

DRAFTING CONTRACTS UNDER THE CISG

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Dealing with Avoidance and Its Consequences: Articles 49(2), 64(2), and 81 Through 88

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I. Introduction

This chapter will discuss the Digest's usefulness as a tool for drafting clauses concerning the avoidance of an international sales contract and its consequences. These matters are addressed in Articles 49(2), 64(2), and Articles 81 to 88 of the United Nations' Convention on Contracts for the International Sale of Goods ("Sales Convention" or "CISG"). Admittedly, when the author was first asked to write this paper and propose clauses that would deal with the issue of avoidance and its consequences, he looked for some guidance and reviewed some of the standard forms that passed by his desk that are somewhat common in the U.S.-Mexico border region, but did not find much to serve as a starting point. He had also never considered including clauses to deal with such specific issues, and have some reservations whether he would actually use them. However, one must seize the opportunity to speculate and imagine, and what better starting point than the CISG Digest?

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A. The UNCITRAL Digest and Drafting in Civil Law and Common Law Legal Practice

The CISG Digest is an effort by the United Nations Commission on International Trade Law (UNCITRAL) to promote the uniform interpretation of the Sales Convention according to the mandate included in Article 7(1),¹ by using the combined wisdom of arbitrators and judges.² The Digest was drafted using a simple but effective template: First, it includes the article that is being discussed, followed by a brief explanation of what the purpose of the provision is, and a brief discussion of the cases dealing with the specific provision that have been rendered based on that provision. It was decided early on that the Digest to the Sales Convention would not be critical of any decision.³ In the author's view, whether or not the Digest is critical is not relevant when approaching the Digest as a drafting tool since, in this case, it is not being used as the basis for a court or arbitral decision, but rather to better understand the scope of each particular provision, and to consider the case law that has so far emerged, as a means to predict things that could happen, and how smart contract drafting can assist in neutralizing potential risks.

If one compares the approach to contract drafting followed by civil law lawyers in Mexico, with the craft as practiced by their U.S. counterparts, we find interesting differences. Contracts drafted by lawyers in common law countries tend to be highly elaborate and complex documents—and thus substantially longer—as compared to contracts drafted by their civil law counterparts. To a Mexican lawyer, a contract drafted by his U.S. colleague will look like the drafter went through a frenzied attempt to envision every possible scenario that might occur. These diverging approaches to contract drafting are better understood if one

¹ CISG art. 7(1): “In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.”

² See Jernej Sekolec, *Digest of case law on the UN Sales Convention: The Combined wisdom of judges and arbitrators promoting uniform interpretation of the Convention*, in *THE DRAFT UNCITRAL DIGEST AND BEYOND: CASES, ANALYSIS AND UNRESOLVED ISSUES IN THE U.N. SALES CONVENTION 1* (Franco Ferrari, Harry Flechtner & Ronald Brand eds., 2004).

³ “A noteworthy feature of the discussion by delegates in the Commission session was the admonition that the Digest should avoid criticism of the decisions of national courts.” Jernej Sekolec, *Digest of case law on the UN Sales Convention: The Combined wisdom of judges and arbitrators promoting uniform interpretation of the Convention*, in *THE DRAFT UNCITRAL DIGEST AND BEYOND: CASES, ANALYSIS AND UNRESOLVED ISSUES IN THE U.N. SALES CONVENTION 1*, 14 (Franco Ferrari, Harry Flechtner & Ronald Brand eds., 2004).

considers the differences between the civil and common law attitudes towards statutes, and the role judges and juries may play in interpreting contracts.⁴

Provisions in a common law statute are typically drafted very specifically, and meant to be interpreted narrowly. They exclusively cover the matters contemplated within their text; thus, absent a specific legal rule, the judge will rely on the common law to fill the lacunae, and application of a statute by analogy will seldom occur. In addition, common law judges enjoy some authority to provide missing terms in contracts by including “reasonable” terms.⁵ Thus, the common law lawyers’ attempt to make a contract as complete as possible is also an attempt to avoid having the judge supply a missing term.⁶

In the Civil Law system, codes are drafted broadly, and if there is an issue for which the civil code provides no specific rule, a civil law judge may apply a provision by analogy. However, a civil law judge has limited or no authority to fashion a rule, because he is deemed to have been charged with a duty to apply the law as enacted by the legislative body, not with authority to write it. Concerning contractual intent, gaps left by the parties are supplied by the civil code, and, contrary to what occurs in the common law, civil law judges may not replace missing terms with reasonable ones.

B. The CISG Digest as a Contract Drafting Tool

As mentioned before, the template followed by the drafters of the CISG Digest, (CISG Article, explanation, and case law), reduces the costs involved in locating information that would otherwise be dispersed, thus saving time and money. The Digest can serve as a “crystal ball” of sorts, allowing the drafter to consider issues that have been argued before courts and tribunals throughout the world. Some of

⁴ See B. Blair Crawford, *Drafting Considerations under the 1980 United Nations Convention on Contracts for the International Sale of Goods*, 8 J.L. & COM. 187 (1998), also available at <http://www.cisg.law.pace.edu/cisg/biblio/crawford.html>.

⁵ See RESTATEMENT (SECOND) CONTRACTS § 204 (1973):
Supplying an Omitted Essential Term.

When the parties to a bargain sufficiently defined to be a contract have not agreed with respect to a term which is essential to a determination of their rights and duties, a term which is reasonable in the circumstances is supplied by the court.

⁶ An additional incentive to writing long contracts may also come from a concern that the attorney could be subject to some sort of disciplinary action, or even a malpractice suit.

the difficulties encountered in international transactions may not be as evident to the contract drafter whose prior experience has been limited to the domestic level.

This is not to say that the CISG Digest should be the only tool. There are many treatises and publications (in paper and on-line) that provide valuable information that is also critical of the cases that have been rendered so far on the Sales Convention, something the CISG Digest intentionally does not do. In the chapter that follows, the author attempts to sum up the reasons for using the Digest as a contract drafting tool.

1. Using the Digest to Restate a Rule Contemplated in the CISG

One reason to use the Digest as a contract drafting tool could be to restate a rule that is already part of the CISG, but that may not be obvious to the parties involved in the contract. For example, under Mexican and Argentine Law, absent an agreement between the parties on the date of payment, a buyer is not required to pay until a formal demand has been made.⁷ The CISG provides that, absent an agreement of the parties, the buyer is to pay for the goods when the seller places either the goods or the documents at buyer's disposition,⁸ and such payment must be made without the need for any request or compliance with any formality on the part of the seller.⁹ Including a specific provision modeled on the Sales Convention's text would serve the purpose of advising a party of the consequence of certain conduct, when those consequences may not be obvious because they represents a deviation from the municipal law rule.

⁷ Article 2080 of the Mexican Federal Civil Code provides that “[i]f the moment at which payment is to be made has not been fixed . . . the creditor may not demand it but only after thirty days following a formal demand, be it judicial or extrajudicial, before a notary or before two witnesses.” Article 509 of the Argentine Civil Code provides that, for obligations subject to a term, a person becomes delinquent at the expiration of any such term, but in cases where no term was expressly stated, the creditor must make a formal demand for payment before the debtor will be deemed delinquent.

⁸ CISG art. 58.

⁹ CISG art. 59.

2. *Using the Digest to Deviate from a Rule Contemplated in the CISG*

On the other hand, parties may be looking to exclude the CISG, or derogate from or vary the effect of any of its provisions.¹⁰ For example, they may want to include a clause to limit the amount of damages that are recoverable under Article 74 of the Sales Convention, or to derogate from the many “reasonable time” provisions that are included in the CISG’s text and instead include fixed periods of time—such as that found in Article 39 requiring the buyer to give notice of the lack of conformity within a “reasonable time” after he has discovered it or ought to have discovered it. After looking at the case law that has developed on a certain issue, a contract drafter may conclude that his client’s interests would be better served by deviating from the rule as expressed in the CISG and as restated in the Digest.

3. *Using the Digest to Add Certainty on Issues Where There is Divergent Case Law*

The decisions cited in the Digest reflect the interpretive trend: what the current state of CISG case law is. There are, however, some issues that have resulted in diverging opinions, such as on the issue of attorney fees, where some decisions deemed these a part of the general damages that may be awarded under Article 74, while some have considered the awarding of attorney fees a matter to be left to the municipal procedural law.¹¹ In situations such as this, a contract drafter may opt to include a proviso either explicitly excluding legal fees in a clause (“damages do not include attorney fees” or “parties shall not be entitled to attorney fees”). In the alternative, a contract drafter may feel comfortable with contemplating an award for damages, and may wish to include a provision stating that attorney fees may be awarded (“the prevailing party will be entitled to damages, including loss of profit, and including attorney fees”).

¹⁰ The right to derogate from or exclude a CISG rule is fully acknowledged in Article 6, which is a restatement of the principle of party autonomy.

¹¹ See, e.g., Harry M. Flechtner, *Recovering Attorney Fees as Damages Under the U.N. Sales Convention (CISG): The Role of Case Law in the New International Commercial Practice, With Comments on Zapata Hermanos v. Hearthside Baking*, 22 Nw. J. INT’L L. & Bus. 121 (2002).

II. Dealing with Avoidance and Its Consequences

The author now turns to a discussion of the CISG Digest and the cases cited on the issues of the time to effect avoidance (Articles 49(2), and 64(2)); on the consequence of avoiding the contract (Article 81); on the buyer's loss of the right to declare the contract avoided (Articles 82 and 83); on the right to pay interest on sums returned in the case of restitution, and to account for benefit conferred by goods (Article 84); and on the issue of preservation of the goods (Articles 85 through 88).

A. The Period of Time for Making a Declaration of Avoidance

CISG Articles 49(2) and 64(2) limit the rights of the buyer and seller to avoid the contract, if they do not do so within a reasonable time. The reasoning behind the time limit is that too much time may allow abuse by the party considering avoidance: they may speculate on the price in a volatile market or cause unnecessary expense.

1. *Avoidance by the Buyer When the Goods Have Been Delivered (Article 49(2))*

Article 49(2) governs the period during which the buyer may send a notice of avoidance to the seller. The Digest's commentary to Article 49(2) basically restates the principal idea of this provision, but does not fully explain the reasons for having a time limit on the buyer's right to avoid the contract after the goods have arrived.¹² A clearer explanation of the policy underlying this provision would be helpful for contract drafters that have limited exposure to the CISG.¹³

The Digest's explanatory discussion of Article 49(2) distinguishes between late delivery and other kinds of breaches of contract. The Digest also states in its comment to 49(2)(a) that in case of late delivery the period for the buyer to declare avoidance begins to run when the buyer *has become aware* of delivery. It is submitted

¹² See UNCITRAL Digest, art. 49, ¶ 16.

¹³ It has been asserted that the purpose underlying Article 49(2) is to avoid causing the seller unnecessary costs, exposure to risk, or even losses due to a fall in the market price of the goods. Moreover, a delay in the buyer's notice of avoidance will delay the seller's opportunity to resell the goods, thus increasing the seller's expense and risk. JOHN O. HONNOLD, *UNIFORM LAW FOR INTERNATIONAL SALES* 330, ¶ 306 (3d ed. 1999).

that this part of the provision could lend itself to abuse by a buyer, who could easily claim that he became aware of the late delivery at a date other than when he actually became aware of it, though no case law has yet discussed this particular issue. Uncertainty, and maybe even abuse, may be limited by forcing the buyer to provide notice of avoidance within a fixed number of days after late delivery has been made, regardless of buyer's awareness.

In case of other kinds of breaches, the Digest restates that the period of time for declaring the contract avoided runs from when the buyer became aware of the breach or ought to have been aware of it, or after the expiration of an extension fixed in a Nachfrist notice under Article 47(1), or after the lapsing of a period of time under Article 48(2).

Clearly, the big question involving Article 49(2) is: what is a reasonable amount of time for the buyer to send the seller a notice of avoidance? The cases cited in the Digest vary greatly as to what courts have determined to be reasonable.¹⁴ A case from the German Bundesgerichtshof found that giving notice five months after being informed of the breach was unreasonable and ordered the buyer to pay the price for the goods,¹⁵ while a case that went to the Oberlandesgerichtshof Koblenz determined that notice given eight weeks after knowledge of breach was unreasonable.¹⁶

In a case involving goods that required repair by the seller, the Oberlandesgericht Oldenburg decided that five weeks was deemed to be a reasonable amount of time in which to provide a notice of avoidance.¹⁷ The seller had argued that according to its general terms and conditions of trade, the defendant was obliged to provide the notice of avoidance within five days. However, the Court made a distinction between the periods that run from the moment the goods have been received, and from the moment after the goods have been received but after their repair by the seller (which would seem to imply that a new period may begin to run after a seller has attempted to repair defective goods).

¹⁴ See UNCITRAL Digest, art. 49, ¶ 16.

¹⁵ Bundesgerichtshof, Germany, 15 February 1995, CLOUT case No. 124, English translation available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/950215g1.html>.

¹⁶ Oberlandesgericht Koblenz, Germany, 31 January 1997, CLOUT case No. 282, available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/970131g1.html>.

¹⁷ Oberlandesgericht Oldenburg, Germany, 1 February 1995, CLOUT case No. 165, available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/950201g1.html>.

The author submits that a shorter period for buyer to provide a notice of avoidance may be warranted in cases where goods have been repaired by the seller, since in such an event the buyer has been made aware of specific defects and he may more easily ascertain whether or not the repair has been effective. In a French case, it was found that notice of avoidance after various extensions had been granted was proper.¹⁸ Finally, a declaration three weeks after notice of lack of conformity was considered timely.¹⁹

2. *The Period of Time for the Seller's Declaration of Avoidance After the Price Has Been Paid (Article 64(2))*

In a manner somewhat mirroring Article 49(2) (buyer's period of time to declare avoidance of delivered goods), Article 64(2) discusses the requirements for the seller to declare avoidance after the price has been paid.²⁰ The Digest explains that when the buyer has paid the price, the seller will lose the right to declare the contract avoided unless he does so *before* he has become aware of performance having been rendered by the buyer.²¹ It is also unclear just what purpose is served by allowing the seller to avoid provided he does so *before* he becomes aware of performance. Because there are no cases cited in the Digest on Article 64(2), a person attempting to rely on the Digest to grasp a better understanding of the CISG, or to use it as a contract drafting tool may find little guidance in the form of examples.²²

¹⁸ Cour d'appel, Versailles, France, 29 January 1998, CLOUT case No. 225, available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/980129f1.html>.

¹⁹ Oberlandesgericht Hamburg, Germany, 26 November 1999, CLOUT case No. 348, available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/991126g1.html>.

²⁰ CISG art. 64(2):

(2) However, in cases where the buyer has paid the price, the seller loses the right to declare the contract avoided unless he does so:

(a) in respect of late performance by the buyer, before the seller has become aware that performance has been rendered; or

(b) in respect of any breach other than late performance by the buyer, within a reasonable time:

(i) after the seller knew or ought to have know of the breach; or

(ii) after the expiration of any additional period of time fixed by the seller in accordance with paragraph (1) of article 63, or after the buyer has declared that he will not perform his obligations within such additional period.

²¹ UNCITRAL Digest, art. 64(2), ¶ 9.

²² Examples of situations that may allow a seller to avoid the contract after the price has been paid include buyer's failure to obtain an import license, or a failure to comply with obligations to establish a distributorship of the goods, or to develop a program for promoting the sale of the goods. JOHN O. HONNOLD, UNIFORM LAW FOR INTERNATIONAL SALES 388–89, ¶ 356 (3d ed. 1999).

The Digest explains that the right to avoid is lost after the expiration of a reasonable period of time starting from the moment when the seller knew or ought to have known of the breach (Article 64(2)(b)(i)), or when a Nachfrist notice has been granted pursuant to Articles 64(2)(b)(ii) and 63(1).²³ This part of the Digest cites no cases on the issue of contract avoidance after the price has been paid.

3. *A Clause Proposed to Deal with Avoidance After Performance Has Been Rendered*

After considering the Digest's discussion on Articles 49(2) and 64(2), the following clause is suggested (it should be included as part of a general clause dealing with the time to effect avoidance):

Time to Effect Avoidance After Performance has Been Rendered.

After performance has been rendered, the party claiming a breach of contract by the other party may avoid the contract, provided that such notice of avoidance is sent within a period of (x) days following the moment from which the circumstance claimed to be a breach of this contract was discovered or ought to have been discovered. In cases where the seller has repaired the goods, the buyer will have a period of (x-y)²⁴ days following repair to send a notice to the seller.

(OPTIONAL):

A non-breaching party may (by notice given in writing) grant at its sole discretion an additional period of time to the breaching party so that it may perform its delinquent obligations within a period of (x) days after notice has been received. A response by the breaching party that it will not perform, or a failure to perform within such a period shall constitute acknowledgment by the breaching party of receipt of notice of avoidance of this contract.

²³ UNCITRAL Digest, art. 64, ¶ 9.

²⁴ It is suggested that this period be shorter, since the buyer shall know what the problem area was, allowing easier identification of the defect.

B. The Effects of Avoidance and Preservation of the Goods

Generally, CISG Article 81 refers to the consequences that stem from a party avoiding the contract, such as releasing the parties from future performance of their pending obligations, while preserving the provision concerning the settlement of disputes. It also addresses the issue of restitution of whatever the parties have exchanged under the contract.

1. Unilateral Avoidance

The Digest notes cases interpreting Article 81(1) to apply only when avoidance is made unilaterally, and not when there has been consensual avoidance. If the contract is terminated by agreement, the rights and obligations of the parties are then to be determined by the parties' agreement.²⁵ Pursuant to Article 81, avoidance releases both parties from their obligations under the CISG, subject to any damages which may be due. Furthermore, avoidance does not affect any provision concerning the settlement of disputes, nor any other right or obligation of the parties consequent upon avoidance of the contract.

a. Severability of Dispute Resolution Clauses

The Digest cites cases supporting the notion that an arbitration clause survives avoidance of the contract.²⁶ This is consistent with modern arbitration statutes, particularly those based on the UNCITRAL Model Law on International Commercial Arbitration.²⁷ The effectiveness of a choice of court clause has not yet been addressed in any of the cases cited by the Digest, but the same result should follow.²⁸

²⁵ UNCITRAL Digest, art. 81, ¶ 2. However, "consensual avoidance" seems to refer to cancellation of the contract, a matter that would fall within the scope of CISG Article 29.

²⁶ UNCITRAL Digest, art. 81, ¶ 4.

²⁷ Article 16(1) of the UNCITRAL Model Law on International Commercial Arbitration provides that: an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitral tribunal that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause.

²⁸ In the case of an arbitration clause, the matter is somewhat settled. The recent adoption of the Hague Convention on Choice of Court Agreements seems to point towards adoption of principles for choice of court clauses that are similar to those applicable under the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention). It is not clear, however, whether autonomy will be considered under the same two approaches that have been applied in the field of

b. Valid Avoidance of the Contract

The Digest recounts a number of cases that have determined that valid avoidance of the contract releases the parties from their pending obligations under the contract.²⁹ An invalid avoidance, be it because it is untimely, or because a party failed to follow a specific procedure, or because there were no substantive grounds for avoidance, will not release the party from performing its obligations.³⁰ Again, the parties have ample opportunity to draft a specific provision to better suit them, clarifying the period of time during which the parties must avoid the contract, and defining the matters to be deemed a fundamental breach of contract (as opposed to an unqualified breach that may entitle a party to damages but not to avoidance of the contract).³¹

2. Restitution Under Article 81(2)

While Article 81(1) sets forth the general rule that avoidance releases the parties from future performance, Article 81(2) provides a rule allowing a party who has performed his part of the bargain, in whole or in part, to claim restitution of whatever that party supplied or paid. The Digest describes certain issues that have arisen, such as: (a) where restitution is to be made; (b) What court has jurisdiction; and (c) who will bear the risk of loss; and (d) in what currency should the reimbursement of any amount paid be made.³²

a. Place to Effect Restitution

The Digest discusses cases that have arrived at different conclusions as to where restitution should be made.³³ Two cases cited in the Digest found that the matter

commercial arbitration. One perspective is that the arbitration clause survives the cancellation or annulment of the contract, while another perspective points to the autonomous interpretation of the clause, *i.e.*, that it is not necessarily governed by the same law that is applicable to the rest of the contract.

²⁹ UNCITRAL Digest, art. 81, ¶ 3.

³⁰ UNCITRAL Digest, art. 81, ¶ 3.

³¹ The CISG contemplates two types of breach: a fundamental breach, which may give rise to an avoidance of the contract; and an unqualified breach, which would allow the non-breaching party to claim damages if these were suffered.

³² UNCITRAL Digest, art 81, ¶¶ 5–6.

³³ UNCITRAL Digest, art. 81, ¶ 7.

fell outside the scope of the CISG, and should be addressed under local rules governing enforcement of a judgment.³⁴ Other cases cited in the Digest lead towards what I consider to be a better result. Using the gap filling rule provided in CISG Article 7(2), and via Article 31, a buyer complies with his duty to return the goods by placing them at the seller's disposal at the buyer's place of business.³⁵ In another case mentioned in the Digest, a German court arrived at a similar result and stated that there was a general principle that the place for performing restitutionary obligations should mirror the place for performing the primary obligations.³⁶

b. Determining the Court with Jurisdiction

The UNCITRAL Digest discusses the issue of place of performance of an obligation for a court to exert jurisdiction under the Brussels Convention's Article 5(1).³⁷ Uncertainty as to which court will have jurisdiction can be greatly reduced via the inclusion of an arbitration clause, or of a choice of court clause. There is, however, an issue that is not discussed in the Digest that could present some problems. Suppose parties to an international sales contract included a choice of court clause pointing towards a U.S. court and restitution is sought. Can a U.S. court order a U.S. seller to take over goods that it has sold to a buyer located abroad? CISG Article 29 states that a court is not bound to require performance of an obligation by the other party, unless the court would typically do so under its own law in respect to a similar contract of sale not governed by the Convention.³⁸ Is forcing a seller to take back goods that it has already sold a form of specific performance?³⁹ If so, a U.S. court could refrain from compelling a party to retrieve goods from a buyer after the contract has been avoided. Such an order to retrieve the goods could represent a high cost to both the seller and buyer, and could warrant a claim

³⁴ Cour d'appel, Paris, France, 14 January 1998, CLOUT case No. 312, English translation available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/980114f1.html>; Landgericht Landshut, Germany, 5 April 1995, English translation available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/950405g1.html>.

³⁵ Oberster Gerichtshof, Austria, 29 June 1999, English translation available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/990629a3.html>.

³⁶ Oberlandesgericht Hamm, Germany, 5 November 1997, CLOUT case No. 295, available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/971105g1.html>.

³⁷ UNCITRAL Digest, art. 81, ¶ 7.

³⁸ CISG art. 29.

³⁹ See Landgericht Krefeld, Germany, 24 November 1992, English abstract available in Unilex at <http://www.unilex.info/case.cfm?pid=1&do=case&id=81&step=Abstract>, cited in UNCITRAL Digest, art. 81, ¶ 6 n.29.

that the non-breaching party could have mitigated the loss by reselling the goods. It is obvious that the holder of the goods will always be in a better position to dispose of them if they are subject to rapid deterioration or if preserving them would entail unreasonable expense. A different scenario may arise when the goods are custom made and there is no willing purchaser for the goods. In this case, a court could compel the seller to take over the goods.

c. Risk of Loss

The Digest discusses two solutions arrived at by local courts under Article 81(2) to determine who bears the risk of loss when restitution must be made.⁴⁰ One such solution is the so called “mirror principle,” whereby restitutionary obligations are to mirror the primary contractual obligations. Thus, if a buyer received delivery of the goods when the manufacturer handed over the goods to the carrier (and transferred risk to the buyer), the buyer will thrust the risk back onto the seller when he hands over the goods to a carrier for their return.⁴¹

d. The Currency of Reimbursement

The Digest cites CLOUT Case 302 for the proposition that the refund of the price is due in the same currency in which the price had been duly paid, and at the exchange rate specified in the contract for payment of the price to the seller.⁴²

e. The Requirement That Restitution Be Concurrent

The issue of mutual restitution is discussed in the Digest, and the cases cited restate the principle that restitution is to be concurrent.⁴³ A clause could be included for informational purposes, to advise the parties that this will be the applicable rule.

⁴⁰ UNCITRAL Digest, art. 81, ¶ 7.

⁴¹ Oberster Gerichtshof, Austria, 29 June 1999, English translation *available at* <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/990629a3.html>.

⁴² International Chamber of Commerce case no. 7660, 1994, CLOUT case No. 302, *available at* <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/947660i1.html>.

⁴³ UNCITRAL Digest, art. 81, ¶ 8.

3. *The Right to Restitution Under Article 81(2) and Third Party Rights Under National Law*

The final part of Article 81 portion of the Digest deals with the issue of third party rights to the goods, in the form of a perfected security interest. The Digest describes the situation when a buyer falls into insolvency, and the seller's recovery of the goods will be more effective than attempting to collect payment.⁴⁴ One of the cases cited dealt with a seller who had retained title to the goods.⁴⁵ The seller sought restitution but a third party creditor had obtained and perfected a security interest in the goods. To avoid situations such as this, a seller would be wise to perfect a security interest in a manner consistent with the laws of the country where the goods will be located, in order to assure himself that he will have a priority in the goods. The parties may allocate the responsibility of who will perform the filing and who will bear the cost of perfection in the contract.

4. *A Clause to Govern the Issue of the Consequences of Avoidance*

Based on the Digest's discussion, the following clause to deal with the issue of the consequences of avoidance is suggested:

Effective avoidance of this contract will release the parties from performing any future obligations under it. Avoidance will be effective if the avoiding party has valid grounds to avoid the contract, and if the procedure set forth in clause "X" above is followed. Avoidance of this contract will not affect the (choice of court) (arbitration clause) mentioned in clause "Y" in this contract.

Upon effective avoidance, the parties will return to each other what has been supplied or paid under the contract. For purposes of complying with the duty to make restitution, each party shall pay the out of pocket expenses as may be required to perform this obligation, provided that such expense is not in excess of (specify amount), but a party giving an effective notice of avoidance will be entitled to recover its expenses,

⁴⁴ UNCITRAL Digest, art. 81, ¶ 9.

⁴⁵ U.S. District Court for the Northern District of Illinois, United States, 28 March 2002, CLOUT case No. 613 (*Usinor Industeel v. Leeco Steel Products, Inc.*, 209 F. Supp. 2d 880, N.D. Ill. (2002)).

without prejudice to the ability to claim additional damages under Articles 74 through 77 of the CISG. If the cost of returning the goods exceeds the amount mentioned in this clause, or if the goods are subject to rapid deterioration, the buyer may sell the goods pursuant to clause (X) in this contract.

If goods are to be returned, the seller shall bear the risk of loss of the goods. The currency for restitution shall be (contract currency), and payment shall be effected by (letter of credit) (wire transfer). No party shall be bound to effect restitution unless the other party is prepared to do so concurrently.

C. Articles 82 and 83: The Buyer's Loss of the Right to Declare the Contract Avoided or to Require the Seller to Deliver Substitute Goods, and the Buyer's Retention of Rights to Other Remedies

Pursuant to CISG Article 82(1), a buyer may lose the right to declare the contract avoided or to require the seller to deliver substitute goods if it is impossible for the buyer to make restitution of the goods substantially in the condition in which he received them.⁴⁶ One Digest case involved a buyer who lost the right to avoid a contract involving flowers because he had discarded some of the plants and resold others.⁴⁷ Similarly, a buyer of textiles lost the right to avoid the contract because he had resold them,⁴⁸ and a buyer of marble slabs lost the right to avoid the contract because he had cut and processed them.⁴⁹

The part of the Digest dealing with Article 82(2) deals with exceptions to the general rule that would otherwise cancel the buyer's right to declare the contract avoided. The discussion of Article 82(2)(a) provides that the buyer retains the right to avoid the contract even if the fact that it cannot make restitution of the goods substantially in the condition in which it received them is not due to its act

⁴⁶ CISG art. 82(1).

⁴⁷ Rechtbank Rotterdam, the Netherlands, 21 November 1996, English abstract available in Unilex at <http://www.unilex.info/case.cfm?pid=1&do=case&id=318&step=Abstract>.

⁴⁸ Oberlandesgericht Düsseldorf, Germany, 10 February 1994, CLOUT case No. 82, English translation available at <http://cisg3w.law.pace.edu/cases/940210g2.html>.

⁴⁹ Oberlandesgericht Koblenz, Germany, 27 September 1991, CLOUT case No. 316, English translation available at <http://cisg3w.law.pace.edu/cases/910927g1.html>.

or omission.⁵⁰ However, in the only case cited,⁵¹ the court based its decision the buyer was not responsible for loss or damage occurring to the goods being shipped back to seller after avoidance because the goods were in the hands of the carrier, and not the buyer—a matter that was addressed when discussing Article 81(2) *supra*.

Article 82(2)(b) preserves a buyer's right to avoid the contract or to demand substitute goods where the buyer's inability to make restitution of the goods substantially in the condition in which they were received is a result of buyer's examination under CISG Article 38.⁵² The cases cited in this part of the Digest are somewhat contradictory. In one case, the court held that a buyer of wire retained the right to avoid the contract even after he had processed it, because the buyer was unable to detect the defects until he had processed the goods.⁵³ In another case, involving marble slabs, the buyer lost his right to avoid the contract because he found out that they had been stuck together only processing the marble and not under during the examination allowed under Article 38.⁵⁴

It is not clear what role if any, CISG Article 40 could play under Article 82(2)(a). Pursuant to Article 40, the seller is not entitled to rely on the provisions of Articles 38 and 39 if the lack of conformity relates to facts that of which knew or could not have been unaware and which he did not disclose to the buyer. If this is so, why should we allow a seller who knowingly sells defective goods to benefit from a buyer's loss of the right to avoid the contract because the buyer only discovered the defect when he began processing the goods? Would this be consistent with the mandate to interpret the Sales Convention in a manner consistent with the promotion of good faith in international trade?

The Digest's discussion of CISG Article 83 describes the subsidiary nature of this provision, *vis-à-vis* Article 82. Thus, in circumstances where the buyer has lost the right to declare the contract avoided or to require substitute goods because it has

⁵⁰ UNCITRAL Digest, art. 82, ¶ 5.

⁵¹ Oberster Gerichtshof, Austria, 29 June 1999, English translation *available at* <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/990629a3.html>.

⁵² UNCITRAL Digest, art. 82, ¶ 6.

⁵³ Bundesgerichtshof, Germany, 25 June 1997, CLOUT case No. 235, English translation *available at* <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/970625g2.html>.

⁵⁴ Oberlandesgericht Koblenz, Germany, 27 September 1991, CLOUT case No. 316, English translation *available at* <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/910927g1.html>.

discarded, consumed, or resold them, other rights shall attach, such as the right to make use of other remedies (*i.e.*, price reduction, or the right to claim damages). The case law on this provision is somewhat scarce, and includes cases where Article 83 was cited to support a broader proposition concerning avoidance.⁵⁵

D. Article 84: The Buyer's Right to Interest on Amounts Paid and the Buyer's Obligation to Account to the Seller for Benefits Derived from the Goods

The Digest's discussion of Article 84 incorporates the principle that upon restitution any party that has derived a benefit from the contract must account for it to the other party. Hence, if a seller is bound to refund the price, he must also pay interest on it (from the date on which the price was paid). Similarly, a buyer is under a duty to account to the seller for all benefits he has derived from the goods.⁵⁶

Like CISG Article 78, Article 84(1) does not provide a specific rate of interest to be applied to sums that are due. Cases have taken differing approaches. Many courts have left the interest rate to be determined by the applicable domestic law.⁵⁷ One case applied the rate of interest applicable at seller's place of business, since that was where sellers were likely to have invested the payments they must refund.⁵⁸ Yet another case, which was later reversed in part, referred to the London Inter-Bank Offered Rate (LIBOR).⁵⁹ Leaving this gap in the contract can lead to upsetting or surprising results. For example, the rate of interest may be too low to compensate an already frustrated buyer, or it may be unusually high—making reimbursement difficult for the seller. A better rule is to include a provision that specifically includes a rate of interest or that provides a specific method

⁵⁵ UNCITRAL Digest, art. 83.

⁵⁶ UNCITRAL Digest, art. 84.

⁵⁷ See cases cited in UNCITRAL Digest, art. 84 n.6.

⁵⁸ Handelsgericht des Kantons Zürich, Switzerland, 5 February 1997, CLOUT case No. 214, English translation available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/970205s1.html>.

⁵⁹ International Chamber of Commerce Arbitration no. 6653, 1993, CLOUT case No. 103, available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/936653i1.html>.

for its determination. To address this specific issue, the following wording based on the CISG's text is suggested:

If the seller is required to refund the price, he shall refund it with interest at the rate of (x) per month from the moment payment was originally made.

To a certain extent, CISG Article 84(2) mirrors paragraph (1). Rather than requiring interest on any sum due, however, the buyer must account to the seller for any benefit he has derived from the goods as a means to avoid unjust enrichment. The Digest cites only two cases discussing this issue, focusing largely on the issue of burden of proof (the seller has the burden of proving the amount of the benefit conferred upon the buyer).⁶⁰

From a practical point of view, the seller's obligation to prove the value of the benefit conferred on the buyer may be a complicated task. This would justify the inclusion of a clause shifting the burden of proof to the buyer. Suppose the seller has sold greenhouses that later prove to be defective because they leak water (and the breach was fundamental); but the farmer was able to extract a benefit from the greenhouses because they provided shade and protection from the wind to the farmer's produce; and the farmer also made use of the greenhouses' irrigation system, thus producing a small return for the farmer. Because of the leakage, the greenhouses are useless during the rainy season and this could constitute a fundamental breach. If the seller is required to ascertain the value of the benefit conferred, he would be in a difficult position to do so, but the buyer has (or should have) all the accounting information. In the event of a dispute, a buyer may be unwilling to release any information to the seller on the benefit conferred by the defective goods. One way to overcome this difficulty would be to include the following clause:

In the event of avoidance, the Buyer will provide accurate information on any benefit that may have been derived from the goods or any part of them. In the event that the Seller questions the accuracy, the Seller may retain an independent accountant to determine the accuracy of the information submitted by the Buyer. The Buyer will allow the Seller and/or his authorized accountant access to review any and all books, accountings, ledgers, inventories, and similar documents. If the information is found

⁶⁰ UNCITRAL Digest, art. 84, ¶ 8.

to be inaccurate, the expense involved in retaining said professional shall be borne exclusively by the Buyer.

A clause such as this could serve as a disincentive to providing inaccurate accountings of what the buyer earned from the goods. Moreover, this clause would be consistent with the principle of good faith embodied in the CISG.

A buyer may still completely refuse to cooperate with the seller in determining the value of the benefit conferred by the goods or part of them. It would then be wise to have included some sort of liquidated damages or even a penalty clause (with prior consultation with counsel in the country where enforcement of the contract may be sought in order to avoid any violation of a rule of public policy).

E. Preservation of the Goods

CISG Articles 85 through 88 deal with preservation of the goods, an issue that can present itself in various circumstances, including when the buyer refuses to take over the goods (Article 85), or when he has received them but intends to exercise his right to send them back to the seller because of a defect that warrants avoidance (Article 86). Article 87 further provides that the party who is bound to preserve the goods may deposit them in the warehouse of a third party, or, in certain cases, may sell them. Finally, Article 88 provides that a party who is bound to preserve the goods in accordance with Article 85 or 86 may sell them by any appropriate means if there has been an unreasonable delay by the other party in taking them back, or in paying the price or cost of preservation, provided reasonable notice of the intention to sell has been given to the other party.

1. Preservation of the Goods by the Seller

Article 85 requires a seller that is facing a buyer reluctant to take over the goods, or to pay the price in situations where the obligations are concurrent, to take such steps as are reasonable in the circumstances to preserve them. The Digest explains that there have been a small number of decisions so far dealing with the issue of the seller's obligation to preserve the goods.⁶¹

⁶¹ UNCITRAL Digest, art. 85, ¶ 2.

Some cases dealing with Article 85 have discussed a right that a seller has to retain goods until it is reimbursed of its expenses incurred in preserving the goods.⁶² In general, this provision has provided little difficulty for the courts, save for the fact that some decisions have based a buyer's right to recover his expenses on Article 74 rather than on Article 85. Thus, a contract provision dealing with this issue should trace the language found in Article 85.

2. *Preservation of the Goods by the Buyer*

Article 86 similarly imposes on a buyer intending to exercise his right to reject the goods the duty to take such steps to preserve them as are reasonable under the circumstances. Moreover, a buyer is entitled to retain the goods until he has been reimbursed his reasonable expenses by the seller. The part of the Digest discussing Article 86 reports very little case law.⁶³ However, as with Article 85, the courts have faced some confusion and have at times based their decisions providing for the buyer's recovery of his preservation expenses on Article 74 of the CISG.⁶⁴ Thus, I would recommend that a clause dealing with this issue trace the language of Article 86, and include a reference to it in order to assist parties and the court in basing a decision on the correct provision of the Sales Convention, so that the judgment is "healthy," and less susceptible to an appeal.

3. *The Duty to Take Steps to Preserve the Goods*

CISG Article 87 clarifies that the preservation of the goods may be performed by depositing the goods "in a warehouse of a third person at the expense of the other party provided that the expense is not unreasonable." This rule applies to both the seller and buyer under Articles 85 and 86 respectively. The Digest cites few cases discussing this issue,⁶⁵ but generally speaking, they seem to have been decided correctly, save for one case. That case, an arbitration award, held the breaching buyer responsible for the seller's cost of storage of goods in a warehouse, but

⁶² UNCITRAL Digest, art. 85, ¶ 3.

⁶³ See UNCITRAL Digest, art. 86, ¶ 2.

⁶⁴ See, e.g., U.S. District Court for the Northern District of New York, United States, 7 September 1994, CLOUT case No. 85 (*Delchi Carrier, SpA v. Rotorex Corp.*, 1994 WL 495787).

⁶⁵ See UNCITRAL Digest, art. 87, ¶ 2.

denied recovery by the seller for damage to the goods during storage, because the risk of loss had not passed to the buyer under the applicable rules.⁶⁶ Though CLOUT cases are not per se binding, parties may wish to add certainty in a situation such by expressly providing who shall bear the risk of loss if the goods require storage.

4. *A Preserving Party's Right to Sell the Goods to a Third Party*

Article 88(1) deals with the issue of the right to sell the goods to a third party in two circumstances: when there has been delay in taking the goods back or expense involved in their preservation. To make the sale, notice to the other party is required. As explained by Professor Honnold, this proviso means that the party has an option to sell the goods.⁶⁷

Article 88(2) deals with goods subject to rapid deterioration or for which preservation would involve unreasonable expense. In this case, the non-breaching party must take all reasonable measures to sell them, and to the extent possible must give notice to the other party of his intention to sell. Professor Honnold explains that this proviso means that the party holding the goods has a duty to sell them,⁶⁸ and is obviously more flexible with the communication requirement. If the contract involves perishable goods, the seller may want to avoid questions about the notice requirement by including a clause stating:

Should the buyer refuse to take over the goods by the agreed upon date, the seller shall have the right to sell them without providing notice to the buyer.

If such a sale occurs, Article 88(3) authorizes the seller to retain from the proceeds an amount equal to the reasonable expenses incurred in preserving and selling the goods, but he must account for the balance.⁶⁹ The Digest includes only two cases that have dealt with the rules in Article 88(3). The first case, a decision

⁶⁶ International Chamber of Commerce Arbitration no. 7197, 1993, CLOUT case No. 104, available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/927197i1.html>.

⁶⁷ JOHN O. HONNOLD, UNIFORM LAW FOR INTERNATIONAL SALES 528, ¶ 457 (3d ed. 1999).

⁶⁸ JOHN O. HONNOLD, UNIFORM LAW FOR INTERNATIONAL SALES 528, ¶ 457 (3d ed. 1999).

⁶⁹ UNCITRAL Digest, art. 88, ¶ 5.

of the Iran/U.S. Claims tribunal,⁷⁰ held a seller correct in selling the goods where there was an unreasonable delay by the buyer in paying the price and the seller had given reasonable notice of its intention to sell. The seller was found to have sold in order to mitigate its damages, to have incurred expenses while attempting to sell the goods all over the world, and thus to be entitled to deduct its expenses from the sale proceeds. The other case cited under Article 88(3) was from a German court that reached a similar result, allowing the buyer of the goods to sell them after he had rejected them and placed them in storage, but denying agent and carriage costs because the buyer failed to prove it was entitled to such deductions.⁷¹ Because practitioners, judges, and arbitrators are being invited to look at the Digest, and the CLOUT cases, it would be wise to include language in a contract to clarify what expenses can be incurred either in storage, carriage, or in hiring a sales agent, when goods have been rejected by the buyer after receipt, or in cases where the buyer has refused to take over the goods.

5. *A Suggested Clause Regarding Preservation of the Goods*

Based on the previous discussion, the following clause deals with issues arising when the seller is required to preserve the goods:

The buyer is aware that if he fails to take over the goods, or to pay the price on the agreed upon date, that the seller may, in accordance with Articles 85 and 87 of the CISG, take such steps as are reasonable in the circumstances to preserve them, and that the seller may deposit the goods in a warehouse of a third person at the expense of the buyer in order to preserve the goods. Seller will be deemed to be holding the goods in bailment for the buyer who shall bear the risk of loss during such period and until the goods are either taken over by the buyer or sold to a third party. Until seller is reimbursed for the expenses incurred in caring for the goods, seller shall have the right to retain them as security.

⁷⁰ Iran/US Claims Tribunal, 28 July 1989 (*Watkins-Johnson Co. v. Islamic Republic of Iran*), available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/890728i2.html>.

⁷¹ Oberlandesgericht Hamburg, Germany, 26 November 1999, CLOUT case No. 348, English translation available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/991126g1.html>.

The seller shall provide notice to the buyer whenever the goods are deposited for storage under the preceding paragraph. The buyer's failure to respond to such notice within (x) days following receipt of such notice shall be construed as an authorization for the seller to sell the goods to a third party. Notwithstanding the seller's right to sell the goods, the buyer shall remain liable for damages and for reimbursement of the expenses incurred by the seller in caring for the goods, and in the event of a sale of the goods, the buyer shall reimburse the seller for all expenses related to such transaction, including but not limited to the payment of costs of sales agents, carriage, and other commissions, and expenses.

The buyer could use a similar clause in the event restitution is required after the contract has been avoided:

The seller is hereby made aware that if the buyer exercises his right to reject the goods after he has received the goods or after they have been placed at his disposal, the buyer may, in accordance with Articles 86 and 87 of the CISG, take such steps as are reasonable in the circumstances to preserve the goods, and that the buyer may deposit the goods in a warehouse of a third person at the expense of the seller. In such event, the buyer shall be deemed to be holding the goods in bailment for the seller who shall bear the risk of loss during such period and until the goods are either taken over by the seller or sold to a third party. Until the buyer is reimbursed for the expenses incurred in caring for the goods, the buyer shall have the right to retain them as security.

The buyer shall provide notice to the seller whenever the goods are deposited for storage under the preceding paragraph. The buyer's failure to respond to such notice within (x) days following receipt thereof shall be construed as an authorization for the buyer to sell the goods to a third party. Notwithstanding the buyers' right to sell the goods, the buyer may still claim damages and may seek reimbursement of the expenses incurred in caring for the goods, and in the event of a sale of the goods, the seller shall reimburse the buyer for the expenses involved in caring for and selling the goods to a third person, including but not limited to the payment of costs of sales agents, carriage, and other commissions, and expenses.