



ON LEGAL UNCERTAINTY REGARDING TIMELY NOTIFICATION OF AVOIDANCE OF THE SALES
CONTRACT

by Ari Korpinen

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ABSTRACT

The paper deals with the topic of timely notification of avoidance. It is noted that legal uncertainty in contractual relations in international trade can be caused by a strict interpretation of the wording in Article 49(2)(b)(i) CISG, which states that the buyer loses his right to avoid the sales contract, unless he avoids the contract within a reasonable period after he knew or ought to have known of the seller's breach of contract. A strict interpretation of the said Article does not allow for the acknowledgment of the buyer's difficulties in assessing the fundamentality of the breach. In a situation where the defect in the delivered goods worsens gradually over time, the breach is yet not fundamental at the time he makes his notice of non-conformity pursuant to Article 39(1) CISG. Later he may learn that the breach has evolved into a fundamental breach and that he would have an interest to avoid the sales contract. A strict interpretation of the wording in Article 49(2)(b)(i) CISG means that the time limit for notifying avoidance is triggered at the same time as the time limit for notifying non-conformity pursuant to Article 39(1) CISG. Consequently, the buyer may already have lost his ability to efficiently avoid the sales contract at the time he would have the right to invoke that remedy in his case. This paper presents a solution to that problem, based on the application of Article 7(1) CISG. It is concluded that uniform application of the CISG as well as the need to observe good faith in international trade requires that the time limit for notifying avoidance is triggered at the time the buyer learned or ought to have learned *about the fundamentality* of the breach, which could be later than when the buyer learned of the breach as such.

1. Introduction

(1.) When a seller and a buyer conclude a sales contract, the seller has an interest to know whether the buyer intends to invoke the remedy of avoidance, or whether the seller can regard the transaction to be permanently finalized. On the other hand, the buyer has an interest to be able to rely on efficient contractual remedies in case the seller has delivered defective goods. Article 49(1) of the United Nations Convention on Contracts for the International Sale of Goods (CISG) provides the remedy of avoidance for the buyer in case the seller is guilty of a fundamental breach. Article 49(2)(b)(i) CISG stipulates that the buyer loses the right to avoid the contract, unless he submits to the seller a *notice of avoidance* within a reasonable time after he knew or ought to have known of the breach. The time limit is designed to protect the seller's interest of reliance on concluded contracts.

(2.) Practical problems arise when the buyer does not learn about the "fundamentality" of the breach at the same time as he learns about the defect that constitutes the breach. Such a situation may arise when the defect in the delivered goods is of such nature that it worsens gradually over time. A strict interpretation of the wording in Article 49(2)(b)(i) CISG provides that the time limit for notifying non-conformity and notifying avoidance are triggered at the same point in time, despite the fact that the buyer may have learned about the fundamentality of the breach later than about the defect in the goods. Consequently, the buyer may already have lost his right to avoid the contract at the time he learns that he would have a right to invoke that remedy. This issue is of practical importance, since the buyer may in fact lose recourse to the economically most efficient remedy for breach due to a strict interpretation of the wording in the CISG.

(3.) In this paper I will show that there are differing viewpoints on this issue in CISG legal literature and that this controversy is also reflected in case law. Furthermore, I will present a solution to the problem which is based on applying Article 7(1) CISG. My first conclusion is that (1) from the need to apply the CISG uniformly follows a requirement to acknowledge separate triggering dates for the time limits for notifying non-conformity and avoidance, respectively. My second conclusion is that (2) the argument of separate triggering dates is supported by the need to observe good faith in international trade.

1.1 Purpose and scope of the paper

(4.) The purpose of this paper is to provide an argument for why it is necessary to acknowledge separate triggering dates for the time limits for notifying non-conformity on one hand and notifying avoidance on the other hand. Furthermore, the purpose is to show how this result can be achieved within the framework of the CISG.

(5.) For the purposes of the discussion it is assumed that the seller has delivered goods that are in non-conformity to the sales contract (Article 35 CISG) and that the non-conformity amounts to a fundamental breach of the sales contract (Article 25 CISG). It is also assumed that the buyer has taken delivery of the goods and paid the purchase price (Article 53 CISG) as well as that the buyer

has inspected the delivered goods (Article 38(1) CISG). Furthermore, it is assumed that the buyer has submitted a *notice of non-conformity* to the seller, pursuant to Article 39(1) CISG. It is assumed that the buyer has not fixed an additional period for performance for the seller (Article 47(1) CISG), which would have the effect of triggering the said time limit after such an additional period has expired (Article 49(2)(b)(ii) CISG). It is further assumed that the seller has not made a request for providing remedy at his own expense for failure to perform his obligations pursuant to Article 48(2) CISG, which would have the effect of triggering the said time limit after the buyer has declared that he will not accept performance (Article 49(2)(b)(iii) CISG).

1.2 Structure of the paper

(6.) After having explained the topic problem in section (2.1), I will present two court cases that provide differing viewpoints as regards the topic problem (2.2). In section (3.1) I submit that the differing case law reflects contradicting views on the topic in CISG legal literature. After that I will present arguments for why separate triggering dates for the respective notifications can be justified under the requirement of uniform application of the CISG in Article 7(1) CISG (3.2). In (3.3) I will explain why the same result can be achieved through recourse to the need to promote good faith in international trade, pursuant to Article 7(1) CISG.

2. On legal uncertainty regarding timely notification of avoidance of the sales contract

2.1 The legal problem explained

(7.) After having taken delivery of and inspected the goods in accordance with the sales contract, the buyer may find a defect in those goods and consequently make a claim that the said goods do not conform to the sales contract. The buyer then wants to invoke a remedy (e.g. price reduction under Article 50 CISG or specific performance under Article 46(1) CISG) against the seller. Under Article 39(1) CISG the buyer loses the right to rely on a lack of conformity of the goods if he does not give notice to the seller specifying the nature of the lack of conformity within a reasonable time after he has discovered it or ought to have discovered it. Therefore, in order to be able to invoke a remedy such as a price reduction or specific performance against the seller, the buyer must send to the seller a *notice of non-conformity* pursuant to Article 39(1) CISG.

(8.) The notice of non-conformity under Article 39(1) CISG does not allow the buyer to invoke the remedy of *avoidance*. Avoidance means that the parties are released from their unperformed obligations and that both parties have to reimburse each other what has been paid or supplied under the contract before the declaration of avoidance.¹ In order to be able to avoid the sales contract efficiently, the buyer must, pursuant to Article 26 CISG, send to the seller a *notice of avoidance*. Article 26 CISG stipulates that “a declaration of avoidance of the contract is effective only if made by notice to the other party”. In that notice the party entitled to avoidance must “clearly and unambiguously make it clear to the other party that the party entitled to avoidance does not intend to stand by the contract any longer”.² Article 49(2)(b)(i) CISG stipulates that “the buyer loses the right to declare the contract avoided unless he does so in respect of any breach

¹ See Leser(Schlechtriem), p.187

² See case ICC Arbitration, 1 March 1999

other than late delivery within a reasonable time after he knew or ought to have known of the breach. Both Article 39 CISG and Article 49(2)(b)(i) CISG stipulate that the buyer must make both the notice of non-conformity and notice of avoidance within a reasonable time after he knew or ought to have known of the breach. Problems arise in a particular sales transaction when the buyer first makes the notice of non-conformity and only later makes the notice of avoidance. Such a situation could arise for instance when the delivered goods have a defect that deteriorates over time. For example, the seller has delivered packaging machines with which it is not possible to package a certain type of goods, even though the buyer has clearly informed the seller of his specific purpose to package such goods and the buyer has not (and should not have) detected the defect during the inspection of the machines. In such a situation it can be that the buyer makes the notice of non-conformity when he learns that the goods are defective, but does not at the time *avoid* the contract because the defect has yet not developed into a fundamental breach. The goods continue to deteriorate after the submission of the notice of non-conformity so much so that the seller's breach of contract eventually amounts to a "fundamental breach" pursuant to Article 49(1) CISG, which entitles the buyer to avoid the contract. Then the aforementioned packaging machines deteriorate over time since they are used to package unsuitable goods and the seller has not informed the buyer of the unsuitability of the machines to package those goods. The buyer did not submit the notice of avoidance at the time he initially learned of the defect, because he did not find the defect to amount to a fundamental breach.

(9.) *Prima facie*, a comparison of the language in Article 39(1) CISG and Article 49(2)(b)(i) CISG gives the impression that the time limit ("reasonable time") is triggered at the *same point* in time, i.e. when the buyer knew or ought to have known of the breach. The buyer may then lose the right to avoid the contract under Article 49(2)(b)(i) CISG, if he submits the notice of avoidance only *after* the notice of non-conformity. A strict interpretation of the said articles produces this result. However, such a result in interpretation can be considered to cause legal uncertainty and confusion in executing certain international trade transactions.

2.2 *The problem in case law*

(10.) The problem with timely notification of avoidance has been dealt with in CISG case law. A Swiss court has ruled in line with the aforementioned [Para 8] strict interpretation of the stipulations in Article 49(2)(b)(i) CISG and Article 39(1) CISG. In the said ruling the Court observed that "if the buyer wishes to declare the contract avoided, it must do so within the same time requested to give due notice of the lack of conformity under Article 39(1) CISG".³ The Court specifically stipulated that the buyer must "in principle" declare avoidance at *the same time* as declaring non-conformity.⁴

(11.) The aforementioned stipulation of the *Handelsgericht Zürich* differs from later case law. An Italian court has ruled in favour of an interpretation that the time limit for notifying non-conformity on one hand and the time limit for notifying avoidance on the other hand are triggered at *different points in time*. The Court stipulated that "the starting point of the time limit for declaring avoidance is not the same moment as that of the time limit for giving notice of non-conformity". The Court further found that "whereas non-conformity has to be notified as soon

³ See case CH – *Handelsgericht Zürich*, 26.4.1995

⁴ See *ibid.*

as it is discovered or ought to have been discovered, avoidance has to be declared only after it appears that the non-conformity amounts to a fundamental breach which cannot otherwise be remedied”.⁵ The Court argued that this finding is justified by the fact that the remedy of avoidance of contract represents a last resort as compared to all other remedies available to the buyer.⁶

(12.) A comparison of the aforementioned rulings reveals that case law is not uniform as regards the issue of when the notice of avoidance can be efficiently made.⁷ The Swiss ruling emphasized strictly the wording of Article 49(2)(b)(i) CISG, i.e. that the time limit for notifying avoidance begins when the buyer learned or ought to have learned about the breach as such. In the Italian ruling, the Court emphasized that in assessing the starting point for the said time limit, regard must be had to the question of when the buyer learned or ought to have learned of the *fundamentality* of the breach. The finding of the Italian court thus provides new substance for solving cases where e.g. the delivered goods deteriorate over time due to a defect in those goods.

3. Solutions for approaching the problem of timely notification of avoidance

3.1 *Fundamentality of the breach is a different issue than the breach itself*

(13.) The finding in the aforementioned Italian court ruling is in line with opinions in legal literature concerning the CISG. *Leser* has noted that “in determining the period within which a declaration [of avoidance] must be made, regard must be had to the difficulty of assessing, whether or not the breach of contract is already fundamental”.⁸ *Leser* further notes that “once it is clear that a party has a right to avoid the contract, he should then be required to make the declaration within a reasonable period thereafter.”⁹ This means that the time limit for efficient avoidance of the sales contract begins at the time when the buyer learned or ought to have learned that the defect in the goods amount to a fundamental breach of the sales contract. This time can be later than the time when the buyer learned or ought to have learned about the defect (i.e. the non-conformity) itself. In the case of slowly deteriorating goods [see Para 8], this stipulation means that the buyer can efficiently avoid the contract when he learns that a major part of the delivered goods have become defective, even if the buyer already has made the notice of non-conformity under Article 39(1) CISG.

(14.) The finding in the Swiss court ruling is in line with the argument presented by *Will*. *Will* maintains that under Article 49(2)(b)(i) CISG “the time limit for avoidance begins to run as soon

⁵ See case *IT – Tribunale di Busto Arsizio*, 13.12.2001

⁶ See *ibid.*

⁷ Technically the facts in the aforementioned Italian and Swiss rulings differ from each other. In the Italian case, the Ecuadorian buyer submitted first the notice of non-conformity and only after the Italian seller did not succeed in its attempts to cure the defect, did the buyer avoid the contract. In the Swiss case, the German buyer gave the notice of non-conformity and notice of avoidance simultaneously (and in the Court’s opinion, too late). Despite the difference in the facts surrounding the case, a comparison of the findings in those rulings can be made in the assessment of the topic problem. The courts have in both cases made categorical statements as to when the time limit for notifying avoidance is triggered. It appears therefore that the different viewpoints regarding this issue clearly represent a genuine difference of opinions between the courts.

⁸ See *Leser(Schlechtriem)*, p.190

⁹ See *ibid.*

as the buyer knows or ought to have known of the breach” and that “the time limits for both [notifying non-conformity and notifying avoidance] begin to run simultaneously [...]”.¹⁰ It appears that there are conflicting views between *Will* and *Leser* on this issue and that the aforementioned Swiss and Italian rulings follow this line of division. In this paper I will provide justifications for why the finding in the Italian ruling can be regarded as accurate.

(15.) In my opinion, Article 7(1) CISG can be used to justify the argument of separate triggering dates for the time limits for notifying non-conformity and avoidance. Article 7(1) CISG stipulates that “in the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade”. Firstly, it can be maintained that “uniformity in application” of the CISG requires that separate triggering points for the time limits for notifying non-conformity and avoidance are accepted. Secondly, it can be maintained that “observance of good faith in international trade” requires acceptance of separate time limits.

3.2 “Uniformity in application” of the CISG motivates separate triggering dates for the time limits

(16.) Article 49(1) CISG stipulates as a prerequisite for the buyer’s right to avoid the sales contract that the seller’s breach of contract is “fundamental”.¹¹ Other remedies such as price reduction (Article 50 CISG) or specific performance (Article 46(1) CISG) can be invoked even when the breach of contract is not fundamental. It is therefore clear that the CISG makes a distinction between remedies as regards the prerequisites for invoking them. In order for the CISG to be uniformly applied pursuant to Article 7(1) CISG, that distinction must be noted also in the interpretation of the language in Article 49(2)(b)(i) CISG. Consequently, when assessing the issue of when the “reasonable time” for avoiding the contract begins, regard is to be had to the fact that a “fundamental breach” of contract is required for a claim of avoidance to be successful. In a particular business transaction the buyer may not be able to assess whether the seller’s breach of contract is fundamental at the time the buyer detects the defect in goods. If the fact that the CISG requires a “fundamental breach” is not noted in the interpretation of the language in Article 49(2)(b)(i) CISG, the CISG is in fact not uniformly applied as required by Article 7(1) CISG. Such a practice would mean that the requirement of a “fundamental breach” would only be noted when applying Article 49(1) CISG, but not when applying Article 49(2)(b)(i) CISG.

3.3 “Good faith in international trade” motivates separate triggering dates for the time limits

(17.) The parties of a sales contract, i.e. the buyer and the seller, have concluded the contract in order to execute a business transaction. The essential elements of the sales contract are the seller’s obligation of delivering goods that conform to the contract and the buyer’s obligation of paying the purchase price and taking delivery. The purpose of the sales contract is to facilitate a trade-off between the parties, i.e. the buyer pays money to the seller in order to receive a good that can be used in production of revenue-creating goods or directly in revenue-creating sales of the purchased good. In order for this theory to hold, the buyer must have remedies at his disposal when the seller breaches the contract (e.g. delivers defective goods). Furthermore, the buyer must be able to

¹⁰ See *Will*(*Bianca/Bonell*), p. 365

¹¹ See *Honnold*, p. 327

withdraw entirely from the contract (i.e. to avoid) in a situation where invoking other remedies would not be as economically efficient a solution for the buyer. Since the CISG has been created to facilitate international trade, the aforementioned realities must also be accepted in the interpretation of the CISG. Consequently, in interpreting the language of Article 49(2)(b)(i) CISG, regard is to be had to the availability of the remedy of avoidance for the buyer when the seller is guilty of a fundamental breach of contract. It follows, as *Leser* has noted, that in assessing the triggering date for the time limit for an efficient notice of avoidance, “regard is to be had to the difficulty in assessing the fundamentality of the breach”.¹² If the time limits for both notifying non-conformity and avoidance are set to begin at the same time, the buyer would not have at its disposal the remedy of avoidance in a situation where the defect in the delivered goods develops into a “fundamental breach” of contract after the buyer has submitted the notice of non-conformity. That result is contrary to good faith in international trade, since it means that the initial purpose of the sales contract – i.e. facilitating a trade-off between the buyer and the seller – is not realized merely due to a strict legal interpretation of the language in Article 49(2)(b)(i) CISG.

(18.) In legal literature it has been discussed that the party entitled to avoidance might speculate with his right to avoid the contract.¹³ For example *Honnold* has argued that a “delay in [...] avoiding a contract after a market change [...] may well be inconsistent with the Convention’s provisions governing these remedies when they are construed in light of the principle of good faith”.¹⁴ A buyer who is entitled to avoidance might for instance hold its decision to avoid the sales contract in anticipation of a change in the market price of the good. In order to prevent such speculation in bad faith, the time limit pursuant to Article 49(2)(b)(i) CISG should as such be relatively short.

(19.) In the author’s opinion the requirement of observing good faith in international trade must also be assessed from the seller’s point of view when setting the triggering date pursuant to Article 49(2)(b)(i) CISG. Allowing separate triggering dates for the time limits for notifying non-conformity and notifying avoidance has in practice the same effect as having simultaneous triggering points but allowing a longer time limit for notifying avoidance than for notifying non-conformity. In CISG legal literature it has been recognized that the seller has an interest “worthy of protection” to know as soon as possible after the contract is formed, whether the buyer will invoke the remedy of avoidance.¹⁵ The stipulation in Article 49(2)(b)(i) CISG reflects the basic idea that insecurity as regards the fate of the sales contract should be avoided.¹⁶ The seller’s interest to be able to trust that an already concluded contract holds is larger, the bigger the contract value is. This follows from the fact that avoidance of the sales contract transforms the contract into a “contractual restitutionary relationship”¹⁷ between buyer and seller, with restitution being made of what has been supplied or paid under the contract. I.e. the seller must reimburse to the buyer the purchase price that the buyer has paid. At least when the reimbursement to the buyer involves a big sum of money, it will affect at least temporarily the seller’s cash-flow situation. It would be unreasonable for the seller to live in uncertainty about the fate of the sales contract for an excessively long time. Therefore it can be argued that “observance of good faith in

¹² See *Leser*(*Schlechtriem*), p. 190

¹³ See *ibid.*

¹⁴ See *Honnold*, p.101

¹⁵ See *Huber*(*v.Caemmerer/Schlechtriem*), p. 493

¹⁶ See *Schlechtriem* 1995, p.110

¹⁷ Term used by *Leser*, see *Leser*(*Schlechtriem*), p.187

international trade” pursuant to Article 7(1) CISG also requires a rather strict assessment of when the buyer “ought to have known” about the fundamentality of the breach, when setting the triggering date pursuant to Article 49(2)(b)(i) CISG. In the final analysis it is a question of balancing the right of the buyer to economically efficient remedies and the right of the seller to be able to trust concluded contracts.

4. Conclusions

(20.) The topic of this paper was the situation where the seller has delivered goods to the buyer that do not conform to the sales contract and where the defect in the goods is of such nature that it worsens gradually over time. Since under a strict interpretation of Article 49(2)(b)(i) CISG the time limit for notifying *avoidance* is triggered at the same time as the time limit for notifying *non-conformity*, the author noted that the buyer may in some cases have already lost the ability to efficiently avoid the contract when he in fact learns for the first time that he would have reason to avoid the contract. The author noted that this problem causes legal uncertainty in international trade transactions [Para. 9].

(21.) In this paper the author presented from CISG case law two court rulings in which the courts have assumed different positions as to the issue of when the time limit for notifying avoidance is triggered, and also noted that these different rulings reflect the controversy regarding the issue in CISG legal literature [Para. 14]. A *strict* interpretation of the wording in Article 49(2)(b)(i) CISG calls for a solution under which the time limit for notifying avoidance is triggered at the time the buyer knew or ought to have known of the breach itself (i.e. regardless of whether he knew or ought to have known of the fundamentality of the breach). A more *flexible* interpretation would acknowledge the buyer’s difficulties in assessing whether the breach is fundamental. The author recommended that flexible interpretation for the case where the defect in the delivered goods is shown to worsen gradually over time. In the author’s opinion that result can be achieved within the framework of the CISG in two separate ways [Para. 15], i.e. by acknowledging that (a) the need to apply the CISG uniformly and (b) the need to promote good faith in international trade call for the aforementioned flexible interpretation of the wording in Article 49(2)(b)(i) CISG. On the other hand, the author also concluded that the need to promote good faith for the benefit of the seller requires that a strict interpretation is assumed as to the issue of *when* the buyer ought to have learned of the fundamentality of the breach [Para. 19].

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List of abbreviations

CH	Switzerland
CISG	United Nations Convention on Contracts for the International Sale of Goods
IT	Italy
ICC	International Chamber of Commerce
P.	Page
Para.	Paragraph
UN	United Nations