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Risky Business: The Impact of the CISG on the International Sale of Goods. A Guide for Merchants to Limit Liability and Increase Certainty Inside and Outside of the CISG.

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A. Introduction

I. The Changing International Landscape of the Sale of Goods, Scope of Note

The ever-increasing globalization of commerce creates a great opportunity for merchants to increase revenue by expanding into new, foreign markets. However, along with this great opportunity comes the complexity of transacting with foreign buyers, who likely have different sales laws and trade customs. The potential for dispute in a transnational sale is great.

Limiting liability and increasing certainty in the international sale of goods requires forethought in contracting by merchants and their counsel. This note will 1) identify key issues faced by international merchants, 2) discuss these issues in relation to international law developments, with a strong emphasis on the Convention on the International Sale of Goods ("CISG"), and 3) offer practical advice for merchants and their counsel to assist them in limiting potential liability, while increasing transaction certainty.

The issues addressed within this note are: 1) choice of law, 2) risk of loss, trade usage, and breach of contract, 3) insurance, insolvency/bankruptcy, 4) E-Commerce, and 5) preventive law. The discussion will consider only commercial sales and will not attempt to address the various consumer protection laws that are in place in many nations.[1]

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* J.D. 2006, Indiana University School of Law – Indianapolis. I would like to thank my family and friends for their continued support throughout the writing of this Note. A special thanks, together with all of my love, is extended to my husband Mark Dutton who got me through the tough times.

[1] Commentary on the Draft Convention on Contracts for the International Sale of Goods prepared by the Secretariat, (2002), available at http://www.cisg-online.ch/cisg/materials-commentary.html.

> It should be noted, however, that article 2 excludes from the sphere of application of this Convention certain contracts for the sale of goods which are likely to be characterized as "civil" contracts by a legal system which recognizes the distinction between civil and commercial contracts. Most notably, article 2 (a) excludes from

European Journal of Law Reform, Vol. VII, no. 3/4, pp 239-275.
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II. Importance of Note

Merchants engaging in the international sale of goods and their counsel need to be able identify potential issues, determine the applicable law, and plan accordingly. Although still in its formative stages, the CISG has altered, and will continue to alter, the landscape of transnational trade. Knowledge of the effects of CISG on international sales is essential for international merchants and their counsel in order to limit merchants' liability and increase certainty when transacting, even when attempting to avoid the CISG's applicability.

III. Establishment and Scope of the CISG

Faced with technological advances making transnational sales common, merchants sought certainty and uniformity in the law. This yearning resulted in the enactment of the 1980 United Nations Convention On Contracts For The International Sale Of Goods (CISG)[2] on 1 January 1988. "Today with [over] 62 contracting States representing over two thirds of world trade, this convention provides a (potentially) uniform regime for international sales."[3] The following chart lists the sixty-seven countries that have adopted the Convention.[4] Two notable countries that have not adopted the CISG are England and Japan.[5]

> the sphere of application of this Convention sales "of goods bought for personal, family or household use." *Id.*
>
> The Convention does not define 'goods'. Nevertheless, pursuant to Article 7(1), the concept of 'goods' should be interpreted autonomously, in light of the Convention's 'international character' and 'the need to promote uniformity in its application', rather than by referring to domestic law for a definition.

Institute of International Law, at http://cisgw3.law.pace.edu/cisg/text/anno-art-01.html#ud17 (last updated 25 Jan. 2005).

[2] S. Treaty Doc. No. 9, 98th Cong. 1st Sess. 22 (1983) [hereinafter CISG], reprinted at USCS Int'l Sale of Goods (2005). The text of the CISG also is readily available from electronic sources: http://www.uncitral.org (official text in English, Arabic, Chinese, French, Russian, and Spanish); http://www.cisg.law.pace.edu.

[3] *Private International Commercial Law: Sale of Goods, LexMercatoria*, at http://www.jus.uio.no/lm/private.international.commercial.law/sale.of.goods#cisg (n.d.)(last visited 4 Feb. 2005).

[4] E. G. Gabbard, J.D., C.P.M., CPCM., *International Contracting: The UNCISG Applies,* 15 (12) Inside Supply Management 16 (2004), available at http://www.napm.org/Pubs/ISMMag/120416.cfm (last visited 4 Feb. 2005).

[5] *Id.*

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COUNTRIES THAT HAVE ADOPTED THE CISG

Argentina	Ecuador	Latvia	Russian Federation
Australia	Egypt	Lesotho	Saint Vincent and the Grenadines
Austria	Estonia	Liberia	
Belarus	Finland	Lithuania	Serbia
Belgium	France	Luxembourg	Singapore
Bosnia and Herzegovina	Gabon	Mauritania	Slovakia
	Georgia	Mexico	Slovenia
Bulgaria	Germany	Mongolia	Spain
Burundi	Greece	Netherlands	Sweden
Canada	Guinea	New Zealand	Switzerland
Chile	Honduras	Norway	Syrian Arab Republic
China	Hungary	Paraguay	Uganda
Colombia	Iceland	Peru	Ukraine
Croatia	Iraq	Poland	United States of America
Cuba	Israel	Republic of Korea	Uruguay
Cyprus	Italy	Republic of Moldava	Uzbekistan
Czech Republic	Kyrgyzstan	Romania	Zambia
Denmark			

Article I of the CISG sets forth the following criteria for determining whether parties to a sale are bound by the convention: "When the sale of goods is between parties whose place of business are in different states or when the rules of private international law lead to the application of the law of a Contracting State."[6]

B. Choice of Law

I. Definition and Importance

Disputing buyers and sellers have placed arbitration panels and courts worldwide in the position of determining what law applies in a transaction involving the international sale of goods.[7] As the determination of what law applies to a particular transaction often determines liability, it is crucial for sellers and their counsel to be aware of what law will govern a transaction when engaging in international trade. Uncertainty reigns in sales transactions that cross national boundaries and are silent as to the governing law in the event of dispute. The

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[6] CISG, *supra* note 2, *Annotated Text of CISG Article 1*, available at http://cisgw3.law.pace.edu/cisg/text/e-text-01.html. "As the list of Contracting States is growing, this criterion is leading more and more often to the applicability of the Convention." *Id.*

[7] "There are many Article 1 cases – almost every CISG case is in a certain sense an Article 1 case." Institute of International Law, at http://cisgw3.law.pace.edu/cisg/text/anno-art-01.html#ud17 (last updated 25 Jan. 2005).

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obvious solution to this uncertainty is for merchants to include a provision in the sales contract specifying which jurisdiction's law will apply in the event a dispute does arise: a choice of law clause.[8]

In the event of a dispute, both the buyer and seller would likely desire their own local or national law to apply. Parties to a sale want this for obvious reasons: familiarity with their own state's applicable law and perceived or real advantage in their state's dispute resolution system, if litigation were to occur.[9] But what if a seller and buyer cannot agree on the law to apply in the event of a dispute? These situations are not uncommon in regard to especially stubborn parties or contracts with state enterprises in Third World countries or with enterprises in Eastern Europe.[10] B. Blair Crawford, writing in the Journal of Law & Commerce, sums up a typical situation involving American and foreign counsel negotiating a choice of law clause:

> Choice of law, like dispute resolution and other legal issues, is generally left to the end when, if a bargain has actually been struck, the merchants are anxious to conclude the transaction. Each side demands its own law and rejects the other's for a variety of real and not-so-real reasons. American lawyers tend to be unfamiliar with foreign legal systems and to doubt that their clients can receive a fair hearing, while foreign lawyers are very much afraid of the cost of U.S. litigation and of what they perceive to be its unpredictability. The usual compromise is the law of (and often a forum in) some "neutral" third country such as Sweden or Switzerland since choice of law and choice of forum tend to go hand-in-hand.[11]

1. Option 1: The Choice of a Neutral State's Law

Parties could choose to have a jurisdiction's law in which neither party resides, be the governing law of their contract.[12] While this could be a compromise worth accepting, as neither party would seem to have an advantage, this option could be perilous. Merchants need to be aware that the selection of a neutral domestic law may lead one of the contracting parties to have its own domestic law apply.[13] "[M]any countries in their push to modernize their domestic laws have taken over well established civil laws."[14] If a seller is not aware that a buyer's country

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[8] *See generally* T. J. Drago & A. F. Zoccolillo, *Be Explicit: Drafting Choice of Law Clauses in International Sale of Goods Contracts*, Metropolitan Corporate Counsel (May 2002), at 9.

[9] *See id.*

[10] P. Winship, *Changing Contract Practices in the Light of the United Nations Sales Convention: A Guide for Practitioners,* 29 Int'l Law. 525 (1995), available at http://www.cisg.law.pace.edu/cisg/biblio/winship.html.

[11] B. Blair Crawford, *Drafting Considerations Under the 1980 United Nations Convention on Contracts for the International Sale of Goods*, 8 J.L. & Com. 187-205 (1988).

[12] *See generally* CISG, Article 1.

[13] B. Zeller, *Application of the CISG and Reasons Why It Matters to You and Your Client, at* http://www.business.vu.edu.au/cisg/CISGhome.htm (n.d.) (last visited 4 Feb. 2005).

[14] *Id.*

> Two considerations should be taken before this practice of exclusion is considered or continued. Let us assume that an Australian Trader wishes to sell goods to Turkey. Neither of the two parties wants to be governed by any of the two domestic systems.

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has adopted another nation's sales law, the seller may unwittingly agree to the application of the third country's law believing it to be a neutral law; when, in fact, it is the buyer's law as well.[15] This can place the buyer in a stronger position in the event of a dispute.[16]

2. Option 2: Agreement to be Bound by the CISG

If either party lives in a state that is a signatory to the CISG, a party refusing to be bound by the other party's law could agree to be bound by the CISG's law by merely not expressly opting out of the CISG. Parties living in places where neither party is a signatory to the CISG could, conversely, agree to be governed by CISG law.[17]

II. Choice of Law and the CISG

The Convention's approach provides an effective solution for the difficult problem of choice of law. The CISG provides an alternative to choosing any state's law as the governing law of the sale, enabling both parties to a contract to remain on equal footing.[18] "The CISG was created to specifically address international business expectations and is a neutral choice of law that is fair to both buyers and sellers. The similarity of the CISG to the UCC makes it less daunting to apply for American merchants and attorneys."[19]

> The Turkish buyer proposes to use the law of a neutral country namely Switzerland. The effect of that choice of law is that the Turkish buyer in practice is using his own law as Turkey in their modernization of commercial laws introduced the Swiss commercial Code (OR) into their own system. The Australian buyer now has to deal with a foreign law whereas the buyer uses his own, well understood domestic law merely with a different front cover. This is not an isolated case as many countries in their push to modernize their domestic laws have taken over well established civil laws such as Italian, German or Swiss commercial laws. Another point to remember when opting for a foreign domestic law is that the domestic system needs to be understood as each system has its own idiosyncrasies. Lets revert back to Swiss law and consider that under article 1(2) of the Civil Code a judge in view of an issue not resolved by the law, has to "make" a law in other words he has to act as legislator. It is quite feasible therefore that despite the exclusion of the CISG a judge could decide that Swiss law should be brought in line with the CISG to achieve a desired outcome.
>
> A second point which needs to be considered is the effects of globalization. Exporters and Importers in Australia are no longer in a position to have their own way with the choice of law and forum selection. The lack of a widely accepted alternative to the laws of England are gone or changing. The alternative namely the CISG has found wide acceptance and will increasingly become the accepted "lex mercantoria".

Id.

15 *See Id.*

16 *See Id.*

17 *See Id.*

18 Winship, *supra* note 11.

19 T. McNamara, *Graduating from Obscurity: The U.N. International Sale of Goods Convention,*

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In the event either party lives in a signatory state, when a contract for an international sale of goods does not make clear which rule of law applies, the Convention provides uniform rules to govern the questions that arise in making and performance of the Contract.[20] As the CISG becomes better known, it is likely to become an acceptable compromise choice of law, even where it might not otherwise be applicable.[21]

III. Opting Out of the CISG

The CISG allows parties to opt out of the provisions set forth by the Convention by contracting for specific domestic law to apply.[22] While some parties may prefer to opt out of the CISG and contract for their own domestic law to govern the contract (for the familiarity and advantage before tribunal reasons previously stated, perhaps), this may create a barrier to business, if an agreement cannot be reached as to whose law should apply.[23] Put another way, the CISG came into existence as a neutral alternative when a choice of law conflict between a buyer and seller threatens to hinder the transaction's completion. Opting out of the CISG brings the parties back to their pre-CISG position: stalled, due to neither party wishing to agree to the other party's choice for which jurisdiction's law will govern the contract.

Parties may wish to opt out of the CISG for other reasons. Some might opt out due to the relatively small amount of time that the CISG has been in existence. Merchants are still unsure about the applicability of the CISG. Domestic courts

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(presented at the Second Annual Florida Bar International Litigation Update Conference International Litigation and Arbitration Committee International Law Section Florida Bar Association, 24 June 2004, Boca Raton, Florida), available at http://66.218.71.225/search/cache?p=Graduating+from+Obscurity%3A+The+U.N.+International+Sale+of+Goods+Convention&sm=Yahoo%21+Search&toggle=1&ei=UTF8&u=www.dgslaw.com/articles/565324.pdf&w=graduating+obscurity+u+n+international+sale+goods+convention&d=632CAEB9E3&icp=1&.intl=us (last visited 4 Feb. 2005).

[20] *See* M. W. Gordon, *Section III: Part II: Some Thoughts on the Receptiveness of Contract Rules in the CISG and UNIDROIT Principles as Reflected in One State's (Florida) Experience of (1) Law School Faculty, (2) Members of the Bar with an International Practice, and (3) Judges*, 46 Am. J. Comp. L. 361, 365 (1998).

[21] *See id.*

[22] CISG, *supra* note 2, *Annotated Text of CISG Article 6,* available at http://cisgw3.law.pace.edu/cisg/text/e-text-06.html. (Article 6 of the CISG states: The parties may exclude the application of this Convention or, subject to article 12, derogate from or vary the effect of any of its provisions.) *Id.*

[23] *See* McNamara*, supra* note 19.

> The CISG is fair and, overall, does not appear to favor buyers at the expense of sellers or vice-versa. The Convention is reasonably well drafted. To the extent that parties have equal bargaining strength and are locked in a struggle over the choice of substantive law governing sales, selection of the CISG may be viewed as a constructive, neutral, and even-handed approach.

Id.

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are unfamiliar with the CISG and case law in these courts is sparse.[24] "The unfamiliarity of traders, lawyers, and courts with the CISG may raise transactional costs and the costs of dispute adjudication."[25]

Assuming that the CISG is applicable to a dispute, practitioners may be faced with the issue of establishing or proving CISG law to the court.[26] "In the absence of any binding precedent in […] state and federal courts, lawyers will likely need to rely on other reported decisions in the United States and on treatises, articles, and other commentary."[27] Another option may be for practitioners to use CISG cases from other contracting states. "This trend may lead to a more unified approach to CISG legal issues."[28]

IV. Advice to Practitioners

When should a merchant opt out of the CISG? "Each international transaction is different. The parties should carefully analyze whether the CISG applies or

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[24] *Id.*

[25] *Id. See also* ALI-ABA Course of Study Materials, Product Distribution and Marketing Volume II, March 1997.

> Pitfalls of International Agency Agreements
> a. U.N. Convention for the Sale of Goods Parties to indefinite agreements may find themselves subject to the provisions of the CISG unless they specifically exclude the convention's provisions within their agreement.
> b. Company or Individual Principals should check local country laws in advance, since some nations allow only companies to enter into agency agreements, for instance China, while individual agents in countries like Spain, Argentina, and Mexico may fall within the purview of the respective labor laws.
> c. Indemnity for TerminationMany nations, including EU nations now require compensation for goodwill accrued and business generated payable to the agent upon termination. Principals should be aware of this and plan the agreement accordingly.
> d. Import Control LawsThe principal should insure that the product underlying the agency agreement is not subject to controls, as many countries including Egypt, Saudi Arabia, and Korea have various restrictions on types of products and methods of distribution.
> e. Export Control LawsPrincipals who export to Middle Eastern countries should be aware of U.S. anti-boycott regulations which if followed by U.S. principals can lead to U.S. tax penalties. Principals should also be aware that many restrictions exist on the export of technological goods.
> f. Agreement Calendar The principal should track the terms of definite agreements, to insure they are not continued beyond their expiration dates. Agreement calendars also allow principals to monitor the agent's performance.
> g. Investigate RepresentativesMany nations have commercial registers or trade associations which give information about representatives, including judicial actions and other clients, thus alerting the principal to potential problems before they occur.

[26] *See* McNamara, *supra* note 19.

[27] Mcnamara, *supra* note 19.

[28] *Id.*

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should be excluded, based on the unique factors, facts and circumstances of the trade."[29] It might be wise, for example, to opt out of the CISG for the purpose of avoiding an unclear area of CISG law.

The pre-emptive step of including a choice of law clause in a transnational sale of goods might not avoid surprising results when a dispute regarding the transaction arises. "The uncertainty which may arise from the parties' choice of law should also not be overestimated. If the parties have chosen the law of a Contracting State, then it is a matter of interpretation whether they meant the Convention or that state's local sales law."[30]

Let's say American and Canadian merchants enter into a contract that states that U.S. law applies, a court may interpret this clause to mean that the CISG is the law that will govern since the United States is a contracting state to the Convention.[31]

This scenario is seen in the U.S. case of *Asante Technologies, Inc. v. PMC-Sierra, Inc*.[32] The court noted that a clause calling for the application of the California Commercial Code or the Uniform Commercial Code could amount to implied exclusion of the CISG, but held that the two clauses in question, which called for the application of California and British Columbia law respectively, "did not evince a clear intent to opt out of the CISG."[33]

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[29] *Id*.

[30] Prof. Dr. P. Schlechtriem, Uniform Sales Law – The UN-Convention on Contracts for the International Sale of Goods 26 (1986), available at http://www.cisg.law.pace.edu/cisg/biblio/schlechtriem.html.

[31] S. C. Symeonides, *Choice of Law in the American Courts in 2001: Fifteenth Annual Survey,* 50 Am. J. Comp. L. 1, at 36 (2002).

[32] *Asante Techs. v. Pmc-Sierra*, *Inc*., 164 F. Supp. 2d 1142 (U.S. Dist. 2001).

[33] *Id*. *see also* S. C. Symeonides, *Choice of Law in the American Courts in 2001: Fifteenth Annual Survey,* 50 Am. J. Comp. L. 1, at 36 (2002). (Symeonides discusses in detail the intricacies of opting out of the CISG by utilizing the *Asante* case.)

> Asante involved a contract for the sale of goods between a California buyer and a British Columbia seller. The contract consisted of two documents; the buyer's purchase order and the seller's conditions of sale, and each document contained a choice-of-law clause pointing to a different state, California and British Columbia, respectively.
>
> The court concluded that, since both the United States and Canada have ratified the CISG, and since both the buyer and the seller had their principal place of business in a CISG country, the CISG was applicable and, as federal law, the CISG preempted contrary state law in both countries. The court acknowledged that the CISG allows contracting parties to opt out of the Convention, provided they do so expressly and clearly. The court held that neither of the two choice-of-law clauses satisfied this condition. The buyer's California clause was ineffective to displace the CISG because, as preempting federal law, the CISG had become part of California law, which was chosen by the clause, and had superseded any contrary or different California rules. For the same reasons, the same was true of the seller's British Columbia clause because the CISG was part of the chosen law of British Columbia.

Id.

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Merchants may also find themselves contracting with a party whose local law has not adopted the CISG. Therefore, when doing business with buyers or sellers from these countries, merchants may want to specifically opt into the CISG to avoid ambiguity or uncertainty regarding choice of law.[34]

Therefore, whether a merchant wants to include or exclude the CISG, an explicit choice of law clause is the only way to address this issue. If parties want to exclude the CISG, the contract should say so in no uncertain terms. This removes the need for an adjudicator to have to determine the parties' intentions at a later date. (Appendix A to this note contains clauses for contracting parties to utilize to opt out of the application of the CISG in a transnational sales contract).

There is no clear-cut answer to the question: should a client opt-in or opt-out of the Convention. The choice will inevitably be decided on a case-by-case basis.

> Because parties may agree to exclude the Convention altogether, it has occasionally been suggested that attorneys should automatically advise clients to exclude [the] Convention. A moment's reflection upon attorneys' professional responsibility to their clients should suggest that this advice is simplistic. Even if a client has the market power to insist on having U.S. law govern the sales contract, the attorney should know enough about the Convention to determine whether state law . . . or the Convention better protects the client's interests. If a client is unable to dictate the choice-of-law term, the attorney should have a command . . . of the Convention's advantages and disadvantages.[35]

As the case law dealing with transnational sales develops, more guidance and precedent for disputes become available.

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[34] *See* Symeonides, *supra* note 31.

[35] Winship, *supra* note 11.

> To say that the Convention should not be excluded without study does not mean either that an attorney should always advise a client to select the Convention or that the attorney should ignore the uncertainties inherent in a new law. Even proponents of the Convention concede the inevitability of uncertainties and that these uncertainties will persist at least until the development of a large body of case law and the publication of doctrinal commentaries.
>
> This fear of uncertainty, however, is often exaggerated. As more and more countries become parties to the Convention, for example, clients trading in numerous foreign countries may discover that using a single contract form governed by the Convention is more efficient than having to select from among different contract forms governed by different national sales laws.

Id.

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C. Risk of Loss, Incoterms, and Breach of Contract Under the Convention on the International Sale of Goods

I. Risk of Loss – When Does the Risk of Loss Pass From Seller to Buyer?

1. The CISG Approach to Risk of Loss

The issue of who must accept the financial loss for lost or damaged goods has always been, and will always remain, a primary concern to merchants. If a sale is subject to the CISG, the involved merchant and it's counsel would be well served to carefully study the CISG's novel approach to risk of loss.

> In its choice of a model for the rules on the passing of risk, the Convention did not rely on precedence in national legislations or on traditional legal concepts. It refuses to link passing of risk to the conclusion of the contract, to the transfer of property, to the execution of the seller's contractual obligation (delivery), or to payment of the transport cost. The main reason for the lack of such a general rule for the passing of risk seems to be that it would be unable to cope with the practical needs of different types of international contracts involving carriage. Trade terms, as reflected by Incoterms, show that none of the classical systems of linking passing of risk to a certain event has been accepted by the commercial world. Therefore, this Convention does not offer one general criterion for the transfer of risk but rather rules covering different situations: Contracts involving carriage, Contracts involving carriage to a particular place and Sale of goods in transit, and then gives a general residual rule.[36]

The CISG's unique approach to risk of loss is addressed in Chapter 4 of the Convention and Articles 66 through 70 in Chapter 4 can have far-reaching effects on the sale of goods internationally. Following are the text of each Article, a brief description, and how Courts have interpreted risk of loss under these Articles under the CISG.

> **Article 66**: *Loss of or damage to the goods after the risk has passed to the buyer does not discharge him from his obligation to pay the price, unless the loss or damage is due to an act or omission of the seller*.[37]

Under the CISG, risk of loss passes on delivery of the goods.[38] Article 66 establishes the effect of the passage of the risk.[39]

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[36] B. von Hoffmann, *International Sale of Goods: Dubrovnik Lectures, Passing of Risk*, *in* P. Sarcevic & P. Volken (Eds.), International Sales of Goods 285-286 (1986).

[37] CISG, *supra* note 2, Article 66, available at http://cisgw3.law.pace.edu/cisg/text/treaty.html (last visited 4 Feb. 2005).

[38] *See id.*

[39] *See id.*

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> As is similar in most domestic law, when the goods are injured or lost after the risk passed, the buyer is not relieved of the obligation to pay unless the loss or damage is due to an act or omission of the seller, and the buyer cannot require the seller to pay damages for the loss or damage of the goods.[40]

Therefore, loss due to damage or destruction is born by the buyer unless the buyer can prove that the loss was due to the act or omission of the seller.[41]

A Chinese court interpreted Article 66 in a case where goods were placed in storage for the buyer to load. Due to a dispute over price, a second contract extended the loading period. The goods became contaminated during the time extension and the court held that the risk of loss had not passed to buyer and placed the risk of loss on seller.[42]

> **Article 67**: *(1) If the contract of sale involves carriage of the goods and the seller is not bound to hand them over at a particular place, the risk passes to the buyer when the goods are handed over to the first carrier for transmission to the buyer in*

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[40] Schlechtriem, *supra* note 30, at 86.

[41] *See id.*

[42] *Japanese Xinsheng Trade Co. v. Ningxia Hui Autonomous Region Nihong Metallurgic Product Co.*, Ningxia, Hui Autonomous Region Higher People's Court, 27 November 2002, (Translation by Wu Dong).

> The present Court holds that this case arose from a sales contract which reflected the true minds of the two parties and did not violate the CISG or Chinese laws so that it was valid. When delivering the second installment of goods (120 tons of corundum) under Contract No. 98NSN-1101, [Buyer] was in delay of loading due to the price dispute and this caused the goods had to be stored at the port for a long time. To settle the dispute in respect of the aforesaid 120 tons of goods, the two parties entered into Contract No. 99NSN-11-1 and altered the loading period to November/ December 1999. The Court holds that, this was a modification of the former contract by the two parties and should be implemented. When fulfilling the second contract, the two parties went to the port to change the packages and check the goods, when they found the goods were polluted by breeze and water. Three days before that, the Bayuquan Entry-Exit Inspection and Quarantine Bureau had inspecting personnel take samples from the goods and do inspection, who issued an inspection report claiming that they conformed to the requirements of the No. 99NSN-11-1 Contract. However, the Bureau did not provide a reasonable explanation for the pollution by breeze and water and the inspection conclusion could not negate the fact that the goods had been polluted. Therefore, the inspection report could not be regarded as proof that the goods conformed to the quality requirements of the contract. As neither party could provide evidence to prove the origins of the pollution, according to the CISG and Incoterms 2000, the risks of the goods should be transferred to [Buyer] when they cross the ship's rail because FOB was the price term used in the contract. In addition, before loading, the two parties agreed to modify the contract and alter the loading period of the goods, which reflected the true minds of the parties and should be implemented. So, the risk of losses had not yet passed to [Buyer] and [Seller] did not take care of the goods in the proper manner before loading. Therefore, [Seller] should bear all the risks of the goods; its claims and accounts lack support by facts or laws and so could not be supported by the Court. [Buyer]'s appeal and accounts conform to the relevant stipulations of the CISG and Incoterms 2000, so that is supported by the Court.

Id. Case abstract available at http://cisgw3.law.pace.edu/cases/021127c1.html.

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> *accordance with the contract of sale. If the seller is bound to hand the goods over to a carrier at a particular place, the risk does not pass to the buyer until the goods are handed over to the carrier at that place. The fact that the seller is authorized to retain documents controlling the disposition of the goods does not affect the passage of the risk. (2) Nevertheless, the risk does not pass to the buyer until the goods are clearly identified to the contract, whether by markings on the goods, by shipping documents, by notice given to the buyer or otherwise.*[43]

Dovetailing with Art. 67, Art. 32(2) of the CISG further elaborates: "If the seller is bound to arrange for carriage of goods, he must make such contracts as are necessary for carriage to the place fixed by means of transport appropriate in the circumstances and according to the usual terms for such transportation."[44] This clause does not specify under which circumstances the seller is bound to arrange for carriage of the goods. If a contract involves the seller in the carriage of goods and the contract does not provide for a specific way of sending the goods, it is most likely up to the seller to arrange for carriage of the goods according to the terms provided for in Art. 32(2).[45] Such an obligation, however, does not bind the seller to arrange for insurance.[46] Although it remains up to the buyer to effect insurance; the seller is obligated to provide the information necessary for conclusion of the insurance contract.[47] Insurance is discussed in more detail in section IV, infra.

It is prudent to assume that "the obligation to deliver the goods at a particular place is the exception, to which the parties must specifically agree."[48] In the case of silence within the contract, the question arises whether or not the seller has to hand the goods over to the first carrier or whether he only is obliged to place the goods at the buyer's disposal at his own place of business.[49] The following is an abstract of a German case and sheds light on how a German Court interpreted CISG Article 67.

> In [this] case, the sellers were located in Austria and customarily placed manufactured furniture in a warehouse in Hungary and then sent invoices to the buyer. According to a series of contracts governing various partial deliveries of furniture, the buyer was to take possession of the goods at the manufacturing works and load the furniture into railway wagons or trucks. The buyer would pay the sellers based on the delivery invoices after taking delivery of the furniture. However, no delivery was taken; the manufacturer went bankrupt, the warehouse closed, and the furniture disappeared. Seller sued for the purchase price, which was denied on the ground that delivery had not occurred […]. The delivery was due at buyer's demand, which had not been made, and the sellers had failed to place the furniture at the buyer's disposal. Thus, the buyer's obligation to pay did not arise and the risk of loss of the goods did not pass to the buyer.[50]

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43 CISG, *supra* note 2, Article 67 available at http://cisgw3.law.pace.edu/cisg/text/treaty.html (last visited Feb. 4, 2005).

44 *See id.,* Article 32(2).

45 *See id.*

46 CISG, *supra* note 2, Article 32(3).

47 *See* von Hoffmann, *supra* note 37.

48 *Id.,* at 284.

49 *See* von Hoffmann, *supra* note 37.

50 L. A. DiMatteo *et al.*, *The Interpretive Turn in International Sales Law: An Analysis of Fifteen*

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> **Article 68**: *The risk in respect of goods sold in transit passes to the buyer from the time of the conclusion of the contract. However, if the circumstances so indicate, the risk is assumed by the buyer from the time the goods were handed over to the carrier who issued the documents embodying the contract of carriage. Nevertheless, if at the time of the conclusion of the contract of sale the seller knew or ought to have known that the goods had been lost or damaged and did not disclose this to the buyer, the loss or damage is at the risk of the seller.*[51]

The general rule is that the buyer bears the risk of loss from the time of the hand over to the first carrier.[52] When goods are sold in transit, the hand over to the first carrier is performed before the contract between the seller and the buyer is completed.[53] This leads to the question of whether or not the buyer has to bear the transit risk even for the time before conclusion of the contract.[54] "The alternative would be to make the risk pass only from the time of conclusion of the sales contract. The practical inconvenience of this latter solution is that it is very difficult to determine when damage occurred to the goods in transit."[55] Such a rule leads to disputes. The buyer is almost always in a better position to inspect goods, preserve any salvageable goods and to submit claims to the insurance carrier when loss occurs.[56] "It seems that there has been an international trade usage, […] which makes risk pass retroactively to the buyer for the whole sea transport."[57]

Looking again to the German case referred to in the previous section,

> [the] [c]ourt held that the provisions for the transfer of risk favored the [buyer]. Under Art. 68 CISG, the risk of goods sold passed at the time of the handing over of the goods to the buyer. However, [buyer] had not taken delivery of the furniture. [Buyer] had objected to [plaintiff's] submission that the furniture had been stored in a warehouse administered and paid for by the [buyer]. [Buyer] had submitted in detail that the furniture had been stored in the manufacturing works which she did not have access to. This corresponded to the contractual agreement that [seller] or the manufacturer was to load the goods.
>
> The Court also held that the risk had not passed due to a default in taking delivery on the part of the [buyer]. [Plaintiff] did not submit that the parties had agreed that [buyer] would take delivery of the furniture at a precise point in time and that [buyer] had violated such an agreement. The submission that the witness A. had informed [buyer] following a fire damage in the year 1995 that the storage occurred at [buyer's] risk did not lead the Court to conclude that an agreement on the passing of risk had been formed. Since the furniture had been stored at the end of 1993 or the beginning of 1994, an event in the year 1995 could not have motivated the

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Years of CISG Jurisprudence, 34 N.W. J. Int'l L. & Bus. 299, 388 (2004). (The case being discussed is OLG Hamm 19 U 127/97, Jun. 23, 1998 (F.R.G.)), available at http://cisgw3.law.pace.edu/cases/980623g1.html. German cases do not list party names.)

51 CISG, *supra* note 2, Article 68, available at http://cisgw3.law.pace.edu/cisg/text/treaty.html.

52 *See* Von Hoffman, *supra* note 36, at 292.

53 *See id.*

54 *See id,* at 293.

55 *Id.*

56 *See id.*

57 *Id.*

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> witness to talk about the loss of risk at the time of storage. Moreover, [plaintiff] did not claim that [buyer] had agreed to such a transfer of risk. A comment by one party alone could not serve to change the rules for the passing of risk under the CISG.[58]

> **Article 69**: *(1) In cases not within articles 67 and 68, the risk passes to the buyer when he takes over the goods or, if he does not do so in due time, from the time when the goods are placed at his disposal and he commits a breach of contract by failing to take delivery. (2) However, if the buyer is bound to take over the goods at a place other than a place of business of the seller, the risk passes when delivery is due and the buyer is aware of the fact that the goods are placed at his disposal at that place. (3) If the contract relates to goods not then identified, the goods are considered not to be placed at the disposal of the buyer until they are clearly identified to the contract.*[59]

The characteristic feature of international sales transactions is that they involve carriage obligations of both the seller and buyer.[60] It is rare for a buyer to assume total liability for transport from the inception of the contract, to the end.[61] Art. 69(1) addresses the passing of risk of loss in sales not involving carriage by the seller. "The principle is that risk passes from the seller to the buyer at the time the buyer takes over the goods at the seller's place of business. Therefore, the risk remains with the seller during the time period the buyer is permitted but not contractually bound to take over the goods."[62] The reason behind this rule is identical to the reasoning discussed previously for risk passing to the buyer once goods have been given to the first carrier in contracts involving transport by the seller: the seller maintains possession of the goods and is best able to protect said goods from damage or destruction.

A rule that places liability on the buyer as soon as the goods are made available to the buyer is overly harsh and unfair to the buyer. This is not to say that the risk remains indefinitely with the seller, for the buyer is required to pick up the goods within a reasonable time.[63]

> On the whole, the underlying policy of the CISG for risk allocation in contracts involving carriage is the following: In export sales, goods are normally insured against transportation risks. Therefore, the main question concerning risk allocation is whether it is easier for the seller or the buyer to claim compensation for loss and damage from the insurance company. The practical consideration after goods have been sent to the buyer is that only the buyer can discover transit damage. The consequence is to let the buyer suffer the loss, thus keeping the seller out of the dealings with the insurance company. The other way around, letting the seller suffer the loss would make the transaction with the insurance company more difficult: First the seller has to be informed of the damage by the buyer and then recover

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58 Oberlandesgericht Hamm 23 June 1998 (Translation by Ruth M. Janal Translation; edited by Camilla Baasch Andersen), available at http://cisgw3.law.pace.edu/cases/980623g1.html#cx.

59 CISG, *supra* note 1, Article 69, available at http://cisgw3.law.pace.edu/cisg/text/treaty.html (last visited 4 Feb. 2005).

60 *See* Von Hoffman, *supra* note 36, at 294.

61 *See* Von Hoffman, *supra* note 36, at 294-295.

62 *Id.*, at 295.

63 *See* Von Hoffman, *supra* note 36, at 294-295.

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> the damage from the insurance company. The risk of loss allocation has therefore become a question of balancing the respective inconveniences of buyer and seller. Such a model of risk allocation is unfamiliar to national systems.[64]

The following is an abstract from a Dutch case dealing with Article 69:

> [A] dryer was to be delivered by truck to Wiesenbad, Germany, a few kilometers from the field where B intended to use the machine. Upon arrival of the truck in Wiesenbad, the driver (an employee of S) requested B to help unload the dryer. After B's personnel, using their own tractor and chain, had successfully lifted the dryer down from the truck and then driven a few meters, the chain holding the dryer broke, causing substantial damage to it.
> Making a general reference to CISG "Article 69", the court in Randers found it "natural" to *interpret the contract* between the parties to mean that *delivery* of the dryer took place "at the latest" when B "took possession" of it, i.e., when the dryer was *unloaded* from the truck by B's personnel. For this reason, and since the court found that the accident was not attributable to S (or its personnel), the court held B liable to S for the agreed price.[65]

> Article 69(2): If a seller is not to deliver the goods at his place of business but rather at another place, including – as in a sale to destination – at the buyer's place of business, the risk passes to the buyer at the earliest moment when the buyer could have taken delivery. Where delivery is to be made at a place which is not the buyer's place of business, such as in the case of warehoused goods, risk passes only when delivery is due and the buyer is in a position to pick up the goods and aware that the goods have been placed at his disposal. Where the buyer does not know - for example, from receipt of a warehouse document or a notice of release, etc. – that and where the goods are available, the risk does not pass until the buyer has been notified (Article 67(2)).[66]

An important point is that risk of loss does not pass to the buyer until the goods are clearly identified in the contract.[67] "Identification can be demonstrated by markings on the goods, shipping documents, notice to the buyer, or other appropriate means."[68]

2. Practical Advice

The Convention's basic rule is that risk passes when the seller hands over the goods to the first carrier. Buyer's might attempt to modify this rule by incorporating out-turn clauses into their contracts. "Generally employed in the oil trade, the clauses make the buyer responsible for only the goods that he actually receives at the end

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64 *Id.*, at 297-298.
65 J. Lookofsky & R. Franz*, Comments on Issues Relating to the Passing of Risk December 2004,* Henschel Randers County Court, Denmark BS 2-2229/2002 decided 8 July 2004, available at http://www.cisg.law.pace.edu/cisg/biblio/lookofsky10.html.
66 Schlechtriem, *supra* note 30, at 90.
67 *See* DiMatteo et al., *supra* note 50, at 407.
68 *Id.*

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of the line."[69] Make certain your merchant understands the potentially adverse ramifications of this modification to the basic rule prior to agreeing to contracts containing out-turn clauses.[70]

The CISG provisions relating to passage of risk have a limited practical utility.[71] "[W]here the parties have agreed no trade terms at all, the regulation under the CISG will apply. But these cases are rare."[72] What does this mean to practitioners? A court uses the CISG's risk of loss sections out of necessity in cases where parties fail to use well-defined, familiar trade terms (such as INCOTERMS). The next section discusses, in part, INCOTERMS and their prevalence in apportioning risk of loss. Trade terms more often define risk of loss, even within the CISG.

A practitioner should also know how the CISG deals with ownership of the goods being sold in a transnational transaction. Pursuant to the CISG, "the risk passes without taking into account who owns the goods. The passing of ownership is not regulated by the CISG according to art. 4(b)."[73] Article 4(b) provides that the Convention is not concerned with "the effect which the contract may have on the property in the goods sold."[74] Moreover, according to Article 67(1), the passage of risk and transfer of title need not occur at the same time, as the seller's retention of "documents controlling the disposition of the goods does not affect the passage of risk."[75]

II. Trade Usage and Incoterms

The seller and buyer may, and often do, agree on when the risk of loss or damage passes to the buyer.[76] Pursuant to article 6 of the CISG, the parties' agreement will govern even if it derogates from the provisions of chapter 4 of the CISG that would otherwise apply.[77] Further, Article 9(1) provides that parties are bound by any practices, including those allocating risk of loss or damage that they have established between themselves.[78]

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[69] N. G. Oberman, *Transfer of risk from seller to buyer in international commercial contracts: A comparative analysis of risk allocation under the CISG, UCC and Incoterms*, available at http://www.cisg.law.pace.edu/cisg/thesis/Oberman.html (last visited 4 February 2005).

[70] *Id.*

[71] *See* DiMatteo et al., *supra* note 50.

[72] *Id.*

[73] A. Romein, The Passing of Risk. A Comparison Between the Passing of Risk under the CISG and German Law (1999).

[74] CISG, *supra* note 2, Article 4(2).

[75] CISG, Article 67(1). *St. Paul Guardian Insurance Company v. Neuromed Medical Systems & Support*. Available at http://www.unilex.info/case.cfm?pid=1&do=case&id=730&step=FullText.

[76] *See generally* CISG, *supra* note 2, Article 1.

[77] *UNCITRAL Digest of case law on the United Nations Convention on the International Sale of Goods*, at 3, available at http://cisgw3.law.pace.edu/cisg/text/anno-art-01.html#ucd (last visited Feb.4, 2005).

[78] CISG, available at http://cisgw3.law.pace.edu/cisg/text/treaty.html (last visited Feb. 4, 2005).

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It is rare when a contract does not at least attempt to identify when risk of loss passes from seller to buyer. Parties will frequently do so by expressly incorporating trade terms into their agreement, such as the International Chamber of Commerce's Incoterms.[79]

> Buyer and seller may agree to vary a standard trade term, adopt a trade term that is local, or use a trade term in connection with the price rather than delivery. The parties may also agree to the allocation of risk in the standard terms or general business conditions of the seller or buyer.[80]

Contracting parties are bound by any usage of which they knew or ought to have known, and which in International law is widely known to, and regularly observed by, parties to similar contracts in he particular trade.[81] Article 8(3) instructs those adjudicating claims under the CISG to determine the parties' intent by looking at relevant circumstances, including any "usages".[82]

Commercial parties, unable to specify every contingency with precision, can reduce transaction costs by incorporating default rules into their contracts; "total contracting costs are minimized to the extent that those defaults reflect risk allocations that most parties would have adopted had they negotiated explicitly about the term. At the same time, defaults can reduce errors in expression and interpretation attributable to more highly tailored contract terms."[83]

Courts have occasionally looked to the prior practices of the parties for evidence of the parties' intent with respect to risk of loss. One court has concluded, however, that one party's conduct with respect to risk on two prior occasions is insufficient to establish a binding practice.[84] A similar ruling was handed down in a German Court.

> [That] Court found that the buyer had no right to a credit due to a practice established between the parties according to Art. 9 CISG, because the granting of a credit on only two occasions during a longer business relationship did not suffice to establish a practice. According to the Court, Art. 9 requires a behavior that is regularly observed and therefore of a certain duration and frequency relating to the length of the business transaction involved.[85]

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[79] International Commercial Terms [hereinafter Incoterms] available at http://www.iccwbo.org/index_incoterms.asp (last visited Feb. 4, 2005). Incoterms are a set of uniform rules codifying the interpretation of delivery trade terms defining the rights and obligations of the exporter and importer in an international transaction. Examples include CIF, FOB, FAS, CFR, etc. *Id.*

[80] *The UNCITRAL Digest of case law on the United Nations Convention on the International Sale of Goods A/CN.9/SER.C/DIGEST/CISG/66* (8 June 2004) [hereinafter Uncitral], available at http://www.cisg.law.pace.edu/cisg/text/anno-art-66.html.

[81] CISG, *supra* note 2, Article 9.

[82] C. P. Gillette, *The Empirical and Theoretical Underpinnings of the Law Merchant: The Law Merchant in the Modern Age: Institutional Design and International Usages under the CISG*, 5 Chi. J. Int'l L. 157, at 168 (2004).

[83] C. P. Gillette, *Harmony and Stasis in Trade Usages for International Sales*, 39 Va. J. Int'l L. 707 (1999).

[84] *Id.*, at 708.

[85] Amtsgericht Duisburg Court, Case Number 49 C 502/00 available at http://www.unilex.info/case.cfm?pid=1&do=case&id=715&step=Abstract (German case citations do not identify parties to proceedings) (last visited 7 March 2005).

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The seller and buyer may also be bound by trade usages with respect to risk of loss or damage. Under Article 9(1), they are bound if they agree to a usage, whether international or local.[86] They are also bound under article 9(2) by widely observed international usages which they know or should know unless they agree otherwise.[87] "If the parties expressly incorporate an Incoterm into their contract paragraph (1) of Article 9 makes the term binding, but the Incoterm is so widely-used courts will enforce an Incoterm even absent express incorporation."[88]

Article 8(3) notes that in determining the parties' intent, due consideration is to be given to "usage."[89] Article 9 (2) states that the parties are bound by "a usage […] which in International trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned."[90] "The conservative view holds that a trade usage must have a distinct international character to be considered while the liberal view allows for the admission of local trade usage."[91] A U.S. court in *St. Paul Insurance Co. v. Neuromed Medical Systems* implied Incoterms Into the CISG through Article 9(2).[92]

> The potential use and misuse of trade usage was also demonstrated in a Swiss court decision. The court used Articles 9(1) (inter-party usage) and 9(2) (international trade usage) to recognize the binding nature of a written confirmation. It creatively argued that the parties "knew or ought to have known the binding nature of such confirmations under both Austrian and Swiss law." The court asserted that due to that knowledge, and that there was no other practice prevailing in the particular trade, the binding nature of a confirmation was a usage under both Articles 9(1) and 9(2). Although, the court was correct in recognizing the binding nature of confirmations as a general trade usage, it is a dangerous precedent to use domestic law as a vehicle in establishing an international trade usage.
>
> The above case and a decision of an Austrian court illustrate how the problem of homeward trend can present itself in various ways. These cases demonstrate that homeward trend bias can influence the recognition of trade usage. An Austrian court held that Article 9(2) "could not be interpreted as barring the application of national or local usage in interpreting a contract." This is a contradiction of Article 9(2)'s requirement that any such usage be widely known in international trade. The court's decision is reconcilable with the express mandate in Article 9(2) given the court's emphasis on the fact that the seller had done business in the country of the local usage for many years and, thus, could not have been unaware of the usage. Instead of declaring national and local usages to be generally applicable, the court should have crafted an exception based upon the facts of the case. In short, a more specific default rule would have made local usage available to the court if the adverse party knew of its existence and knew there was no conflicting international usage.[93]

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86 CISG, available at http://cisgw3.law.pace.edu/cisg/text/treaty.html.
87 *Id.*
88 Chia-Jui Cheng, Clive M Schmitthoffs Select Essays on International Trade Law (1988).
89 CISG, available at http://cisgw3.law.pace.edu/cisg/text/treaty.html (last visited 4 Feb. 2005).
90 DiMatteo*, supra* note 51, at 432.
91 *Id.*
92 *See id.*
93 *Id.*, at 433-434.

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1. Incoterms[94]

> Because of the long standing practice of standardized shipping terms to denote the extent of the parties' contractual obligations under the agreement as well as denoting the allocation of risk of loss between the parties, lawyers engaged in international commercial transactions need to have a ready familiarity with standardized shipping terms. The common international practice of utilizing the Incoterms, either expressly or by implication, in the international sale of goods makes a knowledge of these terms essential for the international commercial practitioner.[95]

The most straightforward method used today in international trade to determine the point at which risk of loss switches from seller to buyer is the usage of Incoterms. (See Appendix B for a list of Incoterms.)

> Each INCOTERM is a three letter acronym related to where the seller's responsibility ends. They should be written into the purchasing or shipping contracts. Some incoterms require the changeover point to be named. As well as buyer and sellers there are "carriers". They are the people who have a contract to transport the goods by land, sea, air or a combination of modes. A seller will be given a bill of lading, way bill or carrier's receipt, that document can be used to prove that the goods have been taken on by the carrier.[96]

The CISG does not contain definitions of delivery terms.[97] Incoterms specify important variations and details that are not covered by the CISG. Therefore, parties contracting under the CISG, continue to have Incoterms address passage of risk and the delivery conditions. In addition, if merchants do not want Incoterms to apply, it is prudent to exclude them.[98] Two U.S. courts have ruled that Incoterms are incorporated through Article 9(2).[99]

One may conclude that risk allocation under the Incoterms is practical as it provides specific moments in time when risk passes from seller to buyer.[100] "These terms apportion risk allocation in advance and allow the respective parties to understand their responsibilities and obligations."[101] The advent of the CISG

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[94] "Incoterms are standard trade definitions most commonly used in international sales contracts. Devised and published by the International Chamber of Commerce, they are at the heart of world trade." Incoterms 2000, available at http://www.iccwbo.org/incoterms/understanding.asp (last visited 7 March 2005).

[95] H. Gabriel, *The International Chamber of Commerce INCOTERMS 1990 – A Guide to their Usage*, 3 Vindobona J. Int'l Comm. L. & Arb. 61, at 70 (1999).

[96] Incoterms available at http://learning.unl.ac.uk/int_purchasing/Incoterms/ (last visited 3 March 2005).

[97] *See generally* CISG, *supra* note 2.

[98] *See generally* Prof. Dr. B. Piltz, *INCOTERMS and the UN Convention on Contracts for the International Sale of Goods*, Online Library: CISG 20 Years (n.d.), available at http://www.20jahre.cisg-library.org/piltz1.html (last visited 8 March 2005).

[99] *See BP Oil Int'l v. Empresa Estatal Petroleos de Ecuador*, 332 F.3d 333 (5th Cir. 2003), and *St. Paul Guardian Ins. Co. v. Neuromed Medical Sys. & Support*, 53 Fed. Appx. 173 (2d Cir. N.Y. 2002).

[100] *See* Oberman, *supra* note 69.

[101] *Id.*

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should not lessen reliance on Incoterms. In a commentary on the Convention Relating to a Uniform Law on the International Sale of Goods (ULIS)[102], an antecedent to the CISG, André Tunc states:

> [The Uniform] Law contains no reference to the principal forms of maritime or land sales (f.o.b., c.i.f., etc.). The draftsmen of the Law considered that this was a matter which was not yet properly ready for unification by means of international convention. To have made provision for the principal forms of sale would, in the first place, have meant doubling the volume of a Law which was already long. Moreover, the rules applicable to the principal forms of sale are still varied and doubtful. It may be said that it is precisely in a situation of this kind that unification is useful. It, however, appears that in this field a process of convergence and unification by persuasion, basically the task undertaken by the International Chamber of Commerce, may be more beneficial to commerce, through the gradual and progressive character of the convergence which it brings about, than an immediate unification by way of international convention. In short, the draftsmen of the Uniform Law felt that the rules governing the principal forms of sale where still changing, constantly adapting themselves to practical needs, and that it was not proper to halt a process probably beneficial to commerce. Of course the Uniform Law can be revised. This revision will, however, require the operation of a rather clumsy procedure. In consequence, it seemed from every point of view that the International chamber of Commerce would play a more useful part in this field than a commission or Conference for Unification and that it was better suited to this role.[103]

2. Burden of Proof for Risk of Loss.

Article 36 fixes the point at which the seller's obligations pertaining to the conformity of goods expires; when the risk of loss passes to the buyer or at the expiration of any express or implied guaranty.[104] The buyer is allocated the burden of proving that the goods were defective prior to the expiration of the seller's obligation point.[105] This was the issue in a German case involving the sale of meat products.[106]

> Upon receipt, the buyer objected to the quality of the meat and sued for a refund. The court reasoned that since the parties had not agreed otherwise, the risk of loss had passed to the buyer when the seller handed over the goods to the first carrier. Therefore, under CISG Articles 36 and 66, the buyer had the burden of proving that the goods did not conform to the contract at the time the risk of loss passed. This burden, demonstrated here, is often difficult to sustain.[107]

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[102] "The antecedents to the CISG are the Convention relating to a Uniform Law on the Formation of Contracts for the International Sale of Goods (ULF) and the Convention relating to a Uniform Law on the International Sale of Goods (ULIS) done at The Hague on 1 July 1964." *Antecedents to the CISG*, available at http://www.cisg.law.pace.edu/cisg/text/antecedents.html.

[103] CISG, *supra* note 2, available at http://www.cisg.law.pace.edu/cisg/text/passage.html (last visited 4 Feb. 2005).

[104] *Id.,* Article 36 available at http://cisgw3.law.pace.edu/cisg/text/e-text-36.html (last visited 4 Feb. 2005).

[105] *See* DiMatteo, *supra* note 50, at 399.

[106] *Id.*

[107] DiMatteo, *supra* note 50, at 399-400.

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Without a specific Incoterm, the buyer in this case was required to accept the court's interpretation of the CISG and its provisions for risk of loss. It is also important to note that not all trade terms address the issue of risk of loss or damage.[108]

> Most national courts interpret the place of delivery under Article 31 as the place of performance of delivery for purposes of determining jurisdiction where the CISG governs the place of delivery. In a 1998 case, the French Court of Appeals in Paris addressed a situation in which the buyer, a French company, ordered winter clothing from a German seller. The goods were subject to a contract specifying the INCOTERM "ex works," which the French court determined to be the defendant's principal place of business in Germany. It declined jurisdiction in favor of the courts of Germany. Where the parties have not specified a place for delivery, French courts have, consistent with Article 31(a), identified the place of delivery to be the place where the goods were handed over to the first carrier for transmission to the buyer. In these cases, the French courts have observed that the place of performance of the obligation to deliver goods and the place of performance of the obligation to deliver conforming goods must be the same.[109]

In *B.P. Oil Int'l, Ltd. v. Empresa Estatal Petroleos De Ecuador*, the buyer refused to accept delivery claiming that the goods did not conform to the contract.[110] The contract provided that the goods were to be delivered "CFR"[111] and undergo a pre-shipment inspection for conformity.[112] Applying the CISG, the court held "that the goods should have been tested for conformity before risk of loss passed to the buyer at the port of shipment. The court also stated that the general principle in the event of subsequent damage or loss was that the buyer must first seek a remedy against the carrier or insurer."[113]

Determination of the place of delivery under Article 31 is relevant to the buyer's obligation to pay and to the passing of the risk of loss under CISG Articles 67-69.[114]

The burden of proof in establishing the passage of risk is an issue that has lead to disputes between buyer and seller.[115] "Article 66 and the other provisions of chapter 4 are silent on who has the burden of establishing that the risk of loss or damage has passed to the buyer."[116] One view is that the burden is on the party

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[108] Uncitral, *supra* note 80. *See, e.g.*, *CLOUT case No. 247* (Audiencia Provincial de Córdoba Spain 31 October 1997) ("CFFO" allocates cost of shipment to the destination, but has no relevance to passing of risk). CLOUT (Case Law on Uncitral Text) is a systematic collection and distribution mechanism for information on court decisions and arbitral awards relating to the Conventions and Model Laws that emanated from the work of the Commission and can be accessed directly at http://unvx01.unov.org/english/clout/.

[109] DiMatteo, *supra* note 50, at 387-388.

[110] *BP Oil Int'l v. Empresa Estatal Petroleos de Ecuador*, 332 F.3d 333 (5th Cir. 2003).

[111] CFR – Cost and Freight – Title, risk and insurance cost pass to buyer when delivered on board the ship by seller who pays the transportation cost to the destination port. Used for sea or inland waterway transportation. http://www.ltdmgmt.com/incoterms.htm.

[112] *See* BP Oil Int'l, *supra* note 110.

[113] *See* DiMatteo, *supra* note 50, at 409.

[114] CISG, *supra* note 2, Articles 67 through 69.

[115] Uncitral, *supra* note 80.

[116] *Id.*

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that argues that the risk has passed.[117] "The issue of who bears the risk arises, however, in the context of actions to enforce obligations of the seller (to deliver conforming goods) or buyer (to pay for the goods) under other provisions of the Convention."[118]

The burden is often on the seller when the seller brings an action to recover the price in accordance with article 62.[119] Buyers will not be faced with liability in the event the seller is unable to prove that the goods were delivered.[120] Two German courts held "that a bill of lading that accurately described the goods sold but did not indicate the name of buyer as recipient was insufficient proof "[121] and "that a stamped but unsigned receipt was not sufficient proof of delivery at the buyer's place of business as required by the contract […]."[122]

When a dispute occurs over "whether damage occurred before or after the risk of loss passed to the buyer, the buyer has the burden of establishing that the damage occurred before the risk of loss passed to it."[123] "Thus, where a seller produced a bill of lading with the master's annotation "clean on board" and the buyer produced no evidence that deterioration occurred before the seller handed over the goods to the carrier, the buyer bore the risk of deterioration."[124]

Merchants should always use Incoterms in contracts involving carriage of goods in international sales.[125] This is the only way to insure that both parties understand their respective obligations. Merchants should also define when risk of loss passes because the CISG will not. Other issues that should be addressed in the contract between seller and buyer include conformity of goods, place of delivery, burden of proof and contract termination following passage of risk of loss to buyer. In addition, a clause specifically taking Article 8(3) and 9(2) of the CISG out of the contract adds certainty to the contract by insuring that trade usages that were not intended are not interpreted as applicable.[126]

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[117] *Id. See CLOUT case No. 338* [Oberlandesgericht Hamm Germany 23 June 1998]. (The court found that the buyer was not obliged to pay the purchase price according to article 66 CISG, because the plaintiff did not prove that the goods were lost after the risk had passed to the buyer.). Available at http://www.cisg.law.pace.edu/cases/980623g1.html#ua.

[118] Uncitral, *supra* note 80.

[119] *See id.* "The seller may require the buyer to pay the price, take delivery or perform his other obligations, unless the seller has resorted to a remedy which is inconsistent with this requirement." CISG, *supra* note 2, Article 62.

[120] *See* Uncitral, *supra* note 80.

[121] *CLOUT case No. 283* (Oberlandesgericht Köln Germany 9 July 1997). (The court held that there was no obligation for the buyer to pay the price under articles 66 and 67(1) where seller did not establish delivery to first carrier) available at http://cisgw3.law.pace.edu/cases/970709g3.html.

[122] Uncitral, *supra* note 80.

[123] *Id.*

[124] *Id.*

[125] J. P. McMahon , *Guide for Managers and Counsel Drafting CISG Contracts and Documents and Compliance Tips for Traders*, January 2004, available at http://www.cisg.law.pace.edu/cisg/contracts.html#a9.

[126] *Id.*

> Under Article 9, the parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely

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III. Breach of Contract

Fundamental breach is an original concept devised during the drafting of the CISG.[127] Much like the risk of loss sections, fundamental breach differs from all other similar concepts in contemporary domestic laws.[128] According to the CISG, breach is fundamental when it results in "such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract."[129] This is subject to the following limitation: "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."[130]

"Art. 69(1) makes risk pass to the buyer if he does not take over the goods in due time."[131] After a reasonable time has passed, the buyer is in breach of contract "by failing to take delivery when the goods are placed at his disposal."[132] Goods are placed at the disposal of the buyer when the goods have been identified to the contract.[133] "Art. 69(1) does not expressly cover the situation in which a breach of

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> known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned. Article 8(3) requires consideration of usages to determine intent or the understanding a reasonable person would have had. When there is a dispute, parties tend to discover trade usages and "experts" who will vouch for their existence, as the need arises.

Id. The following clauses are examples that may be included in a contract to avoid this uncertainty.

> Article 8(3) and Article 9 (2) of the Convention on Contracts for the International Sale of Goods do not apply to this Contract. The parties have not agreed to any usage or made any usage applicable to their contract. Practices which the parties have established between themselves and course of performance shall not be considered in determining their understanding, their intent or their rights and obligations.

Id.

> Article 8(3) and Article 9 (2) of the Convention on Contracts for the International Sale of Goods do not apply to this Contract. The parties have not agreed to any usage or made any usage applicable to their contract. When the terms stated in this document are unclear, evidence of practices which the parties have established between themselves may be considered in determining their understanding, their intent or their rights and obligations.

Id.

[127] Wu Dong, *The Effect of Fundamental Breach on Passage of Risk in the International Sale of Goods under the United Nations Convention on Contracts for the International Sale of Goods: Comparative analysis with the Contract Law of the People's Republic of China*, 7 Vindobona J. Int'l Comm. L. & Arb. 233 (2003), available at http://cisgw3.law.pace.edu/cisg/biblio/dong.html.

[128] *Id.* "[F]undamental breach is not fraught with history. It is a fresh legal concept, born from compromise and – for better or worse – open to interpretation, when it comes to applying the two tests: substantial detriment and unforeseeability." *Id.* (citing Michael Will, in Bianca-Bonell Commentary on the International Sales Law 1984).

[129] CISG, *supra* note 2, Article 25.

[130] Wu Dong, *supra* note 127.

[131] Von Hoffman, *supra* note 36, at 295.

[132] *Id.*

[133] *See id.*

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contract by the buyer does not consist of a refusal to take delivery but of a refusal to do other acts that according to the contract have to be done by the buyer prior to delivery."[134]

> A typical case of such a breach of contract may occur when the buyer is bound to make payment on delivery but refuses to do so. In this situation, the buyer does not fail to take delivery, but it is the unpaid seller who refuses to deliver to the buyer.[135]

Article 25 of the CISG defines a fundamental breach.[136] This leads us to Article 70, which sets out how a fundamental breach affects risk of loss.[137]

"Courts and arbitral decisions have focused on three types of breaches as potentially fundamental – late delivery, deficiencies in the goods, and failure to uphold specific contractual terms."[138] An example or an implied general principle underlying the focus of the CISG is "the principle of favoring the continuation of a contract."[139] The fact that goods can only be rejected for fundamental defects requires buyer to accept defective goods in most instances, thus furthering this principle.

> The importance of completing the transaction in long distance sales, as compared to the broad right of rejection under the perfect tender rule for domestic sales, limits the right of avoidance under the CISG. This is somewhat offset by the incorporation of a uniquely non-common law remedy of price reduction. Thus, the buyer is forced to complete the transaction but is allowed to unilaterally reduce the price by the diminishment of value related to the defect.[140]

> **Article 70**: *If the seller has committed a fundamental breach of contract, articles 67, 68 and 69 do not impair the remedies available to the buyer on account of the breach.*[141]

Risk will stay with the seller or transfer to the buyer based upon the actions taken by buyer once the seller is in breach of the contract.[142] "If the buyer refuses to take over the goods or rejects the goods, the risk reverts to the seller retroactively, meanwhile, the buyer must preserve the goods before the seller takes charge of them."[143] "If the buyer accepts the goods ultimately (i.e., the buyer reduces the price, requires repair or claims damages), the risk is borne by the buyer."[144] A breach by seller can also result in risk being applied retroactively to the seller

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134 *Id.*
135 *Id.*
136 *See generally* DiMatteo, *supra* note 50.
137 *Id.*
138 *Id*,. at 411.
139 *Id.*, at 316.
140 *Id.*, at 315. "The principle [of continuation of performance] can be extracted from Articles 34, 37, 48,49, 51, 64, 71 and 72 of the CISG." *Id.*
141 CISG, *supra* note 2, Article 70.
142 Wu Dong, *supra* note 127.
143 *Id.*
144 *Id.*

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"provided that the buyer may still declare the contract avoided after an additional period time for the seller to cure."[145]

Alternatively, the buyer may be in breach for failure to take delivery in a reasonable amount of time.[146] When this happens, "the risk passes to the buyer as of the time the buyer is in breach."[147]

"Damages pursuant to breach of contract are often limited by contract to avoid surprise; however, both national and local laws of the contracting parties may impose restrictions on liquidated damages clauses and knowledge of these laws in addition to the CISG will protect merchants from incurring unnecessary liability."[148]

D. Insurance, Insolvency/Nonpayment

I. Insurance

As specifically discussed above, the CISG deals with risk of loss in a unique manner. The determination of which party bears the risk of loss under the CISG is a much more difficult matter than determining which of the contracting parties' insurance provider(s) will have to cover the loss under the CISG. Under the CISG, the party's insurance provider must cover the loss if that party bore the risk of loss when the goods were damaged or lost. It is conceivable that insurance will cover most losses that occur in international sales. It is, however, important to detect when risk has passed so that either the buyer or the seller may submit a claim with the insurer.[149]

If delivery terms do not require the seller to obtain insurance of the goods during carriage, then he must provide the buyer with all available information necessary to enable him to effect such insurance.[150]

Contracts involving goods sold in transit apply risk retroactively when the seller provides marine insurance against the loss of the goods. Otherwise, there are very few scenarios where a buyer of goods in transit would assume retroactive responsibility.[151]

II. Insolvency/Bankruptcy

Counsel for a seller should advise his client to take proactive measures to avoid financial trauma in the event a buyer does not pay or files bankruptcy. Graham

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145 *Id.*
146 *Id.*
147 *Id.*
148 McMahon, *supra* note 125.
149 Cheng, *supra* note 88.
150 Gillette, supra note 82, at 169.
151 Cheng, *supra* note 88.

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Cooper discusses traditional protective measures and the reasons for them in the following passage, from his article, The Reclamation Rights of Unpaid and Unsecured Sellers in International Trade.

> Normally a seller will protect its position by obtaining from the buyer an irrevocable letter of credit drawn on a reputable bank, sometimes even obtaining acceptance of the letter of credit by another bank of the seller's choosing. The seller may even require of the buyer various forms of security over some of the buyer's assets prior to entering the transaction or require a guarantee of payment to be given by a third party. More elaborate forms of protection could involve the obtaining of credit insurance by the seller or the requirement of a performance bond to be posted by the buyer. Furthermore, a cautious seller may engage in invoice discounting for security, as well as cash flow, reasons. The reasons for such precautions lie partly in the usual risks of trade -- the defaulting buyer becoming insolvent before payment, for example -- and partly in the special uncertainties involved when trade occurs internationally, where the seller in order to secure a remedy might require recourse to the defaulting buyer's jurisdiction -- one with which the seller might not be familiar, or even, perhaps, a jurisdiction with which a familiarity borne of prior experience gives added reason for caution.[152]

When sellers find themselves unprotected from loss due to buyer's insolvency, the CISG provides remedies for breach of contract. Unfortunately, these remedies will often leave the seller in the same position, due to the insolvency of the buyer. Therefore, a seller is going to look for alternatives, the focus of which will most likely be the recovery of goods.[153]

For sellers to be in a position to request reclamation of goods under the CISG, it is important to make sure that the sellers have fulfilled their end of the bargain.[154] The seller may declare the contract avoided:

> (a) if the failure by the buyer to perform any of his obligations under the contract or this Convention amounts to a fundamental breach of contract, or (b) if the buyer does not, within the additional period fixed by the seller in accordance with paragraph (1) of Article 63, perform his obligation to pay the price or take delivery of the goods, or if he declares that he will not do so within the period of time so fixed.[155]

"The implication from this unusual conjunction of these situations is that failure to pay is not of itself sufficient to create a fundamental breach by the buyer."[156] Avoidance of a contract for nonpayment is not always available under the CISG since avoidance is only applicable when the breach is fundamental.[157] In the event of a non-fundamental breach the CISG provides for damages only, thus enforcing the principle of continuation of a contract.[158] The Nachfrist notice[159] (an automatic

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[152] G. S. Cooper, *The Reclamation Rights of Unpaid and Unsecured Sellers in International Trade*, 1987 Colum. Bus. L. Rev. 17, 18-19 (1987).
[153] *Id*,. at 34.
[154] *See id.*
[155] *Id.*
[156] *Id.*
[157] *See id.*
[158] *See id.*
[159] "Providing an automatic extension of time for the parties to a commercial contract to fulfill their obligations is mandated under German law. Such automatic extension, and its mechanics, is

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extension of time to perform pursuant to a contract) "[…] serves as a device for making the non-payment a fundamental breach."[160] If the seller proceeds with this notice and payment is not made, the avoidance of the contract creates various consequences discussed in Article 81 which provides:

> (1) Avoidance of the contract releases both parties from their obligations under it, subject to any damages which may be due. […]
> (2) A party who has performed the contract either in whole or in part may claim restitution from the other party of whatever the first party has supplied or paid under the contract. If both parties are bound to make restitution, they must do so concurrently.[161]

In the end, an unsecured seller is always left in a precarious position when a buyer fails to pay or becomes insolvent. The only practical advice for sellers is to protect property interests through contract language including reservation of title clauses. This will allow the seller to retain legal ownership in the goods until payment in full is received.[162] "The retention of title device is a good example of a procedure which is not a security device but rather an agreement, in this case about the passing of title, which serves the same purpose as a security but without the need or even the ability to be registered."[163]

"The validity of title retention, or *Romalpa* clauses as they are called in the English and Australian legal system, is not governed by the Convention."[164] Thus, domestic law will determine the validity of such a clause. "This has been the position in literature and commentaries, and in reported case law from civil law jurisdictions. Now, common law jurisdictions take the same position."[165]

In *Roder Zelt- und Hallenkonstruktionen GmbH v. Rosedown Park Party Ltd.,* the Federal Court for the Southern Australian District in Adelaide was confronted with an installment contract between a German seller of tents and other prefabricated structures for public functions and an Australian buyer of such equipment for its rental business for large sports events. After the buyer had

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known in German as *Nachfrist.* Its principal purpose is to provide additional latitude and protection to the debtor contracting party." M. DiPalma, *Nachfrist under National Law, the CISG, and the UNIDROIT and European Principles: A Comparison,* 5 (1) International Contract Adviser 28-38 (1999), available at http://www.cisg.law.pace.edu/cisg/biblio/DiPalma.html.

160 Cooper, *supra* note 152, at 33.

161 *Id*.

162 *Id.*, at 21.

163 *Id.*, at 22.

164 The following is a proposed example of a Rompala clause: The seller reserves the following rights in relation to any goods provided to the buyer by the seller, until all accounts owed by the buyer to the seller are fully paid. 1. Legal ownership of goods; 2. to enter the buyers premises (or the premises of any associated company or agent where the goods are located) without liability for trespass or any resulting damage and retake possession of the goods; and 3. to keep or resell any goods repossessed pursuant to 2).

165 C. W. Pauly, *Is Avoidance Under CISG Art 64 a Powerful Remedy? Comparison of the CISG Remedy with Third-Party Rights*, available at http://www.cpauly.com/html/CISG%20essay%20Pauly%20October%202004.pdf (last visited 7 March 2005).

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fallen behind on his payments and the company was placed under administration, the German seller claimed the unpaid equipment back under the title retention clause in the contract.[166]

> The court found that the CISG governed the construction and meaning of the *Romalpa* clause, but that domestic law would govern its validity. Since both Australian and German law recognized the validity and effects of title retention clauses as not allowing title in the delivered goods to pass until the purchase price has been paid, the seller had retained his title and was able to reclaim his goods from the buyer against the conflicting claims of other creditors.[167]

E. E-Commerce – Managing Electronic Sales While Minimizing Risk

I. Generally

> The benefits of efficiency and interactivity that flow from the expansion of electronic communications are reduced by persistent legal uncertainty […]. In particular, it is difficult to be sure that such communications will satisfy statutory rules that require writing, or signatures, or the use of original documents. Many legal relationships, especially contracts, depend on the intention of the parties. It has not been clear to what extent such intention can be communicated automatically, or by symbolic actions like clicking on an icon on a computer screen.[168]

Merchants need a systematic approach to managing electronic presales and sales processes and documents, one that maximizes business opportunities and minimizes potential pitfalls, claims, and litigation. It is imperative that merchants who sell goods via the Internet use their virtual storefront "to integrate quality assurance and risk management so that solid business transactions with predictable profits are systematically secured."[169]

> By being proactive, [merchants] can build high quality contracts into [their] storefront and install appropriate architecture to respond to various customer and legal requirements. [Merchants] can also embed preventive law in [their] website store structure, so that [their] virtual storefront helps to prevent claims and disputes from arising and eliminates or reduces their impact. For those risks that cannot be fully controlled or eliminated, [businesses] can build in transactional steps and contractual terms that seek to resolve problems quickly, minimize losses, and preserve business relationships.[170]

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166 *Roder Zelt- und Hallenkonstruktionen GmbH v. Rosedown Park Party Ltd*., (1995) 57 Fed. Ct. Rep. (Austl.) 216-240, *CLOUT No. 308* (Fed. Ct., S. Austl. District, Adelaide Apr. 28, 1995).

167 *Id.*

168 Uniform Law Conference of Canada, (1991 Winnipeg, MB) Uniform Electronic Commerce Act, available at http://www.law.ualberta.ca/alri/ulc/current/euecafa.htm.

169 H. Hapio, *Safe Sales in Cyberspace,* available at http://www.preventivelawyer.org/main/default.asp?pid=essays/hapio1.htm (last visited 5 Feb. 2005).

170 *Id.*

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"One of the traditional sales problems that all suppliers have faced under English law over the years is the extent to which they can ensure that their standard terms and conditions, set out on their invoices and other contractual documentation, are incorporated into any contract with a customer."[171] This problem is compounded when customer is another company which sets out its own terms and conditions on its order form.[172] "This has often led to the so-called 'battle of the standard forms' – where both buyer and seller try to ensure that a contract is concluded on their terms."[173] There has been considerable uncertainty over precisely what terms are incorporated in the final agreement in these circumstances.[174]

In a sales transaction conducted over the Internet, a seller is in a considerably stronger position than a traditional one.

> A web-wrap or click-wrap contract involves a buyer being "steered" through the supplier's Web Site, through carefully placed hypertext links, thus binding the buyer to the seller's conditions. There is no buyer's order form with additional, potentially contradictory, terms to confuse the agreement between the buyer and seller. In an ideal internet sales transaction, a buyer should be taken first through a description of the products, then, if the buyer wishes to proceed with a purchase, the buyer would be required to scroll through the supplier's terms and conditions, which would be attached by means of a hypertext link to a description of the goods. Having scrolled through those terms, the buyer will be asked to click on an icon accepting those terms before a further hypertext link takes the buyer to the order form documentation.[175]

Web-wraps should provide an effective mechanism for suppliers to ensure that their terms are incorporated into all contracts concluded over the Internet.[176]

> Legislative efforts have gone a long way to remove statutory impediments to electronic contracting by equating electronic records to paper documents. However, these efforts must be met halfway by parties engaging in electronic commerce. These parties must understand the new rules and effectively use the procedural tools provided to them to ensure that electronic contracts are valid and enforceable. By doing so, they will ensure that their various interests will be procedurally protected.[177]

See Appendix C for an example of an electronic commerce agreement.

A distinction between commercial and consumer sales was referred to in the introduction of this note. Consumers are protected in many legal settings to a greater extent than are commercial parties. Therefore, when possible, merchants should treat consumer buyers separately from commercial buyers for the purpose of, yet again, limiting liability.

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171 *Id.*
172 *See id.*
173 *Id.*
174 *Id.*
175 E-Com Legal Guide (n.d.), available at http://www.bakerinfo.com/apec/ukeuapec.htm#General%20introduction (last visited 7 March 2005).
176 *Id.*
177 J. C. Selman, *The Process of Electronic Contracting: New Rules for the New Commerce*, (n.d.) available at http://www.hewm.com/use/articles/electroniccontracting.pdf#search='ueta%20pace' (last visited March 7, 2005).

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On the Internet, B2B (business-to-business), also known as e-biz, is the exchange of products, services, or information between businesses rather than between businesses and consumers.[178]

> If your products are suitable for both consumer and business sales, your e-commerce team may see great benefits to keeping your e-sales infrastructure the same for both. You must discourage them from doing so.[179]

> While it may seem to make business or technical sense to treat all customers the same, you need to remind your decision-makers that your company will lose contract opportunities available to the B2B sales arena if it elects to do so. You should not volunteer to give up the freedom of contract that you have in B2B sales. The costs and other consequences of potentially limitless liabilities and remedies offered to consumers are not commonly (or knowingly) accepted in B2B dealings. Your shareholders, financing institutions, and insurance carriers would probably argue strongly against such excessive e-risk-taking, too.[180]

II. Under the CISG

When relating internet sales transactions to the CISG, a particularly relevant and potentially problematic aspect of the CISG is its current failure to even address the subject of electronic contracting.[181] While most states in the United States have adopted a version of the Uniform Electronic Transactions Act (UETA)[182], which revises state commercial codes when parties enter into sales contracts by electronic medium, the CISG has not yet addressed that specific issue. However, CISG Article 11 provides that "a contract of sale need not be concluded in or evidenced by writing […]."[183] The logical conclusion would therefore be that contracts may be formed electronically, since there is not requirement for a writing in the CISG.[184] However, a court could disagree, "so it may be prudent for contracting parties to have an overriding agreement to conduct transactions electronically, until the CISG is modified to specifically provide for electronic contracting."[185]

> The United Nations Convention on International Sales of Goods […] does not specifically require a "writing" to form a contract. However, it was written before the widespread use of electronic transactions, and could therefore be subject to interpretation in this modern context. In the U.S., the Electronic Signatures in Global and National Commerce Act (E-SIGN) provides federal law on this subject,

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[178] Definition of B2B available at http://searchcio.techtarget.com/sDefinition/0%2C%2Csid19_gci214411%2C00.html.

[179] H. Haapio and A. Smith*, Safe Sales in Cyberspace,* available at *http://www.cisg.law.pace.edu/cisg/biblio/haapiosmith.html#saf* (last visited 7 March 2005).

[180] *Id.*

[181] Gabbard, *supra* note 4.

[182] The Uniform Electronic Transactions Act was drafted in 1999 and is available at http://www.law.upenn.edu/bll/ulc/fnact99/1990s/ueta99.htm (last visited 7 March 2005).

[183] Gabbard, *supra* note 4.

[184] *Id.*

[185] *Id.*

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> but there are no definitive court interpretations of this relatively new law. Therefore, it is prudent to utilize a form of this ECA to cover electronic transactions until the law on this subject is settled.[186]

F. Preventive Law

The use of preventive law in international trade saves merchant clients money and provides peace of mind in the form of increased certainty when doing business. The potential liability associated with failure to include a well-drafted choice of law clause provides an easy example of the necessity of a proactive approach to sales contracts. Legal protection through a court system is usually the last resort for merchants, who would rather sell goods, than testify in court.[187] A well-crafted contract that addresses all foreseeable issues in the transaction goes a long way in guaranteeing that both parties will perform as agreed.

> The private guarantees of the binding force of contracts include such arrangements as making use of specific assets (such as customer relations, supply, transport, service and other systems and research cooperation) for mutual goals, credible (bilateral) commitments ("changing hostages"), investment in a common project, self-redress, changing business secrets, cross-ownership, gentlemen´s agreements, questions of image, and also (horizontal or vertical) integration between undertakings.[188]

The actual purchase agreement should include the following terms: parties to the agreement, the quantity of identified goods, the price, the terms of payment, quality specifications, the place and time of delivery, passage of risk, provisions for alternate dispute resolution and indemnification.[189] When parties state that the CISG is the applicable law to be applied to the contract, the specific version in respect to language (English, French, Italian, etc.) should also be stated. Inevitably, translations have discrepancies which could result in an unexpected interpretation of the CISG.[190]

> The key ingredients to successful drafting under CISG are likely to be simplicity, and the avoidance, as much as possible, of U.S. terms of art. […] The lesson

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[186] *Id.*

[187] M. Rudanko, *Preventive Law and International Trade*, *in* National Center for Preventive Law (n.d.), available at http://www.preventivelawyer.org/main/default.asp?pid=essays/rudanko.htm (last visited 7 March 2005).

[188] *Id.*

[189] *Id.*

[190] The authentic Russian text of Article 68 considered by the Tribunal in this case does not contain the sentence: The risk in respect of goods sold in transit passes to the buyer from the time of the conclusion of the contract. This discrepancy in authentic texts has been called to the attention of UNCITRAL. UNCITRAL is taking steps to correct the authentic Russian text.

Editorial remarks by A. H. Kritzer on *Diamant Ltd v. Kirov District Tax* Inspectorate of the City of St. Petersburg, Federal Arbitration Court for the Northwestern Circuit, 3 June 2003, available at http://cisgw3.law.pace.edu/cases/030603r1.html#ce (last visited 7 March 2005).

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> here, as with the drafting of all international contracts, is to avoid terms which have a particular local or regional meaning, and to watch very carefully for false cognates.[191]

One suggestion is to use the CISG to streamline negotiations.[192] Merchants should also consider a letter of intent/memorandum of agreement from the outset of any business transaction to establish the framework for the relationship.[193] These can provide terms that benefit both parties and at the same time place specific limitations on liability.

> The CISG promotes uniformity. The CISG may make international transactions easier for "heavy volume" traders who trade with numerous different foreign countries because the domestic sales laws of such other foreign countries are less important if the CISG governs. Further, CISG judicial decision-making continues to spread. There are now thousands of reported CISG decisions worldwide and more every year.[194]

> If the CISG will apply, recognize the absence of the "statute of frauds." […] In the early stages, consider announcing that oral statements are not binding and only the final written agreement will govern. […] [R]ecognize "battle of the forms" issues. Consider requiring a single written agreement signed by both parties rather than an exchange of different and contradictory forms. […] [R]ecognize that the seller may disclaim warranties without following the formal requirements of the UCC. […] [R]ecognize that the "perfect tender" rule will not apply. […] [R]ecognize the potential remedy of a "unilateral price reduction." […] [R]ecognize that there will be some uncertainty with respect to the applicable statute of limitations[.] […] [R]ecognize that there are important issues of international commerce that are *not* addressed in the Convention, including,for example: choice of forum; submission to jurisdiction; alternative dispute resolution (mediation, conciliation, or arbitration); language of contract; language of dispute adjudication; attorney fees for disputes (for example, loserpays); and choice of law for any gaps in the CISG.[195]

G. Conclusion

Concerns over legal issues in international trade are no longer the concerns of large corporations alone. Any business engaging in commercial trade today has the potential of engaging in the international sale of goods. Before entering into a sales transaction with a foreign customer, merchants need to arm themselves with the protection that a well-drafted contract can offer.

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[191] Crawford, *supra* note 11, at 189.

[192] C. E. Rumbaugh, JD, CPCM*, International Purchasing "Rules-of-the-Road" Terms and Conditions in the International Marketplace*, May 1, 2000. NAPM International Purchasing Conference, New Orleans, Louisiana, available at http://www.ism.ws/ConfPastAndOnlineDaily/Files/May00/Rumbaugh-CQ.pdf.

[193] T. McNamara, *U.N. Sale of Goods Convention: Finally Coming of Age?,* 32 Colorado Lawyer (2003), available at http://www.cisg.law.pace.edu/cisg/biblio/mcnamara.html(last visited 7 March 2005).

[194] *Id.*

[195] *Id.*

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The CISG is the default position of most transnational sales agreements for commercial goods. Knowledge of the provisions of the CISG and use of Incoterms in the contract provide merchants with certainty in the contract. This certainty arises from explicit choice of law clauses and trade terms that define exact points when risk of loss transfers from seller to buyer, for example.

The passage of risk of loss carries a great deal of weight in international sales contracts, as most of these contracts will involve the carriage of goods. The CISG puts all parties to the contract on a level playing field and attempts to allocate risk to the party with the best chance of minimizing loss and insuring the integrity of the goods.

Risk of loss and breach of contract are two key issues that create disputes regarding liability of the parties. Since most sales disputes do not make it to any court, it is important to avoid ambiguity in the contract so that the intentions of the parties can be easily interpreted from the writing.

The pre-emptive step of setting out all foreseeable issues in the written contract will reduce legal fees for the parties involved. Additionally, merchants need to insure against loss and require some form of title retention to avoid financial difficulties when a buyer fails to submit payment in full.

With the increase in the Internet as a sales medium comes the prevalence of e-commerce. Merchants who establish a thorough virtual storefront that incorporates the issues set out in this note are protected from the uncertainty that is inevitable in transnational sales agreements.

> Of course, none of these problems can arise when the parties have the foresight to solve the problem in their contract -- either by plain, blunt words or when risk passes to the buyer, or by incorporating a prefabricated solution in a standard contract or in a trade term as defined by Incoterms. And even when the contract gives no explicit solution, the matter may be settled by the practices established by the parties or by trade usage.[196]

The international sale of goods is a risky business. If merchants' counsel becomes well-versed with the intricacies of contracting in this arena, there will be fewer surprises and less exposure to unanticipated liability for their clients.

Appendix A

The following are samples of explicit clauses for contracting parties to utilize to opt out of the application of the CISG in a contract:

> The rights and obligations of the parties under this agreement shall not be governed by the provisions of the 1980 United Nations Convention on Contracts for the International Sale of Goods; rather, these rights and obligations shall be governed by the law of the State of Connecticut, including the Uniform Commercial Code as enacted in Connecticut.[197]

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[196] J. O. Honnold, Risk of Loss, International Sales: The United Nations Convention on Contracts for the International Sale of Goods 8.3 *(*1984).

[197] P. Winship, *Changing Contract Practices in the Light of the United Nations Sales Convention: A Guide for Practitioners,* 29 Int'l law 525 (1995).

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> This Contract shall be governed by and construed under the laws of the Commonwealth of Pennsylvania, not including the 1980 United Nations Convention on Contracts for the International Sale of Goods.[198]
>
> Disclaimer of UN Convention on Sale of Goods. PURSUANT TO ARTICLE 6 OF THE UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS (UN CONVENTION), THE PARTIES AGREE THAT THE UN CONVENTION SHALL NOT APPLY TO THIS AGREEMENT.[199]

Appendix B

The following is a succinct list of the most commonly used trade terms (INCOTERMS) as found on the International Chamber of Commerce web-site.[200]

EXW - Ex Works: Title and risk pass to buyer including payment of all transportation and insurance cost from the seller's door. Used for any mode of transportation.

FCA - Free Carrier: Title and risk pass to buyer including transportation and insurance cost when the seller delivers goods cleared for export to the carrier. Seller is obligated to load the goods on the Buyer's collecting vehicle; it is the Buyer's obligation to receive the Seller's arriving vehicle unloaded.

FAS - Free Alongside Ship: Title and risk pass to buyer including payment of all transportation and insurance cost once delivered alongside ship by the seller. Used for sea or inland waterway transportation. The export clearance obligation rests with the seller.

FOB - Free On Board: Title and risk pass to buyer including payment of all transportation and insurance cost once delivered on board the ship by the seller. Used for sea or inland waterway transportation.

CFR - Cost and Freight: Title, risk and insurance cost pass to buyer when delivered on board the ship by seller who pays the transportation cost to the destination port. Used for sea or inland waterway transportation.

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198 *Id.* (citing E. A. Farnsworth, *Review of Standard Forms or Terms under the Vienna Convention,* 21 Cornell Int'l Law Journal 439, at 447 (1988); *see also* B. Blair Crawford, *Drafting Considerations under the 1980 United Nations Convention on Contracts for the International Sale of Goods,* 8 J.L. & Com 187 (1988)).

199 P. Winship, *Changing Contract Practices in the Light of the United Nations Sales Convention: A Guide for Practitioners*, 29 Int'l Law 525 (1995) (citing R. E. Myrick & P. Smith Wilson, *Licensing Rights to Software, in* PLI, Technology Licensing and Litigation 1993, at 585).

200 Incoterms 2000, available at http://www.ltdmgmt.com/incoterms.htm.

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CIF - Cost, Insurance and Freight: Title and risk pass to buyer when delivered on board the ship by seller who pays transportation and insurance cost to destination port. Used for sea or inland waterway transportation.

CPT - Carriage Paid To: Title, risk and insurance cost pass to buyer when delivered to carrier by seller who pays transportation cost to destination. Used for any mode of transportation.

CIP - Carriage and Insurance Paid To: Title and risk pass to buyer when delivered to carrier by seller who pays transportation and insurance cost to destination. Used for any mode of transportation.

DAF - Delivered at Frontier: Title, risk and responsibility for import clearance pass to buyer when delivered to named border point by seller. Used for any mode of transportation.

DES - Delivered Ex Ship: Title, risk, responsibility for vessel discharge and import clearance pass to buyer when seller delivers goods on board the ship to destination port. Used for sea or inland waterway transportation.

DEQ - Delivered Ex Quay (Duty Paid): Title and risk pass to buyer when delivered on board the ship at the destination point by the seller who delivers goods on dock at destination point cleared for import. Used for sea or inland waterway transportation. DDU - Delivered Duty Unpaid -- Title, risk and responsibility of import clearance pass to buyer when seller delivers goods to named destination point. Used for any mode of transportation. Buyer is obligated for import clearance.

DDU - Delivered Duty Unpaid: Seller fulfills his obligation when goods have been made available at the named place in the country of importation

DDP - Delivered Duty Paid: Title and risk pass to buyer when seller delivers goods to named destination point cleared for import. Used for any mode of transportation. Note: EXW, CPT, CIP, DAF, DDU and DDP are commonly used for any mode of transportation. FAS, FOB, CFR, CIF, DES, and DEQ are used for sea and inland waterway.[201]

Appendix C – Sample E-Commerce Agreement

This Electronic Commerce Agreement is made by and between the following parties in order to facilitate their transacting business via electronic exchanges.

Purchaser: _____
Seller: _____

[201] Incoterms 2000, available at http://www.ltdmgmt.com/incoterms.htm.

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1. Parties Intend to be Bound by Electronic Exchanges

Both parties to this agreement hereby evidence their intention to be bound by the electronic exchanges as described herein and specifically agree as follows:

(a) The parties agree that no separate "writing" shall be required in order to make their EDI transactions legally binding, notwithstanding any contrary requirement in any law.

(b) The parties agree that no "signature" shall be required in order to have legally enforceable EDI transactions between them.

(c) The parties hereby agree that neither will raise any defense of lack of writing or lack of signature or any other similar defense based upon a "Statute of Frauds" or similar rule in any dispute which may arise between them for any transaction entered into through electronic data interchange.

2. Offer and Acceptance

Electronic transmission of an order by Purchaser to Seller shall be effective as an offer when it is received on the Seller's terminal. Said offer shall be accepted by Seller in any one of the following ways:

(a) Via electronic transmission of an acknowledgment, acceptance or receipt of the offer; or

(b) The shipment of the goods called for in the offer.

3. Terms of the Transaction(s)

The terms of any electronic transaction shall be those terms and conditions which may be contained in the electronic data transmissions, plus the terms and conditions attached hereto as *Exhibit A*.

4. Miscellaneous

A. Nothing in this agreement shall be deemed to create any responsibility of either party to buy or sell any specific goods. This agreement is solely intended to facilitate the handling of electronic transactions between the parties. Neither party shall be entitled to, or required to do any certain amount of business with the other, nor shall either party be required to do business with the other for any certain period of time.

B. This agreement may be terminated by either party by giving _____ days written notice to the other. Such termination of this agreement shall not affect any transactions entered into before the effective date of the termination, even if the performance of such transactions is to take place after the effective date of termination.

C. While it is the intent of both parties to use electronic transmission to the extent practical, this agreement does not preclude the exchange of documents by other methods when required by special circumstance.

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D. The parties agree to adopt and maintain reasonable security procedures to ensure that: (1) documents transmitted electronically are authorized; (2) business records and data are protected from improper use; and (3) access codes and electronic identification codes are adequately secured.

E. This agreement shall be governed by the laws.[202]

[202] Gabbard, *supra* note 4, available at http://www.napm.org/pubs/ISMMag/files/120416.pdf (last visited 7 March 2005).