



## Comprehensive analysis of contract of sale of goods

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### Abstract

The central contract in an international sale of goods is the transfer in ownership of the goods that constitute the subject matter of the contract. The sale contract will typically contain a long list of terms. Their extent will depend upon the circumstances, but at a minimum they will deal with: (i) the quantity and quality of the goods, (ii) the price, (iii) the method of payment, (iv) the shipping details, (v) the place of delivery to the buyer, and (vi) the point at which risk passes from one party to the other. In an international sale, contractual terms also include: (i) the choice of law and the choice of forum, (ii) a reference to the co-ordinate contracts of finance, transport, and insurance.

**Keywords:** sale, goods, contract

### Introduction

A number of factors are significant in assessing whether or not the contracting parties have fulfilled their obligations under the contract.

### Invoices

Correct invoicing is essential in an international sales transaction as it affects not only the obligations between the buyer and seller but also, in most cases, financing arrangements made through the parties' bankers, as well as import and customs regulations in the buyer's country. The prudent buyer will often request a pro forma or 'sample' invoice in order to be sure that the invoice will conform to regulations the buyer faces in its own country. The details normally found on the commercial invoice include the names and addresses of the seller and buyer, the date and reference number of the buyer's order, a description of the goods sold, details of packages (including the weight of every bale or case), any identifying marks or numbers on packages, and, of course, the price.

### Packing of Goods

It is normally the duty of the seller to pack the goods in a manner that will assure their safe arrival in good condition, unless the parties have agreed otherwise in the sales contract. Failure to pack the goods properly may be considered a breach of condition and may entitle the buyer to reject the goods. Under the common law, the packing of the goods often forms part of the description of the goods<sup>[1]</sup>. It is customary that FOB and CIF prices include packing charges; therefore, if the seller intends to charge extra for this, it should be clearly stated in the quotation or confirmation. The type of packing chosen will depend upon a number of factors. The way goods are packed will affect the freight charges applicable. If goods are being shipped by sea, packing will vary depending upon whether goods are being shipped on deck or stored in the holds of the ship.

### Timeliness of Delivery

The principal legal systems take slightly different approaches to the obligation of timeliness of delivery. The common law systems generally regard timeliness of delivery as a condition of the contract. Therefore, the innocent party has the right to treat the contract as repudiated once a reasonable time for delivery has expired. While the provisions of the various civil law countries vary, a feature of many is a provision whereby the buyer must demand delivery and allow the seller a reasonable time for performance, even though the seller has delayed delivery in an apparent breach of the contract. This concept is variously referred to as Nachfrist. This approach is also taken in the CISG which provides for a "Nachfrist notice"<sup>[2]</sup>. Such notice allows either party to fix an additional period of time for the other to perform and thus covers a situation of failure of delivery or one in which unacceptable goods have been delivered. During the extended period of time, the granting party may not resort to any remedy for breach of contract.

### Loss of Goods in Transit

The loss of goods through fire, theft, or other misadventure can occur at any time prior to the delivery of the goods: during their transit, while they are being inspected, or after delivery. The question will immediately arise: Which party bears the loss? Usually, the loss is covered by insurance and the question is which of the parties is entitled to collect the insurance proceeds. In many countries, this will depend upon whether title or property in the goods has passed from seller to buyer at the time of the loss. The traditional common law rule, derived from the Sales of Goods Acts, was that the risk of accidental loss of goods passed when the property passed to the purchaser<sup>[3]</sup>. The parties should clarify the time of passage of risk between themselves and also with their insurer. The use of accepted trade terms goes a long way to limiting any problem as to who bears a loss. Generally, most defined trade terms provide that the risk will pass when the goods leave the

custody of the seller, i.e., in ex works contracts when they are collected by the buyer, and in FOB and CIF contracts when the goods are delivered to the carrier.

### **Acceptance and Rejection of Goods**

Under the common law, a buyer who is dissatisfied with the goods must indicate its intention to reject them within a reasonable time. In the absence of specific terms, the rejecting buyer is not obliged to return the goods to the seller, but the buyer becomes a bailee of the goods and must take reasonable care of them. Normally, the buyer's right to reject the goods is reserved until the goods arrive and the buyer has an opportunity to inspect them. This rule can present problems when applied to CIF contracts, where so often the shipping documents are sold or pledged before the buyer has the opportunity to inspect the goods. Under the UCC and the CISG, inspection of the goods and notice of any breach of contract is required. The CISG provides that the buyer must examine the goods within as short a period as is practicable<sup>[4]</sup>. The buyer must then give notice of lack of conformity within a reasonable time after it has been discovered or ought to have been discovered (no more than two years)<sup>[5]</sup>.

### **Certificate of Inspection**

An international seller is often required by contract to provide a certificate of quality from a recognized expert. Some are certificates of standard quality addressed to any person interested while others are addressed and prepared specifically for the parties to the contract. Depending upon the subject matter of the contract, these certificates may be issued by a scientist, a consultant, a trade association, a classification organization or an inspection organization. In negotiating requirements for such certificates, parties should be aware of the distinction between the quality of the goods and their condition when they arrive. It is important to express clearly what is covered by the certificate to avoid disputes later. A certificate of inspection is not the same as a certificate of quality as it states only that goods have been inspected and found to be in good condition. If more is expected of the inspection certificate, this must be clearly stated in the sale of goods contract as well as in the contract with the inspection organization<sup>[6]</sup>. Pre-shipment inspection is very important in international trade. If goods are inspected before they are delivered to the carrier and are found not to conform to the contract, costly shipping charges and trans-national legal disputes can be avoided.

### **Breach of Contract**

The remedies available under the common law and, the CISG are generally similar where there is a clear or acknowledged breach of contract. Damages under the common law will encompass an amount designed to compensate for the breach and may include an amount for lost profits which are a reasonably foreseeable result of the breach<sup>[7]</sup>. The CISG provides that damages shall consist of a sum equal to the loss, including loss of profit that was foreseeable at the time of the conclusion of the contract. If the breach is of a serious or important term of the contract, i.e. a condition, the innocent party is released from further obligation under the contract<sup>[8]</sup>. If the breach relates to a less serious term, i.e. a warranty, the

innocent party must continue to honour the contract, but is entitled to recover damages to cover the diminished value of the contract. Specific Performance is a remedy sought by the innocent party to a contract that has been breached in which the court orders the defaulting party to perform the obligations under the contract. The common law limits the granting of this remedy to cases in which the goods are unique or other circumstances in which damages are inappropriate. The civil law system, on the other hand, applies the principle much more readily, on the basis that the buyer wants what was ordered, not just compensation for the consequences of the failure to deliver. The Convention reflects this civil law tradition, but qualifies by providing that performance should be limited to cases in countries in which specific performance would be allowed by the domestic law of the land<sup>[9]</sup>.

### **International Regime for Sale of Goods**

The law relating to domestic sale of goods in India remains the Sale of Goods Act of 1930. However, the law applicable to international sale of goods is not uniform. There is a lot of deference shown to the choice of law and jurisdiction as agreed between the parties. Therefore, the fixation of jurisdiction and choice of law involves complex and multi-faceted questions of private international law. One of the early attempts to provide uniformity to the law came in the form of Hague Convention of 1964. This was followed up on by the UNCITRAL draft of 1977 which eventually served as the base model that culminated into the United Nations Convention on Contracts for International Sale of Goods. This Convention, which first came into force in 1988, appears likely to achieve the goal of widespread acceptance and use. As of January 2007, some 70 countries had ratified the convention, including Canada, the United States, China and the Russian Federation, and it is rapidly becoming an international standard for international sales contracts.

### **Application of CISG**

The Convention on the International Sale of Goods (CISG) applies to all contracts of sale of goods when the parties have their places of business in different contracting states or under a contract whose choice of law is a contracting state. In most instances it will automatically apply unless the parties 'opt' or contract out of it. The CISG applies only to commercial sales of goods and does not apply to household or domestic goods, goods sold by auction, or sales of securities, electricity, or aircraft. Contracts of sale are distinguished from contracts for services in two respects by CISG Art. 3. A contract for the supply of goods to be manufactured or produced is considered to be a sale unless the party who orders the goods undertakes to supply a substantial part of the materials necessary for their manufacture or production. When the preponderant part of the obligations of the party who furnishes the goods consists in the supply of labour or other services, the Convention does not apply.

The basic principle of contractual freedom in the international sale of goods is recognized by the provision that permits the parties to exclude the application of this Convention or derogate from or vary the effect of any of its provisions. The exclusion of the Convention would most often result from the choice by the parties of the law of a non-contracting State or

of the domestic law of a contracting State to be the law applicable to the contract. Derogation from the Convention would occur whenever a provision in the contract provided a different rule from that found in the Convention.

### Scope of CISG

The CISG governs the formation of the contract of sale and the rights and obligations of the seller and the buyer; however, it does not deal with the validity of the contract. Issues such as fraud, minority, or other problems of capacity are not covered by the Convention. Instead, they are left to be resolved by domestic law. Nor does the Convention deal with questions of title to the goods. Also excluded from the Convention are questions of product liability<sup>[10]</sup>.

### Case law Under CISG

There are a lot of cases settled under the CISG due to the growing importance of the convention. The cases discussed below deal with the three areas of CISG that have seen the maximum amount of litigation, namely, a) Application of CISG, b) Requirement of Notice, and c) Modicum of damages.

- a) Application of CISG: It has been decided by the Courts of Italy<sup>[11]</sup>, Germany<sup>[12]</sup> and Switzerland<sup>[13]</sup> that before resorting to the private international law rules of the forum, courts of Contracting States have to look into whether the Convention applies; in other words, recourse to the Convention prevails over recourse to the forum's private international law; since as a substantive law convention the CISG's rules are more specific and lead directly to a substantive solution whereas the private international law approach requires a two step approach (identification of the applicable law and application thereof).
- b) Notice Requirement: The German Supreme Court has held that notice of the mere fact of a lack of conformity is insufficient, but that the buyer must specify the precise nature of the defects; that notice should indicate both the nature and the extent of the lack of conformity, and should convey the results of the buyer's examination of the goods; that notice should be specific enough to allow the seller to comprehend the buyer's claim and to take appropriate steps in response, i.e., to examine the goods and arrange for a substitute delivery or otherwise remedy the lack of conformity; that the purpose of the specificity requirement is to enable the seller to understand the kind of breach claimed by the buyer and to take the steps necessary to cure it, such as initiating a substitute or additional delivery<sup>[14]</sup>.

Damages: The ICC Court of Arbitration held in a case that Defendant has to prove that Claimant failed to comply with its obligation to mitigate its loss pursuant to Art. 77 CISG. However, Defendant by just generally arguing that it does not deem appropriate the procedure of reselling the (blended) coke, without offering any evidence whatsoever in order to support this argument, fails to sufficiently substantiate, let alone prove, its allegation. Consequently, since Defendant did not show any facts which would support that Claimant's loss could have been - partially - avoided (e.g. by reference to a less expensive way of disposing of the coke) the Arbitral

Tribunal concludes that Claimant's way of disposing of the delivered coke which could not have been sold otherwise was accurate. Absent of any proof to the contrary; the Arbitral Tribunal, therefore, finds that Claimant did not violate its obligation to mitigate its damage<sup>[15]</sup>.

### References

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16. [ICC Court of Arbitration, case No. 9187 of June 1999, available online at <http://cisgw3.law.pace.edu/cases/999187i1.html>].