties.

According to Art 71, a party may suspend the performance of his obligations if, after the conclusion of the contract, it becomes apparent that the other party **will not perform** a substantial part of his obligations as a result of:

- a serious deficiency in his ability of perform or in his creditworthiness; or
- his conduct in preparing to perform or in performing the contract.

In practice, the deficiency in the other party's creditworthiness will be of primary importance. It must however be noted that suspension of performance is only permitted if, resulting from this, a breach of contract is apparent. It must therefore be clear that the other party will not perform a substantial part of the contract.

6. The Seller's Right to Cure (Art 48)

Art 48 of the Convention gives the seller the right to remedy any failure to perform his obligations, even after delivery. This right is called "right to Cure" or **"Second Tendering"**. It restricts the possibilities of the buyer, because, of course, as long as the seller has the right to cure, the buyer cannot exercise any rights that would otherwise arise out of the breach of contract, but are contradictory to such an approach.

According to Art 48 para 2, the seller can ask the buyer to accept performance within a certain period of time. Even if the buyer does not reply to this request within a

reasonable time, he may not resort to a remedy inconsistent with performance by the seller before the period of time runs out.

The right to cure is therefore subject to the buyer's approval. If he does not allow for such a remedy, and the breach is fundamental, the buyer may declare the contract avoided. In this case, the seller is not allowed to go for second tendering.

If the buyer agrees, remedy must be made, according to Art 48, at seller's "own expense", "without unreasonable delay and without causing the buyer unreasonable inconvenience or uncertainty of reimbursement of expenses advanced".

Furthermore, the buyer retains his right to claim damages even though such remedy has been made.

This leads us to the last point, which is nevertheless of high importance:

IV. Liability for Damages (Art 74 to 77)

1. General

According to the Convention, the liability for damages arising out of a breach of contract is – unlike in many national laws - **not based on default**, but more similar to a liability based on **guarantee.** There are, however, certain differences from a really "strict liability". A party is not liable if he proves that the failure was due to an impediment "beyond his control", which he could not reasonably have avoided. In any case, a party may not relay on a failure of the other party to the extent that he, himself, caused it.

Damages are always **monetary** compensation and always include loss of profit. There is, however, buyer's duty to mitigate his losses. Damages for personal injuries are

excluded from the Convention and have to be determined by the applicable national law.

As far as the claim for damages is based on defect in quality or quantity of the goods or based on third-party claims, giving notice is obligatory. As has been pointed out before, also in terms of damages, the Convention does not distinguish between the different kinds of breach of contract and therefore **every** possible **kind** of breach is covered.

Let us recall that damages can be claimed in addition to any other remedy.

2. Foreseeability of damage (Art 74)

According to Art 74 sentence 2, it is necessary that such damages have at least been foreseeable to the responsible party as a possible consequence of the breach of contract. Therefore, damages that a diligent seller could not have taken into account when entering into the agreement are excluded from recovery.

3. Calculation of damages (Art 75 and 76)

There are two different ways to effect calculation of damages, the claim for actual losses and the abstract calculation.

Actual losses are calculated by elaborating the difference between the contract price and the price in the substitute transaction; further damages, for example for extra transportation costs, can be claimed in addition.

An **abstract calculation** is possible, if the buyer has not made a substitute transaction and the goods in question have a market price. The amount of damages is then calculated as difference between the price fixed by the contract and the current price at the time of avoidance. Also in this case, any further damages may be recovered.

V. Summary

So - in brief - the most important features of the CISG in case of breach of contract by the seller may be summed up as follows:

At his choice, the buyer has the legal remedies of

- **specific performance**,
- the **demand for repair** and the **delivery of substitute goods**,
- **reduction in price** and
- if the breach of contract is fundamental **or** if the buyer has set an additional period of time for performance, the **avoidance** of the contract.
- In addition to that, the buyer can claim **damages**.

On the other hand, the seller has the **right to cure** his failure to perform his obligations and the buyer has the duty to **mitigate damages**.

As these principles are widely applied, they will hopefully also be accepted in practice as soon as the UN Convention on the International Sale of Goods has been ratified in Turkey.