

Prijevara i materijalni nedostaci po Bečkoj konvenciji - dvije strane istog novčića?

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**FRAUDULENT MISREPRESENTATION AND NON-
CONFORMITY WITHIN THE CISG – TWO SIDES
OF THE SAME COIN?**

Master Thesis

Mentor: doc. dr. sc. Antun Bilić

Zagreb, September 2023

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Summary

To address the globalization of world trade and the business practices of parties in various contracting states, the United Nations Convention on Contracts for the International Sale of Goods (“**CISG**”) was developed. Despite this notable goal, the relationship between the CISG and domestic provisions on issues of contract validity has been a much discussed issue since the CISG entered into force.¹ Fraudulent misrepresentation continues to be a problem even after 35 years of the CISG. This article examines different solutions to the CISG's validity gap due to fraudulent misrepresentation.

Even if it has been asserted that the CISG will continue to be one of the biggest success stories in the area of unifying international private law, fraudulent misrepresentation is an issue still not resolved and left for the future courts, arbitrators and academia to find a solution.

Key Words: CISG, Fraudulent misrepresentation, non-conformity, validity, uniformity, different solutions.

¹ Magnus, Ulrich., Opting in and opting out: Can there be uniform interpretation or does *variatio delectate* govern? in: *Journal of Law & Commerce*, Volume 38, 2019-2020, p. 4.

Sažetak

Kako bi se odgovorilo na globalizaciju svjetske trgovine i poslovne prakse stranaka u različitim državama ugovornicama, razvijena je Konvencija Ujedinjenih naroda o ugovorima o međunarodnoj prodaji robe ("CISG"). Unatoč ovom značajnom cilju, odnos između CISG-a i domaćih odredbi o pitanjima valjanosti ugovora tema je o kojoj se puno raspravljalo od dana kada je CISG stupio na snagu. Prijevarno postupanje u vezi s međunarodnom prodajom robe predstavlja problem čak i nakon 35 godina postojanja CISG-a. Ovaj rad ispituje različita rješenja glede uređenja pitanja prijevarnog postupanja unutar CISG-a.

Iako je CISG jedna od najvećih uspjeha u području objedinjavanja međunarodnog privatnog prava, pitanje prijevarnog postupanje i uređenje tog odnosa i dan danas zahtjeva posebnu pažnju. Takvo se postupanje može i ne mora gledati kroz prizmu materijalnih nedostataka kako ih uređuje CISG.

Ključne riječi: CISG, prijevarno postupanje, valjanost ugovora, materijalni nedostaci, globalizacija, objedinjavanje međunarodnog privatnog prava.

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1. INTRODUCTION

It is never possible to completely create uniform international contract law or uniform law in general. Instead, the scope of uniform legal instruments is often constrained because there are not enough uniform provisions that everyone can agree on, or because it is not necessary to agree upon them.² Under the United Nations Convention on Contracts for the International Sale of Goods ("CISG"), this function is particularly important and difficult in terms of domestic legal remedies and their applicability to CISG contracts.

The CISG's primary goal is to achieve global uniformity with regard to the creation of international sales contracts and the legal rights and obligations of both the seller and the buyer. As a result of "*the growth of international trade on the basis of equality and mutual benefit*," the states parties to the CISG seek to "*promote friendly relations*" with one another. This ultimate goal is impacted by the adoption of uniform regulations that govern the international contract sale of goods, which forms the basis of all international trade, and take into account the various social, economic, and legal systems that would help remove legal barriers to international trade and promote the expansion of foreign trade. An examination of the CISG's Preamble reveals that the authors really did intended that "*the adoption of consistent regulations to guide contracts for the sale of goods internationally and to always keep in mind the various social, economic, and legal systems would help remove legal obstacles to trade internationally and encourage the growth of foreign trade.*"

Despite the pledge in the Preamble, the CISG expressly excludes from its scope a few crucial contractual concerns, such as the validity of the contract. Thus, the CISG does not provide a formal harmonization of international sales law. This exemption has been viewed as a danger to overall development of the CISG.

Any recourse to local, non-unified law in such circumstances runs the risk of upsetting the balance of rights and obligations between international buyers and sellers that has been established by the CISG; whenever domestic law gives a party a remedy that it would not have under the CISG's rules, its concurrent application potentially undermines predictability and legal certainty in international trade.

² Report of Committee of the Whole I Relating to the Draft Convention on the International Sale of Goods, U.N. Doc. A/32117/Annex I, 1977, p. 146.

This article will address the topic of contract invalidity due to fraudulent misrepresentation and how it compares to the CISG's non-conformity regulation as one of the conceivable events that could jeopardize legal certainty in international trade.

2. FRAUDULENT MISREPRESENTATION UNDER THE CISG

Within the CISG, fraudulent misrepresentation can be seen from two perspectives. The first perspective examines fraudulent misrepresentation through the lens of the provisions on non-conformity and the good faith principle. That viewpoint more closely aligns with the consistent application of the CISG and acknowledges its purpose.

On the other side, strategy for protecting national law is to treat fraudulent misrepresentation as a non-CISG-governed issue of contract validity. That viewpoint, however, might raise issues with the objective of the CISG and its uniform application.

2.1. Non – Conformity provisions

The CISG does not use the term fraudulent misrepresentation. National laws usually describe it as an untrue statement of facts made by one contracting party to the other, which induced that other party to enter into the contract.³ From the perspective of the misrepresenting party, it can be either innocent, negligent or fraudulent.⁴ Misrepresentation often relates to the features of the goods. For example, one party convinces the other that the goods have a certain characteristic, which in fact, they do not. Believing it, the other party concludes a contract.

The CISG, however, regulates non-conformity of the goods. According to Art. 35 of the CISG the seller must deliver goods which are of the quantity, quality and description required by the contract. If the goods do not correspond to the contract at the time when the risk passes to the buyer, the seller is liable.⁵ The CISG does not differentiate between the reasons for non-conformity. It is also irrelevant whether the goods were non-conforming from the moment of the conclusion of the contract, or non-conformity arose during the phase of delivery.⁶

³ Furmstone Cheshire, Fifoot & Furmston's Law of Contract, Butterworths, 1996, pp. 275 – 276; Širova Lucia, Misrepresentation under English Contract Law and Its Comparison to Slovak Contract Law in: International and Comparative Law Review, V. 16, no. 2, 2016, p. 200; Beale Hugh, Chitty on Contracts, General Principles, Twenty seventh edition, Sweet & Maxwell, 1994, pp. 333 – 334.

⁴ Schroeter, Ulrich G. Defining the Borders of Uniform International Contract Law: The CISG and Remedies for Innocent, Negligent, or Fraudulent Misrepresentation, Oxford University Press, 2007, in: Villanova Law Review Volume 58, 2013, pp. 16 – 36; *ibid.*, p.201.

⁵ Art. 36 of the CISG.

⁶ Arts. 35 and 42 of the CISG.

Consequently, if misrepresentation causes the goods to deviate from the contract, the goods are non-conforming in the sense of Art. 35 of the CISG.⁷ For example, in *Used car case* the buyer concluded a contract for a sale of car relying on documents which showed that the car was first licensed in 1992 and the mileage on the odometer was low. Subsequently it was discovered that car had been actually licensed in 1990 and that the mileage on the odometer was much higher. Since the seller fraudulently misrepresented the car's features, the Cologne Higher Regional Court ("**OLG Köln**") ordered the seller to pay damages under articles 35(1), 40, 45 and 74 CISG. The courts followed the same reasoning in many other similar cases, and applied the CISG.⁸

A number of scholars indeed argue that, when misrepresentation is caused by fraud, a defrauded buyer can additionally rely on the provisions of national law. This is supposedly justified by the fact that the CISG does not take into account the risk of the seller's dishonest behaviour and does not provide for the adequate consequences.⁹ It is true that the CISG does not mention fraud or dishonesty. However, the CISG regulates the consequences of seller's dishonest behaviour. According to Art. 40 CISG, despite its omission to timely notify the seller about non-conformity, the buyer does not lose its right to rely on non-conformity if non-conformity relates to facts which the seller knew or could not have been unaware and which it did not disclose to the buyer. Therefore, there are many scholars which state that Art. 40 deals with

⁷ Art. 35 of the CISG; Kröll Stefan, Mistelis Loukas, Perales Viscasillas Pilar, *UN Convention on Contracts for the International Sale of Goods (CISG) Commentary*, C. H. Beck Hart Nomos, 2011, pp. 540- 541; Heiz Christoph R., *Validity of Contracts Under the United Nations Convention on Contracts for the International Sale of Goods in: Vanderbilt Law Review* 639, Volume 20, Issue 4, 2021 p. 651 – 654; Schlechtriem Peter, Butler Peter, *UN Law on International Sales, The UN Convention on the International Sale of goods*, SPRINGER, 2009, pp. 33 - 113, 43 – 44; Honnold John O., *Uniform Law for International Sales under the 1980 United Nations Convention*, Third edition, 1999, pp. 115 - 241; Schlechtriem Peter, Schwenger Ingeborg, *Commentary on the UN Convention on the International Sale of Goods (CISG)*, Fourth edition, Oxford University Press, 2016, p. 530 – 531; 1. *Pamesa Ceramica v. Yisrael Mendelson Ltd*, The Supreme Court sitting as the Court of Civil Appeals 17 March 2009; Ferrari Franco, Flechtner Harry, Brand Ronald, *The Draft UNCITRAL Digest and Beyond: Cases, Analysis and Unresolved Issues in the U.N. Sales Convention*, Sellier, European Law Publisher, 2004, pp. 243 - 244; Schroeter, Ulrich G., *Defining the Borders of Uniform International Contract Law: The CISG and Remedies for Innocent, Negligent, or Fraudulent Misrepresentation*, Oxford University Press, (2007), Clay case, *Oberlandesgericht Koblenz (Court of Appeal Koblenz) CISG - online 2301 24 February 2011*; Schlechtriem Peter, Schwenger Ingeborg, Schroeter Ulrich G. *Kommentar zum UN-Kaufrecht (CISG)*, CH. BECK, 2019, p. 112, Schlechtriem Peter, *Uniform Sales Law – the UN – Convention on contracts for the International Sale of Goods*, Manz, Vienna, 1986, p. 473.

⁸ *Beijing Light Automobile Co., Ltd v. Connell Limited Partnership*, CISG – online 379, 05 June 1998, *Menthol USP Brand crystals case*, Bundesgericht/Tribunal fédéral (Swiss Federal Supreme Court) CISG – online 838, 13 January 2004; *Used car case I, Oberlandesgericht Köln (Court of Appeal Cologne)*, CISG – online 254, 21 May 1996; *Fallini Stefano & Co. snc v. Fordic BV, Rechtbank Roermond (District Court Roermond)*, CISG – online 29, 19 December 1991; *Rheinland Versicherungen v. Atlarex s.r.l.*, Tribunale di Vigevano (District Court Vigevano), CISG – online 493, 12 July 2000; *Foil case I, Oberlandesgericht Karlsruhe (Court of Appeal Karlsruhe)*, CISG – online 263, 25 June 1997; *German Wine case, Landgericht Trier (District Court Trier)*, CISG – online 160, 12 October 1995; 54 O 644/94, Landgericht Landshut, 05 April 1995.

⁹ Schlechtriem/Schwenger, *op.cit.* u bilj. 7, pp. 618 - 619; Heiz, *op.cit.* u bilj. 7, p. 654.

situation of seller's gross negligence and intent and as a consequence Art. 40 CISG takes into account fraudulent behaviour, and similar cases of bad faith.¹⁰

This is also confirmed by case law. When the seller was "fraudulent" or when it used a "willful deception" the courts did not apply national law, but Art. 40 CISG and other provisions of the CISG.¹¹

Furthermore, the CISG standard remedies for non-conformity of the goods are considered to be sufficient to compensate a defrauded buyer. The buyer is authorised to request the goods which conform to the contract or, if the fraud was substantial, it can immediately avoid the contract and claim restitution.¹² In addition, the buyer can claim all the damages it suffered, and, if it already paid the price, it can claim interest.¹³ Practically, the remedies under the CISG do not differ from the ones national laws provide in situations of fraudulent behaviour.

¹⁰ Schlechtriem/Butler, *op.cit.* u bilj. 7, p. 129; Paprika powder case II, Bundesgerichtshof (German Supreme Court, CISG – online 847, 30 June 2004; Schlechtriem, *op.cit.* u bilj. 7. p. 69 - 72; Garro Alejandro, The buyer's "Safety valve" under Article 40: What is the seller supposed to know and when? in: *Jornal of Law and Commerce*, Volume 25, 2005 p. 259 – 260; Ferrari/Fletcher/Brand, *op.cit.* u bilj. 7, p. 695; Huber Peter, Mullis Alastair, *The CISG: A new textbook for students and practitioners*, Sellier European Law, Publishers, 2007, p. 164; Lookofsky Joseph, *Understanding the CISG, A Compact Guide to the 1980 United Nations Convention on Contracts for the International Sale of Goods*, Fourth (World-wide) Edition, Kluwer Law International, 2012, p. 33, Beijing Light Automobile Co., Ltd v. Connell Limited Partnership, *loc.cit.* u bilj. 8.

¹¹ Used car case I, *loc.cit.* u bilj. 8; German vine, *loc.cit.* u bilj. 8; Fallini Stefano & Co. snc v. Fordic BV, *loc.cit.* u bilj. 8; Rheinland Versicherungen v. Atlarex s.r.l, *loc.cit.* u bilj. 8; Foil case I, *loc.cit.* u bilj. 8; 54 O 644/94, *loc.cit.* u bilj. 8; Beijing Light Automobile Co., Ltd v. Connell Limited, *loc. cit.* u bilj. 8.

¹² Arts. 46, 25, 49, 81 (2) CISG.

¹³ Art. 74 of the CISG.

2.2. “Good faith” principle

The statement that the CISG must be construed to "observe good faith in international trade" is the most puzzling of all the principles in Article 7. A lengthy and unique debate is dedicated to the use of the good faith principle as a defense against fraudulent misrepresentation under the CISG. In fact, until this day, it appears that there is no consensus on what this principle implies or how to apply it. Most scholars fail to define the principle at all or instead employ general language that lacks any substantive meaning. When discussing the substantive meaning of the term "good faith," it is frequently necessary to interpret the idea via the prism of moral and/or ethical principles.

Accordingly, it has been noted that good faith in international trade should be seen as a moral or ethical standard that business people should uphold, reflecting core ethical ideals in international sales contracts.¹⁴ Some scholars believe that even though the appeal of moral and/or ethical standards is quite understandable, it is obvious that such an approach, once introduced in the area of international commercial transactions, becomes completely useless as it rests on undeterminable set of variables and even broader definitions.¹⁵

Those scholars believe that the CISG does not take into account the risk of seller's fraud and that it does not envisage adequate consequences. Therefore, the buyer can additionally rely on the remedies provided by the otherwise applicable national law.¹⁶ However, there are other scholars that believe in that scenario national law could title every situation as “fraud” and wrest it from the CISG's scope of application so they find the solution within the good faith principle.

A proper evaluation of the CISG's good faith principle must begin with recognizing that the good faith in international trade is specifically mentioned in the wording of Art. 7(1) of the CISG. Namely, according to Art. 7 (1) the CISG has to be interpreted in light of the observance of good faith in international trade. Thus, the meaning of good faith is determined by the CISG, and not by national laws.¹⁷ According to the CISG, good faith is an obligation of the parties to

¹⁴ Kröll Stefan, Mistelis Loukas, Perales Viscasillas Pilar, *op. cit.* u bilj. 7. p. 121.

¹⁵ Nina Tepoš, Hrvoje Markovinović, The CISG and the Good Faith Principle, *Journal of Law & Commerce*, Vol.38 (2019-2020), pp. 18-19.

¹⁶ Magnus, *op.cit.* u bilj. 1, p. 370; Schlechtriem Peter, Schwenzler Ingeborg, *Kommentar zum Einheitlichen UN- Kaufrecht (CISG)*, Sixth Edition, C.H.Beck Helbing Lichtenhahn Verlag, 2013, p. 618; *Kröll/Mistellis/Viscasillas*, pp. 72 - 73.; Honnold, *op.cit.* u bilj. 7, p. 114; *Slechtriem*, p. 32 – 34.

¹⁷ *Kröll/Mistellis/Viscasillas*, *op.cit.* u bilj. 7, pp. 114 – 115; Schlechtriem/Butler, *op.cit.* u bilj. 7, p. 48 - 50; Dulces Luisi v. Seoul International, COMPROMEX. Comisión para la Protección del Comercio Exterior de Mexico, M/115/97, 30 November 1998; Sheehy Benedict, Good Faith in the CISG: The Interpretation Problems of Article 7, In: *SSRN Electronic Journal*, 2004, pp. 4 - 35; Felemegas John,

act honestly and fairly.¹⁸ Therefore, good faith prohibits the parties to act fraudulently, i.e. to intentionally deceive the other party. The meaning of fraud can also be discerned from Art. 40 CISG.¹⁹ The seller who knows about non-conformity of the goods and does not disclose it to the buyer acts intentionally, in bad faith and thus fraudulently. Jurisprudence increasingly began to adopt such a position.²⁰ For example in the case of *Dulce Luisi v. Seoul International*²¹ the Korean company had a Letter of Credit issued with terms that ultimately contradicted the revised terms of the contract, with the apparent purpose of defrauding the Mexican company. The Mexican Trade Tribunal, accepted jurisdiction and applied the CISG. The Tribunal stated that the buyer acted against one of the basic principles in international trade, that companies participating in international commercial transactions must observe good faith, thus the buyer acted fraudulently. Commentators to this decision usually agree that the decision stand for “(...) *an application of good faith (under the CISG) as a means of penalizing civil fraud in international level.*”²²

Despite the fact that historically this may not have been what the CISG's creators meant the good faith principle to stand for, it seems that case law has gone in a different direction.

An International Approach to the Interpretation of the United Nations Convention on Contracts for the International Sale of Goods (1980) as Uniform Sales Law, CAMBRIDGE University Press, 2007, p. 13 - 14; *Lookofsky, op. cit. u bilj. 10, p. 32 – 33.*

¹⁸ Powers Paul J., ‘Defining the Undefinable: Good Faith and the United Nations Convention on the Contracts for the International Sale of Goods in: *Journal of Law Commerce p. 334*; Iftime Emanuela, Good Faith in International Sales Law in: *Acta Universitatis George Bacoiva, Juridica, Volume 3, Issue 2, 2014, pp. 1. – 2*; Troy Keily, Good faith & the Vienna Convention on contracts for the international sale of goods (CISG) in: *vj 1999/1 p. 18, 38*; Bridge, *op.cit. u bilj. 16, pp. 98 – 115.*

¹⁹ Ferrari/Fletcher/Brand, *op. cit. u bilj. 7, p. 681 – 683*; Garro, *op.cit. u bilj. 10, p. 253.*

²⁰ *Kröll/Mistellis/Viscasillas, op.cit. u bilj. 7, p. 68 – 69.*

²¹ *Dulces Luisi v. Seoul International, COMPROMEX. Comisión para la Protección del Comercio Exterior de Mexico, M/115/97, 30 November 1998.*

²² Sheehy, *op.cit. u bilj. 18 p. 8.*

2.3. (I)relevance of the "validity exception" under article 4 (a) of the CISG

Only some components of a sales contract are governed by the CISG. The formation of the contract as well as the rights and obligations of the seller and the buyer are governed by Art. 4(1) of the CISG. Unless it expressly provides otherwise, the CISG is not concerned with the validity of the contract.

Some scholars believe that the CISG provisions on non-conformity of the goods do not "expressly provide otherwise" in regard to the contract validity. The development of CISG article 4 (a) appears to suggest that the Working Group purposefully relegated all questions of fraud to domestic law and removed all questions of mistake from the CISG. The purpose of the non-conformity provisions is to sanction the breach of contract, and not the lack of consent during contract formation.²³ Therefore, the issue of lack of consent during contract formation should be left to national laws as a matter of contract validity. The lack of consent is typically caused by fraud, duress, threat or incapacity.²⁴ They all go far beyond a mere non-conformity.²⁵ Fraud presupposes wilful deception or dishonesty which persuaded the other party to conclude the contract. Consequently, it is not governed by the CISG.²⁶

According to Art. 4(1) of the CISG, it governs the formation of the contract and the rights and obligations of the seller and the buyer. Unless it expressly provides otherwise, the CISG is not concerned with the validity of the contract.²⁷

²³ Perović Vujačić Jelena S., Contracts for the international sale of goods: A comparative review of the solutions of the UN convention on the international sale of goods and the Serbian law of obligations, *Revija Kopaoničke škole prirodnog prava*, Volume 1, Issue 1, 2022, p. 197; Bydlinski, Franz, *Das allgemeine Vertragsrecht, Das UNCITRAL-Kaufrecht im Vergleich zum österreichischen Recht*, 1985, pp. 85 – 86; Lookofsky, *op.cit.* u bilj. 10, p. 280; Loizou Soterios, *CISG: scope of application*, Pace University, Elisabeth Haub school of law institute of international commercial law – Jams global training series, 2017, p. 6; Schroeter, *op.cit.* u bilj.7, p. 33.

²⁴ Ferrari/Flechtner/Brand, *op.cit.* u bilj. 7, p. 522; Kröll/Mistelís/Perales Viscasillas, *op.cit.* u bilj. 7, p. 69; Kastely Amy, H., The Right to Require Performance in International Sales: Towards an International Interpretation of the Vienna Convention, *Washington Law Review*, Volume 63, Issue 3, 1988, p. 646; Huber/Mullis p. 23; Loizou, p. 6; Magnus, p. 235; Perović/Vujačić, p. 197; United Nations Commission on International Trade Law, Volume VIII: 1977, p. 42.

²⁵ Schlechtriem/Schwenzer, *op.cit.* u bilj. 7, pp. 618 – 619; Kröll/Mistelís/Perales Viscasillas, *op.cit.* u bilj. 7, pp. 541 – 542.

²⁶ Heiz, *op.cit.* u bilj. 7, p. 654; Honnold, *op.cit.* u bilj. 7, p. 31; Schlechtriem, p. 32

²⁷ Longobardi Laura E., Disclaimers of Implied Warranties: The 1980 United Nations Convention on Contracts for the International Sale of Goods, *Fordham Law Review* Volume 53, Issue 4, 1985, p. 868; *Malaysia Dairy Industries Pte. Ltd. v. Dairex Holland BV*, *Rechtbank's-Hertogenbosch Unilex rolnr. 9981 / HA ZA 95-2299*, 2 October 1998; *Asante Technologies, Inc., v. Pmc-Sierra, Inc*, United States Distric

This can be illustrated on an example of sale of Van Gogh painting. After the seller convinced the buyer that the painting was original, the parties entered into a contract. Subsequently it was discovered that the painting was a forgery. Since the contract provided for an original Van Gogh, the buyer can invoke non-conformity of the goods in accordance with Art. 35 of the CISG. However, this is not sufficient to sanction seller's wilful deception and remedy buyer's lack of consent.²⁸

Consequently, the impact of fraud on the contract validity has to be assessed under the national law. This is supported by the case law. In Miami Valley case, the US plaintiff claimed that German defendant fraudulently misrepresented the specifications of a paper winder. The U.S. District Court for the Southern District of Ohio concluded that "*the CISG drafters made no attempt to prescribe the legal effect of a seller's negligent or fraudulent misrepresentation*". Thus, it allowed plaintiff to proceed with the arguments under national law.²⁹

However, on the other side, some scholars believe that the "*validity exception*" in subparagraph (a) is not all-inclusive and does not state that all disputes over the validity of sales contracts or of usages fall beyond the purview of the CISG – rather, it expressly presupposes that the CISG may apply to such matters under other articles of the CISG. The challenging element of this phrase is "*expressly provided*". It is unclear exactly what it signifies.

The CISG does not in any of its provisions mention the term validity, so the crucial part is to define validity.

Court, N.D. California, No. C 01 – 20230 JW., 30 July 2001; Ferrari /Flechtner/Brand,*op.cit.* u bilj. 7, pp. 99 – 100.

²⁸ Art. 4 CISG; Heiz, *op.cit.* u bilj.7, pp. 652 – 654; Honnold,*op.cit.* u bilj. 7, p. 31; Blair H. Allen, Hard cases under the Convention on the international sale of goods: A proposed taxonomy of interpretative challenges, Duke Journal of Comparative & International Law, Volume 269, Issue 21, 2011, p. 317; Soinco SACI et al. v. NKAP, Handelskammer Zürich CISG – online 1291 31 May 1996.

²⁹ Miami Valley Paper, LLC v. Lebbing Engineering & Consulting GmbH, U.S. District Court for the Southern District of Ohio, CISG – online 1362, 10 October 2006.

2.3.1. Defining validity within the CISG

The meaning of the term "validity" within the CISG is still mostly ambiguous. There are usually two approaches to that issue so far:

- 1) validity definition as a question for national law,
- 2) validity definition as a question for CISG.

2.3.1.1. Validity definition as a question for national law

Some scholars believe that CISG itself points to domestic law as the source to define validity of international sales contract.³⁰ The reasons are two folded:

- 1) validity of the contract rises a question of national public policy³¹ and
- 2) governments use validity to deem certain events improper in national jurisdiction.³²

In court practice, two US federal district courts held that ‘validity’ within the CISG encompasses “*any issue by which the domestic law would render the contract void, voidable or unenforceable.*”³³ On that track, Prof. Peter Schlechtriem made an attempt to explain the concept validity in more detail:

*“(…) if a contract is rendered void ab initio, either retroactively by a legal act of the state or of the parties such as avoidance for mistake or revocation of one’s consent under special provisions protecting certain persons such as consumers, or by a ‘resolutive’ condition (i.e., a condition subsequent) or a denial of approval of relevant authorities, the respective rule or provision is a rule that goes to validity and therefore is governed by domestic law and not by the CISG.”*³⁴

³⁰ Longobardi, *op.cit.* u bilj. 28, p. 874; Alcaraz, p. 62, Walt, pp. 4-5.

³¹ Longobardi, *op.cit.* u bilj. 28, p. 874 – 875; Kastely, *op.cit.* u bilj. 25, p. 646; *United Nations Commission on International Trade Law, Yearbook, Volume VIII: 1977, p. 42.*

³² Longobardi, *op.cit.* u bilj. 28, p. 874 – 875.

³³ *Geneva Pharmaceuticals Technology Corp v Barr Laboratories, Inc and Others*, 201 F Supp 2d 236, 282 (SDNY 2002); *Barbara Berry, SA de CV v Ken M Spooner Farms, Inc*, 59 UCC Rep Serv 2d 443 (WD Wash 2006).

³⁴ Peter Schlechtriem, ‘Article 4’ in Peter Schlechtriem and Ingeborg Schwenzer (eds), *Commentary on the UN Convention on the International Sale of Goods (CISG)* (2nd edn, Oxford University Press 2005) para 7.

Both definitions focus on the effect specified in the domestic legislation rather than the events leading up to that effect.³⁵ In following this strategy, scholars have typically taken a liberal approach of validity-related effects. Therefore, there is somewhat of a consensus that fraud, duress, and incapacity are validity questions under Article 4(1) of the CISG.³⁶

2.3.1.2. Validity definition as a question for CISG

A recent example is the stance given by two important German CISG scholars, who contend that a domestic law that prohibits one party from relying on particular contractual terms does not affect the contract's "validity" as used in Article 4 sentence 2(a) CISG.³⁷ The true reasons for trying to keep the domestic provision in question outside the CISG's "validity exception" lay not in its effect upon the contract, but rather in the reasons that triggered such an effect under the provision. It may not be immediately obvious to everyone the difference between the "voidable" type of effect on the one hand and the "cannot be relied upon" type of effect on the other. It is argued that even followers of the upper approach while dealing with a question that is clearly not covered by the CISG, adopted a rather flexible understanding of the term validity.³⁸ In doing so, they in fact do not look to the effect specified in domestic legislation, but rather to the reasons that led to it and if the CISG has already addressed them. Therefore, Prof. Schroeter provided for a different definition:

"(...) by provisions concerned with 'the validity of the contract', Article 4(a) of the CISG refers to legal limits to party autonomy."

This definition is based on the grant priority of party autonomy within the CISG. According to it, the CISG never specifies the level of the parties' autonomy and does not forbid the parties' will from determining what constitutes "validity". Therefore, the fact that a particular issue is covered by this validity exception does not automatically imply that it is subject to domestic law rather than the CISG.

A further need is that the CISG itself does not "*provide otherwise.*"

³⁵ Longobardi, *op.cit.* u bilj. 28, p. 881.

³⁶ *Kastely, op.cit.* u bilj. 25, p. 646; *United Nations Commission on International Trade Law, Yearbook, Volume VIII: 1977*, p. 42; *Kroll/Mistelis/Viscasilas, op.cit.* u bilj. 7, p. 69; *Huber/Mullis* p. 23; *Koneru*, p. 146; *Blair, op.cit.* u bilj. 29, p. 317; *Magnus*, p. 235.

³⁷ B. Piltz, 'Gestaltung von Exportverträgen nach der Schuldrechtsreform', *Internationales Handelsrecht*, 2002, p. 5; P. Schlechtriem, *Internationales UN-Kaufrecht*, 4th edition, Mohr Siebeck, Tübingen, 2007, para. 147 – both with reference to § 444 of the German Civil Code as in force since 1 January 2002.

³⁸ Schroeter, *op.cit.* u bilj. 7, p. 61.

It is a general consensus that the CISG does not cover the issues of:³⁹

- legal limits on what to sell;
- legal limits on who to sell to or to purchase from;
- legal limits on how to sell.

On the other hand, there are some validity issues that are covered by the CISG:⁴⁰

- formal validity;
- open-price contracts and pretium certum;
- initial objective impossibility.

Border line issues are:⁴¹

- fraudulent misrepresentation;
- contract clauses limiting a party's rights under the contract;
- surprising contract clauses;
- prohibitions of interest.

³⁹ Schroeter, contract validity, pp. 57. – 62.

⁴⁰ Schroeter, Contract validity, pp. 62. – 65.

⁴¹ Schroeter, pp. 65. – 69.

2.4. SUPREMACY OF THE CISG OVER NATIONAL LAW

When an issue is governed by the CISG it cannot be, at the same time, governed by national law. This is called the exclusivity of the CISG.⁴² It is enshrined in Art. 7 which provides that the CISG should be interpreted in line with its international character and the need to promote uniformity in its application. Understanding the significance of Article 7's instruction to interpret the CISG in line with its "international character" requires tracing the phrase's origins back to the Convention pertaining to a uniform legislation on the international sale of products ("ULIS"). The Working Group's formulation of CISG Article 7 was heavily inspired by Articles 2 and 17 of the ULIS. The ULIS specifically says in Article 2 that "*rules of private international law and the domestic laws resulting therefrom shall be excluded for the purpose of the application of the present Law*". These two clauses were designed to create a self-contained sales law that could be interpreted and applied independently of national laws by the nations that negotiated the ULIS.

Various amendments were suggested by national representatives participating in the CISG deliberations, but finally the Working Group decided on a change that would become the opening clause of CISG Article 7: "*In the interpretation and application of the provisions of this Convention, regard is to be had to its international character and to the need to promote uniformity*". The phrasing of article 7(1) suggests that judges should refrain from using a domestic definition of a provision or a phrase that would clash with its application when interpreting CISG provisions. For instance, the use of domestic concepts like "merchantability" and "average quality" were rejected in a case involving the sale of condensate crude oil when the arbitral body considered the conformity of the goods to the contract on the grounds that these interpretations would lead to a different outcome than what the CISG's drafters had intended. The "reasonable quality" criterion, which was in keeping with the CISG's overarching principles, was used to interpret the meaning of conformance instead.⁴³ Departing from the CISG's "international character" would be against its "international character," thus decision-makers must remember the exact reason it was created.

The legislative background of Article 7 thus reveals that the directive to interpret the CISG in accordance with its "international character" was included by the drafters to instruct courts

⁴² Schlectriem/Schwenzer, *op.cit.* u bilj. 7, p. 531; Felemegas, *op.cit.* u bilj. 18, p. 11; Hartnell, *op.cit.* u bilj. 16, pp. 1 – 93.

⁴³ Larry DiMatteo and others, 'The Interpretive Turn in International Sales Law: An Analysis of Fifteen Years of CISG Jurisprudence' (2004) 34 Northwest J Int'l L & Bus 299, 397.

to treat the CISG as an autonomous body of law rather than as a place to graft their domestic rules and traditions.

Furthermore, the importance of promoting uniformity when interpreting its provisions is emphasized in Article 7(1). The justification for this directive is clear: the consistency of rulings will decide if the CISG has been effective in achieving its goals, namely to remove legal obstacles and encourage the growth of global trade. Additionally, consistency in decisions promotes transactional clarity and aids in establishing and using the buyer's right to use the CISG's avoidance remedy. Although no definition of uniformity is given, scholars explain this issue in some detail. To guarantee that the rule of consistency is correctly applied, it is advised that the international nature of the CISG be understood along with it. This is supported by some CISG rulings. For example, the Serbian Chamber of Commerce Court of Arbitral stated that interpretation must be, 'consistent with foreign judicial practice, which was to be taken into consideration for the uniform application of the Convention, on the basis of article 7(1).

The national law could apply only if an issue is neither expressly settled in the CISG nor it can be settled according to its general principles.⁴⁴ The CISG contains a detailed regime on non-conformity of the goods. It is universally accepted that those provisions exclude the application of national law.⁴⁵ Allowing national law on misrepresentation to be applied despite the existence of CISG provisions, opens the door to forum shopping and legal uncertainty.

⁴⁴ Art. 7 (2) CISG)

⁴⁵ Kröll/Mistellis/Viscasillas, p. 541, p. 68; Ferrari/Fletcher/Brand, *op.cit.* u bilj. 7, pp. 243 - 249; Schlectriem/Schwenzer, p. 53; Bridge p. 19, Sheehy, *op. cit.* u bilj. 18, pp. 9 – 28; Felemegas John, 'The United Nations Convention on Contracts for the International Sale of Goods: Article 7 and Uniform Interpretation' in Pace Int'l L Rev (eds), Review of the Convention on Contracts for the International Sale of Goods, 2000, p. 10-11, Hartnell, *op.cit.* u bilj. 16, pp. 1 - 93, Bridge, pp. 526 – 527.

3. CONCLUSION

The CISG's scholars declared that they wanted to encourage the growth of global trade while taking into account the many legal, social, and economic systems that exist around the world. While several difficulties were addressed and resolved in the creation of the CISG, the perplexing and hotly contested subject of validity has persisted. Supporters may argue that leaving it up to the various domestic systems to determine whether a contract is legal allows for flexibility, but the truth remains that as long as there is no unified legislation on the matter, different court systems will apply different laws, and parties won't have a consistent expectation of what will happen next. One must look to the laws of many states, and establish agreement among the laws on matters like fraudulent misrepresentation.

The CISG states that contracts for international sale of goods shall be governed by uniform laws. The CISG's stated goals, however, appears to have been compromised by the absence of contract validity regulations. Significant validity difficulties have been restricted to the domestic law, which has led to adjudicators' reaching varying conclusions, which has resulted in inconsistent outcomes and legal unpredictability.

Fraudulent misrepresentation under the CISG is one of the most disputed and inelegant areas of uniform contract law. Most validity disputes are not covered by the CISG, particularly those that concern nations, or political issues. Despite the fact that it can be challenging to establish the appropriate line, a surprising number of other validity issues are in fact covered by the CISG. The provision in Article 4(a) of the CISG meant to provide direction in this area has not achieved what it was intended to. Due to the way it was written, it scarcely counts as a boundary maker that precisely tells us where the line dividing uniform law and domestic law is located but rather just as a warning sign that indicates *there is a border somewhere around here*.

In the same way, art. 40 of the CISG has been read as suggesting that a negligent buyer deserves more protection than a negligent seller, whose failure to disclose seems closer to fraudulent misrepresentations than a buyer's failure to file a timely complaint on account of material non-conformity of the goods.

Therefore, it is a challenging but necessary undertaking to specify the precise substantive scope of the CISG. It is necessary because the scope decides over which domestic rules of law the CISG prevails, thereby preempting the application of concurrent domestic law. It is difficult since the CISG itself offers no direction for the process by which this definition is to be achieved.

To find a uniform approach in this respect will remain a task for courts, arbitrators and academia in the upcoming years, but rethinking the validity exclusion is a crucial part of the answer.

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