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A Comparative Analysis on the Avoidance of Contract under CISG and PICC

Leung Sze Lum

Avoidance serves as an aggrieved party’s most serious remedy. It is not a suitable remedy, except in exceptional situations. In light of CISG-AC Opinion No.5, this paper compares the circumstances under which avoidance of contract may take place under CISG and PICC, and explores how uncertainties arising from the principle of fundamental breach can be tackled.

Being the **ultima ratio**, avoidance serves as the aggrieved party’s **most serious remedy**. Hurting sellers badly and often being disadvantageous to buyers, it is not a suitable remedy except exceptional situations. Strict requirements for avoidance (and termination) are found in CISG and PICC, and they possess common characteristics. Opposed to ULIS, CISG rejected *ipso facto* avoidance, requiring notice. The same requirement is present in PICC. Avoidance in both is also a unilateral act requiring no court actions. Declaration of avoidance is sufficient. Once conditions are fulfilled the power to terminate lies at the discretion of the entitled party.

In CISG, circumstances for avoidance of contract include fundamental breach; failure to perform after additional notice; anticipatory breach; and partial

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1. See Judgment by Landgericht [District Court] München, Germany, 27 February 2002 English translation by Stefan Kuhn, [http://cisgw3.law.pace.edu/cases/020227g1.html](http://cisgw3.law.pace.edu/cases/020227g1.html)
3. See Judgment by Schweizerisches Bundesgericht (I. Zivilabteilung) [Supreme Court in Switzerland], 28 October 1998, [http://cisgw3.law.pace.edu/cases/981028s1.html](http://cisgw3.law.pace.edu/cases/981028s1.html)
4. Avoidance refers to a different concept in PICC. See section 2 of UNIDROIT Principles of International Commercial Contracts 2010(PICC)
6. Art. 7.3.1 UNIDROIT Principles
9. Arts.49(1)(a); 64(1)(a) CISG
10. Arts.49(1)(b); 64(1)(b) CISG
11. Art.72 CISG
avoidance. In the following, approaches of CISG and PICC towards these four aspects will be compared to examine the compatibility of these two instruments.

Fundamental breach serves as an important ground for avoidance. 49(1)(a) CISG allows an action for buyers to avoid the contract if the seller’s failure to perform amounts to a fundamental breach. Mirror provision for sellers is found in 64(1)(a). Fundamental breach is defined as those which “the detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract, unless the party in breach would not have reasonably foreseen such result.” In comparison, 7.3.1(1) and 7.3.1(2)(a) PICC are almost identical to that of the CISG.

One common element is the substantial deprivation on aggrieved party’s expectation. In CISG, such expectations are justified depends on circumstances such as contract provisions and customary usages. Examples from cases include failure to deliver; non-conforming goods or documents; defects in title; non-payment and failure to take delivery. The official commentary of PICC also requires that the breach must be of “material importance”.

Both provisions require foreseeability. In Article 25 CISG and 7.3.1(2)(a) PICC, a breach is fundamental if “the substantial deprivation was reasonably foreseeable to the breaching party.” However, no precise definitions, such as the time foreseeability should be determined, are provided. This may pose problems to specific fact situations including documentary sales and commodity trades.

PICC contains different approaches in determining fundamental breach. From

12 Art.51 CISG; Art.73 CISG
13 Art.25 CISG
15 UNIDROIT Principles of International Commercial Contracts Official Commentary on Article 7.3.2, Comment 2
7.3.1(2)(b), fundamental breach may occur if strict compliance with the unfulfilled obligation is of essence under the contract. Unlike CISG, 7.3.1(2)(b) looks not at the actual gravity of non-performance but the nature of the contractual obligations which strict performance might be of essence.\textsuperscript{18} Some commentaries suggest that this principle is commonly found among commercial transactions.\textsuperscript{19} Certain fault elements are present in PICC as fundamental breach may arise where the non-performance is intentional or reckless\textsuperscript{20} and where the parties’ trust deteriorates to an extent that future performance cannot be relied on.\textsuperscript{21} Although the principle of good faith is important, ‘fault’ is not generally a condition to contractual liability under CISG.\textsuperscript{22}

Another different approach in PICC refers to unmeritorious termination under 7.3.1(2)(e), that consideration will be given on whether the non-performing party would suffer disproportionate loss as a result of preparation or performance.\textsuperscript{23} Since harm deriving from breach is not the motive for termination\textsuperscript{24} and the determination of significant loss may be arbitrary,\textsuperscript{25} this approach is not applicable under CISG. Also, CISG gives no consideration to the reason of non-performance unless the breach is neither controllable nor foreseeable, while renegotiation\textsuperscript{26} and termination by court\textsuperscript{27} in cases of hardship is available in the UNIDROIT Principles.

The relationship between the seller’s right to cure\textsuperscript{28} and the buyer’s right to terminate remains a contentious issue as CISG itself provides no clear answers. Diverging interpretations are found.\textsuperscript{29} Much controversy exists on whether

\begin{footnotesize}
\begin{enumerate}
\item UNIDROIT Principles of International Commercial Contracts Official Commentary on Article 7.3.1, Comment 3b
\item Ibid.
\item Art.7.3.2(c) UNIDROIT Principles
\item Art. 7.3.2(d) UNIDROIT Principles
\item Art. 7.3.1(2)e UNIDROIT Principles
\item Takahashi (n 17) 103
\item Art. 6.2.3(1) UNIDROIT Principles
\item Art. 6.2.3(4)(a) UNIDROIT Principles
\item Arts. 37, 48 CISG
\item Singh (n 22); Christopher Kee, ‘Commentary on the Manner in which the UNIDROIT Principles May Be Used to Interpret or Supplement Article 48 of the CISG’ (2004) <http://www.cisg.law.pace.edu/cisg/principles/uni48.html> assessed 20 March 2013; Janse van Vuuren,
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notice to cure halts buyer's declaration of avoidance.\textsuperscript{30} Case law shows that courts are reluctant to conclude fundamental breach if speedy repair without inconvenience is available.\textsuperscript{31} One Swiss case explained that CISG “proceeds from the fundamental precedence of preservation of the contract”.\textsuperscript{32} Fulfillment of the contract remains possible provided that defects can be removed and buyer's essential interests are not at risk. PICC adopts completely different approach. 7.1.4(3) suggests that buyer's right to terminate will be suspended provided that the offer to cure is appropriate and the buyer has no “legitimate interest” in refusing.\textsuperscript{33} If the breach is capable of cure no fundamental non-performance can be found.\textsuperscript{34}

49(1)(b) and 64(1)(b) CISG provides another ground for avoidance applicable in case of seller’s non-delivery\textsuperscript{35} and buyer’s non-payment or failure to take delivery.\textsuperscript{36} Avoidance without fundamental breach is possible if the aggrieved party had fixed a reasonable additional time (Known as Nachfrist)\textsuperscript{37} in accordance with 47(1) or 63(1) CISG respectively requiring performance and the other party failed to comply within that period\textsuperscript{38} or made declaration of non-compliance.\textsuperscript{39} 7.3.1(3) PICC adopts a similar, yet slightly different approach. 7.1.5(3) provides broader scope, that in case of delay in performance which is not fundamental, the aggrieved party has right to give notice allowing additional reasonable time and may terminate the contract at the end of that period. Automatic termination after the period allowed is possible, if the aggrieved party provided it in the notice. Thus, the concept of "additional period of time" is commonly found among CISG and PICC.\textsuperscript{40} It is

\textsuperscript{32} Art. 7.1.4(3) UNIDROIT Principles
\textsuperscript{33} Kee (n 29)
\textsuperscript{34} Art. 49(1)(b) CISG
\textsuperscript{35} Art. 64(1)(b) CISG
\textsuperscript{37} UNCITRAL digest of case law on Article 49 (n 14) para. 21
\textsuperscript{38} UNCITRAL digest of case law on Article 49 (n 14) para. 21
\textsuperscript{39} UNCITRAL digest of case law on Article 49 (n 14) para. 21
suggested these requirements remove uncertainties about when delayed performance will be rendered. Difficulties about whether the breach constitutes fundamental non-performance can be overcome. Reasonable time is another common element, however none of these rules contain precise definition on its degree. What is being "Reasonable" must be made in light of the circumstances of the case at hand.

However, fixing of a Nachfrist of unreasonable length triggers the question regarding consequences to the notice. CISG is silent on this issue and the prevailing opinion is that a Nachfrist of unreasonable length does not make the notice ineffective but instead initiates a period of reasonable length. This view is confirmed by Oberlandesgericht Celle, that reasonability can be satisfied if the unreasonably short period extended through a reasonable period of time. Other cases also followed this approach. Nevertheless some commentators take a different view, arguing that an unreasonable period invalidates the notice. Koch considered this view as lacking persuasion as it fails to give appropriate account to the rules of interpretation in CISG, especially the principle of good faith. In comparison, PICC adopts a slightly different approach. Sentence 2 of 7.1.5(3) limits the right to exercise avoidance remedies if the Nachfrist is of unreasonable length, by extending the Nachfrist to a reasonable length. Thus PICC conforms to the prevailing view and may supplement CISG in this aspect. A "de minimus threshold" is also expressly included, that limits the applicability of Nachfrist where the unperformed

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41 Bruno Zeller, ‘Buyer's notice fixing additional final period for performance: Remarks on the manner in which the Principles of European Contract Law may be used to interpret or supplement Articles 47 and 49(1)(b) CISG’ (2001) <http://www.cisg.law.pace.edu/cisg/text/peclcomp47.html> Assessed 16 March 2013
46 See Judgment by Oberlandesgericht [Appellate Court] Naumburg, Germany, 27 April 1999, English translation by Jarno Vanto < http://cisgw3.law.pace.edu/cases/990427g1.html>
47 Koch (n 44)
48 Koch (n 44)
obligation is minor.\textsuperscript{49}

Provisions on time limits on avoidance are highly similar. In CISG, under certain circumstances such as late delivery\textsuperscript{50} and other cases of breaches,\textsuperscript{51} buyers may lose the right to avoid within reasonable period if the seller had delivered the goods. Similarly, in cases of late performance\textsuperscript{52} or other breaches\textsuperscript{53} sellers may lose the right to avoid within reasonable period if the buyer had paid the price. The scope in PICC is broader, which in case of late performance or non-conformity right to terminate can be lost unless notice is given within a reasonable time.\textsuperscript{54} Thus it covers late payment, delivery as well as late taking delivery stipulated in CISG. It is substantively identical to the provisions of CISG.

Based on the Anglo-American doctrine of anticipatory repudiation,\textsuperscript{55} Article 72 CISG allows an innocent party to avoid the contract when it is clear before delivery that non-performance or fundamental breach would occur.\textsuperscript{56} Similar provisions are found in CISG for installments.\textsuperscript{57} These provisions can be compared with 7.3.3 and 7.3.4 PICC, which allows termination of agreements prior to the date of performance.

Despite slight differences in wordings,\textsuperscript{58} 7.3.3 PICC resembles Article 72(1) CISG in substance. For avoidance prior to performance, a clear indication of fundamental non-performance must be shown. The most difficult aspect of interpretation refers to the measure of certainty.\textsuperscript{59} Although case law

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\item \textsuperscript{49} Art. 7.1.4 UNIDROIT Principles
\item \textsuperscript{50} Art. 49(2)(a) CISG
\item \textsuperscript{51} Art. 49(2)(b) CISG
\item \textsuperscript{52} Art. 64(2)(a) CISG
\item \textsuperscript{53} Art. 64(2)(b) CISG
\item \textsuperscript{54} Art. 7.3.2(2) UNIDROIT Principles
\item \textsuperscript{55} Sieg Eiselen, ‘Remarks on the manner in which the UNIDROIT Principles of International Commercial Contracts may be used to interpret or supplement Articles 71 and 72 of the CISG’ (2002) <http://www.cisg.law.pace.edu/cisg/text/peclcomp71,72.html> Assessed 28 March 2013
\item \textsuperscript{57} Art. 73(2) CISG
\item \textsuperscript{58} Compare the wordings between Art. 72(1) CISG and Art. 7.3.3 UNIDROIT Principles; Art. 72(1) CISG requires a party “will commit the fundamental breach” while Art. 7.3.3 UNIDROIT Principles only requires that “it must be clear that a fundamental non-performance will take place”
\end{itemize}
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suggested a very high probability is required, both provisions are silent on the meaning of “clear indication”.

In contrast to the strict approach in PICC that notice is not required, CISG takes a more lenient approach, obliging the innocent party to notify its intention to avoid the contract unless the other party has clearly declared not to perform. This approach provides certainty as parties can provide assurance of performance and the adequacy of assurance can be assessed.

In 72(2) CISG the position remains unclear, where failures or refusals to produce adequate security fall into the category of fundamental breach or “clear indication of fundamental non-performance”. There are different opinions between commentators while in one case buyer’s failure to provide adequate assurance was held to satisfy requirements of Article 72. However, 7.3.4 PICC clearly stipulates that failure to provide assurance within reasonable time entitles the other party to terminate.

CISG allows avoidance on parts or installments which does not conform to the contract or has not been delivered at all, provided these non-performing parts amount to fundamental breach. From UNCITRAL case digest, examples of such include failure to deliver promised goods or open a letter of credit; the specific installments were found to be fundamentally defective. While provisions are made for partial avoidance and


60 See Judgment by Landgericht [District Court] Berlin, Germany, 30 September 1992, English translation by Thomas Arntz <http://cisgw3.law.pace.edu/cases/920930g1.html>

61 Art. 72(2) CISG; Art. 73(3) CISG;


64 Eiselen (n 55)


66 Art. 51(1) CISG

67 Art. 73(1) CISG


69 UNCITRAL digest of case law on Article 73 (n 68)

70 UNCITRAL digest of case law on Article 73 (n 68)

71 Art. 3.2.13 UNIDROIT Principles
performance,\textsuperscript{72} PICC has no explicit provisions on partial termination. This may due to PICC recognizes partial performance as a kind of non-performance, which the aggrieved party deserves remedy at maturity of the contract.\textsuperscript{73}

73(3) CISG allows retroactive avoidance, byauthorizing avoidance on past or future installments that are so interdependent with the avoided installment, which no longer serves purposes contemplated by the parties. PICC adopts a prospective approach.\textsuperscript{74} Compared with the retroactive treatment on avoidance,\textsuperscript{75} restitution under termination can only be claimed on future periods.\textsuperscript{76}

Facing the uncertainties in CISG provisions discussed above, opinion no. 5 of CISG-AC provides more insight on fundamental breach. In determining fundamental breach, regard is to be given to the terms of the contract\textsuperscript{77} and the purpose for which the goods are bought.\textsuperscript{78} Parties’ autonomy is respected as it is up to the parties to stipulate what they consider to be essential. From cases, it is likely that fundamental breach arises if the breach concerns certain explicitly agreed features.\textsuperscript{79} Buyers’ purpose of goods bought, such as self-consumption, resale and disposal is important in determining fundamental breaches. Different intended usage of the goods may render different results.\textsuperscript{80} These opinions may account for the lack of precise definitions in CISG and PICC, as much depends on circumstances of each contract.

As to the relationship between cure and avoidance, the blackletter opinion confirms the prevailing views, case law and PICC provisions that no

\textsuperscript{72} Art. 6.1.3 UNIDROIT Principles
\textsuperscript{73} UNIDROIT Principles of International Commercial Contracts Official Commentary on Article 6.1.3, Comment 2
\textsuperscript{74} Florian Mohs, ‘Commentary on the manner in which Articles 7.3.5 and 7.3.6 of the UNIDROIT Principles compare with Articles 81 and 82 of the CISG’ (2004) <http://www.cisg.law.pace.edu/cisg/biblio/mohs.html> Assessed 28 March 2013
\textsuperscript{75} Art. 3.17(1) UNIDROIT Principles
\textsuperscript{76} Art. 7.3.7(1) UNIDROIT Principles
\textsuperscript{77} CISG-AC Opinion no 5, The buyer’s right to avoid the contract in case of non-conforming goods or documents 7 May 2005, Badenweiler (Germany). Rapporteur: Professor Dr. Ingeborg Schwenzer, LL.M., Professor of Private Law, University of Basel. Opinion 1
\textsuperscript{78} CISG-AC Opinion no 5 (n 77) Opinion 2
\textsuperscript{79} CISG-AC Opinion no 5 (n 77) Commentary 4.2
\textsuperscript{80} CISG-AC Opinion no 5 (n 77) Commentary 4.3; See also UNCITRAL digest of case law on Article 49 (n 14) para. 11; UNCITRAL digest of case law on Article 64 (n 42) para. 5
fundamental breach arises if the non-conformity can be remedied without unreasonable inconvenience with weight accorded to time of performance.\textsuperscript{81} Additional costs do not influence fundamental breach \textit{per se}.\textsuperscript{82} The same is provided for documentary sales.\textsuperscript{83} The official commentary emphasizes the purpose of goods to be used, the importance of timely repair and buyer’s ability to repair himself, which is akin to 7.1.4 (3) PICC.\textsuperscript{84} The commentary also follows the view in 7.3.1(c) and 7.3.1(d) PICC that trust is an important factor in determining acceptance of cure.

Special attention is given to documents and commodity trades. For accompanying documents, the buyer may avoid the contract by resorting to the general mechanisms of CISG for fundamental breach,\textsuperscript{85} where in documentary sales clean document is of the essence of the contract.\textsuperscript{86} In commodity markets where prices are subject to considerable fluctuations and string transactions prevail,\textsuperscript{87} it was suggested that special standards have to be applied that timely delivery of conforming documents is essential.\textsuperscript{88} This is in form with the usages pursuant to Article 8 CISG and the treatment on commodity sales is quite similar to the perfect tender rule.

To conclude, despite slight differences in approach, CISG is highly similar to PICC in circumstances regarding avoidance. Therefore, some scholars advocate making use of PICC to interpret ambiguous terms of CISG.\textsuperscript{89} CISG-AC’s opinion may shed light on fundamental breach in specific situations, providing more certainty.

\textsuperscript{81} CISG-AC Opinion no 5 (n 77) Opinion 3
\textsuperscript{82} CISG-AC Opinion no 5 (n 77) Opinion 4
\textsuperscript{83} CISG-AC Opinion no 5 (n 77) Opinion 6
\textsuperscript{84} CISG-AC Opinion no 5 (n 77) Commentary 4.4; 4.5
\textsuperscript{85} CISG-AC Opinion no 5 (n 77) Opinion 5
\textsuperscript{86} CISG-AC Opinion no 5 (n 77) Commentary 4.13
\textsuperscript{87} Ingeborg Schwenzer, ‘The Danger of Domestic Pre-Conceived Views with Respect to the Uniform Interpretation of the CISG: The Question of Avoidance in the Case of Non-Conforming Goods and Documents’ (2005) Victoria University of Wellington Law Review 805
\textsuperscript{88} CISG-AC Opinion no 5 (n 77) Opinion 7; See also Peter Schlechtriem, ‘Subsequent Performance and Delivery Deadlines - Avoidance of CISG Sales Contracts Due to Non-conformity of the Goods’ (2006) Issue No.1, 18 Pace International Law Review 83-98
\textsuperscript{89} Koch (n 44)
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