

THE FUNDAMENTAL BREACH OF CONTRACT OF SALE UNDER THE CISG

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Abstract. *While a breach of contract implies the failure of one party to fulfil the obligations arising from the contract, the fundamental breach of contract is an aggravated form of breach of contract. The concept of the fundamental breach of contract of sale is recognized in Article 25 of the CISG (UN Convention on Contracts for the International Sale of Goods, 1980). In an ordinary breach of contract of sales, the applicable legal remedies are ordinary legal remedies (such as substitution of goods, damages). In case of a fundamental (substantial) breach, the unilateral declaration of termination of the contract of sale is used as the last resort (to void the contract). Given that it is perceived as a special aggravated type of breach of contract of sale, the fundamental breach has to be carefully analysed in more detail.*

Key words: *Contract of sale, breach of contract, CISG*

1. INTRODUCTION

In post-World War II era, the international trade increased and triggered globalization. Since the law of the place of destination of goods is the applicable law in disputes including a foreign element in international trade, there is unspecified applicable law for the seller. Naturally, national contract law provisions are insufficient to regulate the international sales transactions. The globalization of trade entails the regional and global unification of sales law (Ruangvichathorn, 2020:133).¹ Therefore, the UNCITRAL (the UN Commission on International Trade Law) drafted the text of the CISG (UN Convention on Contracts for the International Sale of Goods) in 1980 to create uniform sales law at the global level and to reduce

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¹ Ruangvichathorn Jumpita, The Harmonization of ASEAN Sales Law: A Comparative Study with Thai Sales Law and CISG, *Thammasat Law Journal*, Vol.49, No.1, 2020, page 133.

legal uncertainty. The CISG has 93 signatory states. It is clear that it removes legal barriers to a certain degree (Ay, 2021:138).²

Breach of contract is not defined in the CISG. In legal doctrine, it may be defined as the unjustifiable failure of any provision or condition of the contract by one of the parties. Differently from the ordinary breach of contract of sale, the CISG recognizes the concept of fundamental breach of contract of sale. Under Article 25 CISG, a breach of contract of sale is considered 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.” (Jovicic, 2018: 41).³ This provision sets up two criteria to assess breach as the fundamental breach: detriment and foreseeability (Huber, Mullis, 2007: 213).⁴ As a result of the fundamental breach, it is possible to resort to the avoidance of contract, which is a unilateral termination of contract as the last resort. Given that it is perceived as a special type of breach of contract of sale, the fundamental breach has to be carefully analysed.

2. THE DEFINITION OF THE FUNDAMENTAL BREACH OF CONTRACT

2.1. Detriment

Under Article 25 of the CIGS, In order to be deemed fundamental, a breach of contract of sale must result in a detriment that “substantially deprives” the aggrieved party of what he is “entitled to expect under the contract”. The reference to “under the contract” is certain proof that the yardstick for breach of contract of sale is first in the express and implied provisions of the contract of sale itself (Koch, 1998: 71).⁵ This reference is a decisive factor. For instance, according to the principle of freedom of contract, the parties have free will to specify their contract whose breach is considered to be fundamental or substantive (Ahmed, Hussein, 2017: 128).⁶ However, if there is no choice of law clause specifying the fundamental breach, this reference causes open questions regarding other circumstances which should be taken into account, such as: negotiations, trade practices between parties, usages, and any subsequent conduct of the parties (Koch, 1998: 71). Article 9 of the CISG fills the gap in this situation. Pursuant to Article 9 of the CISG, the parties are bound by any trade usages or business practices to which they have agreed or established between them. For instance, the China Arbitration Commission found that the parties had established a business practice regarding the issue of quality (specifically, of confirming the cloth sample) in the stage of performing the “general” contract (Pamboukis, 2005:

² Ay, Yunus Emre, The Scope of the Convention on International Sale of Goods, *Uluslararası Ticaret ve Tahkim Hukuku Dergisi (Journal of International Trade and Arbitration Law)*, Vol.10, Issue:1, 2021, p. 138.

³ Jovicic Katarina, The Concept of the Fundamental Breach of Contract in the CISG, *Strani pravni zivot/ Foreign Legal Life*, Issue:4, Belgrade, 2018, page 41.

⁴ Huber, Peter, MULLIS Alastair, The CISG A New Textbook for Students and Practitioners, *European Law Publishers*, 2007, page 213.

⁵ Koch Robert, The Concept of Fundamental Breach of Contract under the United Nations Convention on Contracts for the International Sale of Goods, LLM Dissertation, Supervisor: David Stevens, *McGill University Faculty of Law*, 1998, p. 71

⁶ Ahmed Bzhar Abdullah, HUSSEIN Hassan Mustafa, Avoidance of Contract as a Remedy under CISG and SGA: Comparative Analysis, *Journal of Law, Policy and Globalization*, Vol.61, 2017, page 128.

113).⁷ Therefore, it is seen that determination of detriment criterion depends on the merits of each specific case. The CISG Secretariat Commentary explains the determination of detriment as follows:

“The determination whether the injury is substantial must be made in light of the circumstances of each case, e.g. the monetary value of the contract, the monetary harm caused by the breach, or the extent to which the breach interferes with other activities of the injured party.” (Agapiou, 2016: 153)⁸

2.2. Foreseeability

Foreseeability is the other criterion of fundamental breach but it does not shed much light on the concept of fundamental breach. First of all, the criterion of foreseeability is vague. Even if a breach of contract of sale causes substantial deprivation of what the buyer was entitled to expect under the contract between parties, there is no fundamental breach if the breaching party (seller) *“did not foresee and a reasonable person of the same kind in the same circumstances would not have foreseen such a result”* (Article 25 CISG). It is explained that *“one must not only take into account the actual subjective knowledge of the defaulting party but also inquire into whether an average party to the same kind of contract and in the same circumstances would have foreseen the result”* (Agapiou, 2016: 154). Therefore, many scholars are of the opinion that foreseeability is a burden of proof rule and requires taking into account the defaulting party’s knowledge of the harsh consequences of the breach of contract of sale. On the other hand, the foreseeability criterion under Article 25 of the CISG has a similar effect as the same criterion under the general rule for calculation of damages in Article 74 CISG. There is a limitation imposed on the aggrieved party in case the other party could not foresee the far-reaching consequences (Koch, 1998: 72).

Another point that should be examined refers to the term *“a reasonable person of the same kind in the same circumstances”*, which includes another ambiguity. Some authors suggest that the concept of “foreseeability” entails not only the subjective perspective of the defaulting (breaching) party but also the objective perspective of the reasonable merchant on the position of the defaulting party (Koch, 1998: 72). Yet, it is still insufficient to understand the concept of a reasonable person. Other authors suggest that the qualification of a reasonable person and the defaulting party have the same socio-economic background. Prior dealings, negotiations, political climate, legislation, global and regional market conditions are taken into account to assess ‘the same circumstance’ (Ahmed, Hussein, 2017: 129).

In addition, the most debated issue under Article 25 of the CISG is the time of foreseeability because there is no provision which regulates determination of the foreseeability time in Article 25 CISG. It is unclear whether the time of forming or breaching a contract must be considered to determine the time of foreseeability (Ahmed, Hussein, 2017: 129). In the doctrine, some scholars are of the opinion that the time of the conclusion of contract should be accepted because rights and obligations of parties are determined when

⁷ Pamboukis Ch., The Concept and Function of Usages in the United Nations Convention on the International Sale of Goods, *Journal of Law and Commerce*, Vol:25, Issue:1, 2005, p. 113.

⁸ Agapiou Nevi, Buyer’s Remedies under the CISG and English Sales Law: A Comparative Analysis, *University of Leicester School of Law*, PhD Thesis, 2016, p.153.

the contract is concluded (Sayin, 2019: 94-95).⁹ In this view, foreseeability is a substitute for provisions or a part of the contract of sale (Ishida, 2020: 75).¹⁰ Professor Schlechtriem (1998) explains this view as a substitute for certain contractual terms as follows:

“In the author’s opinion, the role which foreseeability plays makes it clear that it is the time when the contract was concluded that is decisive. The promisor’s knowledge or the foreseeability of the promisee’s interest in individual contractual obligations and methods of performance can be a ‘substitute’ for the need to reach clear agreement in the contract on the importance for those matters, i.e. it can make an appropriate interpretation of the contract possible. However, the importance attached by a promise to a particular obligation, which has been shown otherwise than by express agreement, must nevertheless be fixed by the time the contract is concluded. If knowledge or foreseeability is to be equivalent to express agreement, it must in any event exist at the time when the contract was concluded.” (Ishida, 2020:75).

3. SPECIFIC CASE SCENARIOS

3.1. Delay in Delivery

As a general principle, late delivery does not constitute a fundamental breach of contract of sale. The buyer may claim damages when the delay causes any damage. For this reason, generally, he is not entitled to terminate the contract of sale. Further circumstances must be presented to consider the delay as a fundamental breach. Where the buyer and the seller have agreed that the delivery time of goods is of the essence for the performance of the contract (e.g. in case of just-in-time delivery), late delivery may constitute a fundamental breach of contract of sale (Magnus, 2005: 434).¹¹ The punctual delivery may be sensitive in some cases. The nature of goods is important. In particular, perishable goods should be delivered on time. Seasonal articles should also be delivered on time. Late delivery of seasonal goods may prevent the marketing of such goods on time. The most interesting example is that delay will also be considered fundamental where it was clear that the buyer had already resold the goods (Huber, Mullis, 2007: 226). In accordance with these examples, the Oldenburg District Court refused fundamental breach in a conflict between an Italian seller and a German buyer, where the seller had delivered summer clothes one day later than the agreed time. Relying on the fact that the buyer accepted delivery of the goods instead of refusing them, the German Court concluded that punctual delivery was not essential for the relationship (Koch, 1998: 45-46).

If both parties fail to perform their obligations on time, one party may fix additional time to the other party to carry out the obligations, regardless of whether the obligation is ancillary or basic. The seller may fix additional period for the buyer to take over the goods, pay the price, or to enable the seller to complete delivery process. The buyer may fix additional

⁹ Sayin Ceren, *Viyana Satım Sözleşmesinde Satıcının Ayıptan Doğan Sorumluluğu (Liability of the Seller for Default in the Convention on International Sale of Goods)*, LLM Thesis, *Ankara University Faculty of Law*, Supervisor: Prof. Hasan Ayrancı, Ankara, 2019, pp. 94-95.

¹⁰ Ishida Yasutoshi, Identifying Fundamental Breach of Article 25 and 49 of the CISG: The Good Faith Duty of Collaborative Efforts to Cure Defects – Make the Parties Draw a Line in the Sand of Substantiality, *Michigan Journal of International Law*, Volume:41, Issue:1, 2020, page 75.

¹¹ Magnus Ulrich, The Remedy of Avoidance of Contract under CISG – General Remarks and Special Cases, *Journal of Law and Commerce*, Vol:25, 2005, p. 434.

period for the seller to deliver goods, supply substitute goods in case of nonconformity of goods, and repair non-confirming goods (Duncan, 2000: 1383).¹² This additional time for performance must be a reasonable time. According to Peter Schlechtriem, the reasonable time depends largely on the circumstances as follows (Duncan, 2000: 1384):

- “1 Length of time of the contractual delivery period (transactions with short delivery dates justify a shorter additional period, long delivery dates require a longer additional period);
2. The buyer’s recognizable interest in rapid delivery, if the seller should have been aware of that interest upon conclusion of contract;
3. The nature of the seller’s obligation (a longer period is reasonable for delivery of complicated apparatus and machinery of the seller’s own manufacture than for delivery of fungible goods by a wholesaler);
4. The nature of the impediment to delivery (if the seller is affected by a fire or strike, the buyer can be expected to wait for a certain time if the delivery is not particularly urgent).”

3.2. Definite Non-Delivery

Where the seller refuses the delivery of goods or does not deliver the goods, such non-performance constitutes fundamental breach. If the performance of the contract is significantly carried out, there is no fundamental breach (Magnus, 2005: 433). If the seller declares that he will not definitely perform his obligations, it will usually be considered as a fundamental breach (Huber, Mullis, 2007: 227). In *Ste Calzados Magnanni v SARL Shoes General International* case, the buyer (a French company) ordered 8651 pairs of shoes from the seller (a Spanish company). However, the seller denied order made by the buyer and refused delivery. As a result of this situation, the buyer resorted to the avoidance of the contract and got shoes from other manufactures. The court ruled that “*refusal, without any legitimate reason, to fulfil an order received by falsely maintaining that the order had not been placed constitutes a fundamental breach by the seller within the meaning of Article 25 of the CISG.*” (Ahmed, Hussein, 2017: 131).

3.3. Delivery of non-Confirming Goods

Delivery of non-confirming goods is one of the most debated issues within the context of the fundamental breach of contract of sale. Pursuant to Article 35 of the CISG, the seller must deliver the goods in the manner required by the contract. The goods must be of the quantity, quality and description required by the contract. Unless otherwise agreed by the parties in the contract of sale, the confirming goods shall meet the following conditions:

- a) they are fit for the purposes for which goods of the same description would ordinarily be used,
- b) they are fit for any particular purpose which is clearly (expressly) or tacitly (impliedly) made known to the seller at the time of formation of the contract of sale,
- c) they have the same quality as the sample goods sent from the seller to the buyer,
- d) they are packaged or contained in the ordinary manner for such goods or, if there is no such manner, in a manner adequate to preserve and protect goods.

¹² Duncan JR John C., *Nachfrist Was Ist? Thinking Globally and Acting Locally: Considering Time Extension Principles of the UN Convention on Contracts for the International Sale of Goods in Revising the Uniform Commercial Code*, *BYU Law Review*, Vol:2000, Issue:4, 2000, p. 1383.

This article became the subject matter of many cases. On 28 December 2008, the Shanghai First Instance Court ruled that there is the fundamental breach in case the seller had delivered only minor parts of the liquors ordered by the buyer and none of the brands listed in the contract of sale. Other courts rendered similar decisions in cases where the major part of the goods were either non-confirming or significantly affected by the non-confirming goods. An American court ruled that it is a fundamental breach of the contract of sale that 93% of delivered goods perform below the standard cooling capacity for air conditions. In a French case, it was ruled that 380 of 445 non-confirming motherboards constitute the fundamental breach. A German court held that 420 kg out of 22 tons non-confirming goods amounts to a fundamental breach. In an Italian case, the value of more than 90% of the non-confirming goods amounts to a fundamental breach. However, it should be noted that excess delivery of goods does not constitute fundamental breach (Chen, Pair, 2011: 669).¹³

One of the most important cases related to Article 35 of the CISG is the “*New Zealand Mussels case*”, which was heard by the German Court in 1995.¹⁴ The German buyer ordered 1750 kg of New Zealand Mussels from the Swiss seller, and the seller delivered the goods on time to the place agreed by the parties. Upon the seller’s payment request, the buyer notified that the level of cadmium concentration is higher than the rate determined by the German authorities. The German court ruled that the foreign seller cannot know the public law provisions and administrative criteria; therefore, the buyer cannot rely upon the knowledge of the foreign seller; the buyer can be expected to have such information in the place of destination or in his own country. The buyer must give relevant information to the seller. Therefore, the German court accepted the seller’ request for payment from the buyer (Atamer, 2005: 202).¹⁵ For this situation, the German court determined three exceptions as follows:

- 1) The country of the seller has the same standards as the country of the buyer.
- 3) The seller was informed about the standards of goods by the buyer.
- 3) Relevant factors (such as: the relationship between the buyer and the seller in pre-shipment of goods, the existence of the headquarter or a branch of the seller in the country of the buyer, the fact that the seller sells the goods to the country of the buyer for a long time, or other reasonable conditions) demonstrating that the seller knows the criteria in the country of the buyer (Can, Tuna, 2019: 2186).¹⁶

In a different case, the Spanish seller had been selling spice to the German buyer regularly. In the last order, the Spanish seller sold a bulk of spice containing a high level of ethylenoxid. The German buyer wanted to substitute spices due to the high ethylenoxid level. The German courts justified the request of the German buyer by the fact that both parties had a long-term spice trade relationship (Atamer, 2005: 202). In particular, a

¹³ Chen Markus Müller, Pair Lara M., Chapter 35: Avoidance for non-Conformity of Goods under Art. 49(1)(A) CISG, in: Liber Amicorum Eric Bergsten International Arbitration and Commercial Law: Synergy, Convergence and Evolution, Edited by Stefan Kröll, L.A. Mistelis, P. Perales Viscasillas & V. Rogers, *Kluwer Law International*, 2011, p. 669.

¹⁴ Article 35(2)(a) CISG “fit for the purpose for which they would ordinarily be used”.

¹⁵ Atamer Yeşim Müride, Uluslararası Satım Sözleşmelerine İlişkin Birleşmiş Milletler Antlaşması (CISG) Uyarınca Satıcının Yükümlülükleri ve Sözleşmeye Aykırılığın Sonuçları (The Seller's Obligations and the Consequences of Breaching the Contract of Sale under the CISG), Beta Yayınları, İstanbul, 2005, p. 202

¹⁶ Can Hacı, Tuna Ekin, Sınırtaşın Sözleşmelere İlişkin Meseleler Gümrükten Geçmeyen Mallardan Kaynaklanan Hukuki Sorumluluğa İlişkin Bir Vaka İncelemesi (Issues Related to International Contracts: A Case Study of Legal Liability Arising from Non-customs Goods), *Dokuz Eylül Üniversitesi Hukuk Fakültesi Dergisi*, Volume:19, Issue:2, 2019, p. 2186.

revolving letter of credit may create a presumption as it proves long-term trade between the buyer and the seller.

3.4. Breach of other Obligations

A breach of obligations other than those presented in the aforesaid situations may also amount to a fundamental breach. A Letter of Credit (L/C) fraud may be considered a fundamental breach. Additional obligations are provided in the CISG. For instance, pursuant to Article 32 of the CISG, the seller must provide the identification of the goods to arrange for the carriage of the goods or give notice of the consignment specifying goods if there is no identification. Such a violation of obligations may amount to a fundamental breach. Furthermore, additional obligations may be specifically agreed by the parties (Magnus, 2005:435). For example, if both parties have agreed the documentary letter of credit as the payment method and the buyer will not open the letter of credit, this amounts to a fundamental breach of contract of sale (Taştan, 2019: 387-388).¹⁷

4. CONCLUSION

The fundamental breach of contract of sale is a special form of breach of contract in the CISG (UN Convention on Contracts for the International Sale of Goods, 1980). Thus, it is important to determine whether the breach of contract of sale is an ordinary breach or a fundamental breach in order to enjoy avoidance of contract or not. Since the purpose of the CISG provisions is to keep the contract of sale in effect, the fundamental breach which causes the termination of contract is considered the last resort (Toker, 2016: 241).¹⁸

Secondly, the fundamental breach has two elements: the detriment (substantial deprivation of the aggrieved party of what he is “entitled to expect under the contract”) and foreseeability. The determination of these basic two elements depends on the merits of each specific case. Both elements are determined in accordance with the provisions of the contract of sale. Therefore, the fundamental breach of contract of sale should be assessed on the case- by-case basis. In the sale of goods, the common types of fundamental breach are overdue delivery of goods, definite non-delivery of goods, and delivery of non-confirming goods. However, some other violations (e.g. L/C fraud or a failure open an L/C, failure to identify the goods, provide specification or give notice) may also amount to a fundamental breach.

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¹⁷ Taştan Furkan Güven, Viyana Satım Antlaşmasına (CISG) Göre Alıcının Sözleşmeyi İhlali Halinde Satıcının Hakları (The Seller's Rights in Case of Buyer's Breach of Contract under the CISG), *Yıldırım Beyazıt Hukuk Dergisi*, Year:3, Issue:1, 2019, pp. 387-388.

¹⁸ Toker Ali Gümrah, Viyana Satım Sözleşmesi (CISG) Uyarınca Sözleşmenin Esaslı İhlali (Fundamental Breach of Contract pursuant to the CISG), *Public and Private International Law Bulletin*, Volume:33, Issue:1, 2016, p. 241.

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BITNA POVREDA UGOVORA O PRODAJI PREMA KONVENCIJI UN O UGOVORIMA O MEĐUNARODNOJ PRODAJI ROBE (CISG)

Dok obična povreda ugovora predstavlja neizvršenje ugovorne obaveze jedne od ugovornih strana, bitna povreda ugovora predstavlja teži oblik povrede ugovora. Koncept bitne povrede ugovora o prodaji prepoznat je u članu 25 Konvencije UN o ugovorima o međunarodnoj prodaji robe (CISG, 1980). Prilikom obične povrede ugovora o prodaji, primenjuju se redovna pravna sredstva kao što su zamena robe, naknada štete, itd. Prema članu 25 Konvencije UN o ugovorima o međunarodnoj prodaji robe (CISG), kod bitne povrede ugovora o prodaji, jednostrana izjava o raskidu ugovora o prodaji primenjuje se kao poslednje sredstvo. S obzirom da se radi se o posebnoj i teškoj obliku povrede ugovora, bitna povreda ugovora o prodaji zaslužuje pažljivu analizu.

Ključne reči: ugovor o prodaji, bitna povreda ugovora, Konvencija UN o ugovorima o međunarodnoj prodaji robe (CISG)