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The Small Print: Damage Liability
Comparative study on
Article 74 of the CISG and Section 53 of the SGA

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Summary

Since the U.K. after more than 30 years from the CISG's enforcement still has not adopted the Convention, the question arises; how come? Could it be that this partially is due to differences in how the English applicable law and the CISG addresses liability for damages? The objective of this paper is to elucidate the similarities and differences in the two laws, regarding the seller's obligation to pay damages to the buyer for delivering defective goods. This is executed to enlighten what consequences these similarities and differences enclose to commercial actors on the international market when concluding their contracts.

This paper is based on the usage of legal methodology, which means that the information collected for this paper originates from the cornerstones of the regulatory system and the body of legal rules which the CISG respectively the English law is based on.

The differences found do not primarily concern the method of calculation damages although the ambiguous language in the CISG leaves the courts with some flexibility, the main differences are attributable to the limitations to pay damages and what costs may be included in the seller's obligation to recover the buyer's loss. For instance, contrary to the CISG, the SGA does not validate all penalty clauses, and contrary to the SGA, the CISG does not allow for the breaching party to pay for losses caused to physical persons or the losing party to pay for the winning party's litigation expenses.

Commercial actors are faced with the problem that the amount of payable damages differs to a great extent due to the certain circumstances surrounding a specific contract. But if glancing at the information provided in this paper and not digging to deep into it, it might be fair to stipulate that the CISG in relation to the SGA does limit the sum of recoverable damages since it does not allow certain indemnity interests or litigation costs to be included. Additionally, because of the CISG's international character it does leave some discretion to domestic laws, and merchants may have to choose between the legal certainty provided by the English law and the, maybe not so preferable, flexibility offered by the CISG.

Five keywords in this paper: damages, defective goods, article 74, section 53, comparative.

Sammanfattning

Eftersom Storbritannien efter mer än 30 år sedan CISG:s ikraftträdande fortfarande inte har anslutit sig till konventionen, frågan uppstår om varför så är fallet. Kan det vara så att det till en viss del kan bero på skillnader angående hur den engelska tillämpliga lagen ifråga och CISG ställer sig till skyldigheten att betala skadestånd? Syftet med uppsatsen är att klargöra de likheter och skillnader i de två lagarna beträffande säljarens förpliktelse att betala skadestånd till köparen för att ha levererat defekta varor. Klargörelsen är utförd för att upplysa vilka konsekvenser de här likheterna och skillnaderna för med sig till kommersiella aktörer på den internationella marknaden när de sluter avtal.

Till grund för den här uppsatsen är användandet av juridisk metod. Uppsatsen är därmed baserad på information hämtad från de olika hörnstenarna som CISG:s respektive Englands rätts- och regelsystem baseras på.

De skillnader som funnits hänför sig primärt inte till metoden för uträkning av skadestånd, även om det vaga språket i CISG lämnar utrymme till domstolar för flexibilitet, utan den huvudsakliga skillnaden ligger i begränsningarna för att betala skadestånd och vilka kostnader som inkluderas i säljarens förpliktelse att återställa köparens förlust. Till exempel, till skillnad från CISG, giltigförklarar SGA inte alla straffklausuler, och i kontrast till SGA tillåter inte CISG att den kontraktsbrytande parten betalar för skador orsakade på fysiska personer, och inte heller att den förlorande parten ska betala för den segrande partens juridiska kostnader hänförliga till domstolsprocessen.

Kommersiella aktörer stöter på det problemet att skadeståndets summa i stor utsträckning skiljer sig åt beroende på de rådande omständigheterna kring ett särskilt kontrakt. Men efter snabb överblick av informationen utredd i den här uppsatsen, och om man inte gräver för djupt, kan det finnas skäl att stipulera att CISG i relation till SGA begränsar skadeståndet eftersom den inte tillåter vissa ersättningar eller juridiska kostnader att anses som utbetalbara. Dessutom, eftersom CISG internationella karaktär lämnar en viss bestämmanderätt till nationella lagar, medför att handelsmän därför måste välja mellan juridisk säkerhet tillskriven engelsk lag och, den kanske inte så tilltalande flexibiliteten given av CISG.

Fem nyckelord i denna uppsats: skadestånd, defekta varor, artikel 74, section 53, komparativ.

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Abbreviations

[CISG]	[United Nations Convention on International Sale of Goods 1980]
[CPR]	[Civil Procedure Rules]
[SGA]	[Sale of Goods Act 1979]
[WTO]	[World Trade Organisation]

1. Prelude

1.1 Subject/Background

The society we live in today is completely different from the one that was current just 50 years ago. Today we live in a globalised world where the access to information is infinite, no geographical sites are inaccessible, and hardly any goods or merchandise is too far away or too unsuitable to pursue commerce with. Countries and states positive economical growth more often derives from legal persons' commerce with merchandise over territorial barriers and this phenomenon is of enormous importance for our well-being and comfort in today's modern society.

A natural consequence of the free trade is the legal problems enclosed when countries that conduct commerce with each other have different types of legal systems and legal rules concerning trade and sales. This has to some degree tried to get harmonised through for example the WTO and CISG, but since both are founded on voluntarily membership, there are still countries standing outside of these institutions. Sweden has, with some restrictions, incorporated the CISG as its applicable law on international sale of goods¹ when pursuing commerce with countries outside of Scandinavia².

It can accidentally be easy to assume that CISG is more or less always the applicable law on sale of goods with an international character since as many as 76 countries now are adherent to the Convention³, but the fact is that one of the big trading nations have still not ratified the CISG and therefore have other applicable provisions on these sales. The significant nation kept in mind is of course the United Kingdom. Since the UK does pursue a lot of international trading and has a reputation of beings specialists on commercial law and it is of great significance to know if and how its applicable law differs from others, and especially if and how it differs from the CISG which is the law which is most often applicable on international sale of goods in a major part of the world's countries.

One of the important questions for companies conducting international trading is what can be the cost and how much can a possible event of a breach of contract cost in

¹ 1 § Lag (1987:822) om internationella köp

² 2 § Lag (1987:822) om internationella köp

³ 7 July 2010

monetary terms? This is an issue which might be disregarded in some extent, or at least not as illuminated as it should, during the conclusion of contracts. The avoidance of this sensitive question can partially be due to the fact that since the parties of a contract of course has the intentions and motives to comply with their obligations, and accordingly do not want to harm or make their business relationship uncomfortable by bringing questions of damages to the table. But, the importance of legal rules of damages are not avoidable since it can get costly and expensive for the breaching party if they do not have insight or and knowledge about how to guard themselves from foreign and unfamiliar rules that might expand their obligations to pay damages.

1.2 Aim

Since a lot of commercial disputes are brought before English courts⁴, the English courts are known for its expertise in commercial law, and because they have not ratified the CISG, one might wonder why this is? If there now is a unified and harmonised law on international sale of goods, why do commercial disputes seek their way to England? There are surely a number of reasons why this is a fact, but since a lot of disputes are solved in England, maybe there is a difference in the way they deal with approach and the calculation of damages?

The aim of this paper is accordingly to clarify the similarities and the differences in the equivalent damage provisions in the CISG and the English applicable law. An account is to be given to what are the current rules in force in both the English law and in the CISG in regards of damage liability for defective goods. Thus, the two provisions which are the main focus are article 74 CISG and section 53 SGA, which each regulate the calculation of payable damages for defective goods. This is done in order to reach an understanding of how they relate to each other, and what consequences these similarities and differences have when commercial actors conclude their contracts of commerce, i.e. how they should make proper decisions from the perspective of choice of law.

1.3 Problem

This paper will attempt to make a comparative investigation and analysis between the CISG and the applicable English law in regards of their rules concerning damages. Finally, and most important, do commercial actors have to worry about paying largely different amounts of damages if they are in breach of contract when basing a contract on CISG or on English law?

Briefly, the questions this paper will try to answer are:

- 1) What are the differences and similarities in the rules of damages according to CISG and the English applicable law?

⁴ Mullis, Alastair, *Twenty-Five Years on -- The United Kingdom, Damages and the Vienna Sales Convention*; in footnote 6; In at least 50% of the cases before the English courts, one party is not British and in 30% neither is.

2) What are the consequences for commercial actors when faced with this choice of law?

1.4 Method and materials

This paper is based on the usage of legal methodology, which means that the information collected for this paper is based on the regulatory system and the body of legal rules which both the CISG and the English law is based on. Because the legal body of CISG and that of English law differs significantly, the source of materials also differs. The survey of the CISG is based on literature as well as articles of legal science, and some cases concerning disputes about damages are also used as base of information. The common law system which is exercised in the UK addresses a lot of legal power to the precedence of case law, where a lot of elaborated legal rules are found. Therefore, the English case law is the primary source and the usage of legal literature and articles is less extensive than in the survey of CISG. Most of the case law and the articles were found on the internet, where The Pace Law School located in the U.S. has an easily accessible and usable website containing all the scholarly materials necessary for an academic writing about the CISG. Because this paper does not concern Swedish law, most of the relevant materials are written in English. All the relevant cases are selected as they were recurrently mentioned in both articles and literature.

1.5 Demarcations

This paper will only bring attention to the sale of goods, therefore contracts on sale of services or other subjects fall outside of the scope of this paper. The choice of law for this paper is restricted to the CISG and the equivalent applicable English law; the SGA. I will furthermore in this paper only consider damages payable due to the seller's failure to deliver goods which comply with his obligations, i.e. breach of warranty. Also, throughout the paper, the survey and analysis will be based on the assumption of the continuation of the contract, and any legal rules concerning damages when a contract has been avoided goes beyond the interest of this paper. Breaches referable to any other obligations, such as delays or non-delivery, will not be given an account for. The paper will be written from the perspective that the seller is the party in breach of his obligation, and the buyer will therefore be the aggrieved party, and in order to not cause any confusion they will be referred to as 'the promisor' respectively 'the promisee'.

1.6 Disposition

In the paper's second chapter, an account will be given for the application of the current legal rule in the CISG concerning payable damages due to breach of contract; namely the article 74. The third chapter will give a survey of the equivalent legal rule in English law; section 53 of the SGA, or, if you like, the rules set out in the case of *Hadley v Baxendale*, which is the predecessor to section 53. Subsequently, the fourth chapter will try to

analyse the similarities and the differences between the provisions in the two laws. Finally, a conclusion will be produced in the fifth chapter where the possible consequences for commercial actors will be addressed.

2. Article 74 CISG

2.1 INTRODUCTION

The CISG is a binding agreement or contract between nations which establishes a set of rules governing certain aspects of the making and performance of commercial contracts between sellers and buyers who have their places of business in different countries. By adopting the CISG, a nation accepts that it overrules the national sales code or sales law.⁵ Without a doubt, CISG has been one of the more successful international instruments produced. Few other commercial law conventions have attracted as many adherents, and it has had a considerable impact internationally on the reform of sales and contract laws.⁶ In addition, it should be recognised that one of the goals of the CISG is that the results of the cases decided under the CISG will be harmonised.⁷

2.2 FREEDOM OF CONTRACT

As an introduction to the following survey, it should first be remembered that the principle of freedom of contract is a general legal rule with international spread, and that it is also applicable on contracts based upon the CISG⁸. According to this rule, the parties to a contract on international sale of goods have the freedom to set aside the provisions of the CISG, entirely or partially, and to design their own clauses regarding warranty of the goods as well as the terms setting out the extension of damages⁹. And since the intention of the parties to a contract takes priority before the provisions of the CISG, these parties may agree on a minimum or maximum sum for the payable damages, or any other method of calculating damages as they wish to use. In addition, the CISG does not eliminate the possibility for the parties to agree upon a penalty clause, which owns the

⁵ Article 1 CISG

⁶ Mullis, *Twenty-Five Years on -- The United Kingdom, Damages and the Vienna Sales Convention*; under part I

⁷ Murphy, Arthur G. Jr., *Consequential Damages in Contracts for the International Sale of Goods and the Legacy of Hadley*; under 'Conclusion'

⁸ Article 6 CISG

⁹ Which is probably more often the case, rather than not

function of both providing compensation and to act as prevention in the sense that it is to be perceived as a threat.¹⁰

Now, after making clear that there are no legal provisions¹¹ hindering the parties from agreeing upon a tailor-made contract, I will furthermore not bring this any more attention since this paper is written from the perspective that the relevant legal provisions are enforceable upon the contracts of sale. This is concluded either by the parties in an adherent country neglecting their possibility to form a contract, or by utilizing the establishment of the freedom of contract and agreeing on a choice of law as to be applicable on their contract. This privilege can be described as the core of this paper since its survey poses a foundation for deciding on a choice of law.

2.3 APPLYING ARTICLE 74

If the goods referred to a specific sale do not comply with the agreed specifications in that contract, the promisor is in breach of article 35 CISG, which clarifies in what way goods are to be considered defective. The provision of article 36 furthermore explains that the promisor is to be held liable for his non-conformity to his obligations in accordance with the contract and article 35.¹² The amount of damages which the breaching party is liable for, and how it is calculated, is to be found in article 74 of the CISG;

Article 74 CISG: "Damages for breach of contract by one party consist of a sum equal to the loss, including loss of profit, suffered by the other party as a consequence of the breach. Such damages may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a possible consequence of the breach of the contract."

Apart from the basic rule in article 74, the CISG contains only a few provisions concerning the assessment of loss, namely those in article 75 and 76. But those two articles can only be used if the contract has been avoided¹³. The rule set out in article 74 appears fairly abstract, but is formulated that way for a reason; the article is applicable for damages by both buyer and seller which may arise from a wide range of situations, therefore a flexibility is preferred in order for the courts to calculate the loss in a manner which best suits the circumstances in each case.¹⁴

¹⁰ Schlechtriem, Peter, *Commentary on the UN Convention on Contracts for the International Sale of Goods (CISG)*, 3rd ed., p. 572

¹¹ Except for limitations as to public policy

¹² Article 45(1)(b) CISG also enforces a general right for the buyer to claim damages for the seller's breach of contract or any of his obligations under the CISG

¹³ See articles 75 and 76 CISG; "If the contract is avoided(...)"

¹⁴ Secretariat Commentary, *Guide to CISG Article 74*; paragraph 4

While being granted this flexibility, when calculating the payable damages to the aggrieved party, the courts must calculate the damages pertaining to article 74 by taking the CISG's international character and unificatory purpose into account. It furthermore gives the courts the opportunity to apply proven principles of domestic law in their calculation, only if they correspond with approaches in other legal systems (e.g. common law system vs. civil law system) and observe the principle of good faith in international trade in accordance with article 7(1) of the CISG.¹⁵

2.3.1 BASIC PRINCIPLE

The CISG lacks a separate provision for breach of warranty, and the opportunity to claim damages through article 74 is a general remedy which is basically available to a party whenever there has been any objective breach of a contract.¹⁶ Although, its enforcement cannot be claimed if the promisee has successfully exercised another remedy within CISG and thereby wholly or partially redressed his loss¹⁷, and the article additionally requires the continuation and performance of the contract as a whole, as mentioned above. This article provides for full compensation to the promisee when an obligation based on the CISG has been breached by the promisor, which means that the promisee is entitled to damage for both the loss suffered and the loss of profit. In general terms, the promisee has a right to be fully compensated for all disadvantages he suffers as a result of the promisor's breach of contract.¹⁸

To establish those suffered losses, a comparison has to be made between the situation the promisee finds himself in due to the breach of contract and to the situation he would have been in if the contract had been correctly performed.¹⁹

In the second sentence of article 74 CISG, the important general limitation to damages is found. This principle is based on the presumption that the party in breach of the contract is liable to recover for a breach of warranty regardless of whether or not it is his fault.²⁰ Article 74 merely requires that the loss be foreseeable by the party in breach; the liability for the promisor to pay damages is limited to the loss which he foresaw or ought to have foreseen at the time of the conclusion of the contract. This prerequisite has to be considered in the light of the circumstances of which he then knew or ought to have known, as a possible consequence of the breach of the contract. Accordingly, this principle's purpose is to limit a party's liability to those inherent risks assumed by the conclusion of the contract.²¹ When applying this rule when interpreting a clause which has been breached in a contract, according to article 6 of the CISG, the precedence is

¹⁵ Schlechtriem, p. 556

¹⁶ Schneider, Eric C, *Measuring Damages under the CISG*

¹⁷ Schlechtriem, p. 555

¹⁸ *Sapphire International Petroleums Ltd. v. National Iranian Oil Co.*

¹⁹ Murphy, *Consequential Damages in Contracts for the International Sale of Goods and the Legacy of Hadley*;

²⁰ Schlechtriem, p. 554

²¹ Op. cit., p. 554-555

given to the express or implied intentions of the parties when defining that clause. This must be interpreted as that the promisor can only escape liability by proving that his failure to perform was caused by an impediment beyond his control which he neither could have taken into account when concluding the contract nor have avoided or overcome.²²

As shown above, article 74 provides for damages for loss, including loss of profit, suffered as a consequence of a breach of contract. But neither the article nor the CISG itself define in more detail which are the losses able to be fully compensated. More important is the fact that the purpose of a contract may find the promisee entitled to compensation of general, not precise sum of monetary compensation. The reasonable limitation of liability for compensation is not to be achieved by using a restrictive interpretation of 'loss', but by using the foreseeability rule, while at the same time taking into account the specific purpose of the contract.²³

2.3.2 CALCULATION OF LOSS

Under article 74, the promisee is entitled to be compensated for the value of his contractual expectation which ended up unrealized, in order to receive the benefit of the bargain. This is often measured by "the difference between the value to the aggrieved party of the performance that should have been received and the value to that party of what was actually received".²⁴

The wording of article 74 makes it clear that the basic philosophy of the action is to place the aggrieved party in the same economic position he would have been in if the contract had been performed. If the promisee receives defective goods, the loss suffered might be measured in a number of different ways. If the promisee is able to cure the defect, his loss would often equal the cost of the repairs²⁵. If the goods delivered were to be used in a production process, his loss might also include the loss resulting from lowered production during the period the defective goods could not be used. Even if the loss cannot be exactly calculated, it can only be recovered if it can be shown that the lack of the goods in the promisee's business has led to appreciable difficulties. Furthermore, if the defective goods had a recognized value which fluctuated, the loss to the promisee would be equal to the difference between the value of the goods as they exist and the value the goods would have had if they had been as obliged in the contract.²⁶ A stricter test is to be applied when applying the foreseeability of a promisee's loss of goodwill or costumers as a result of a delivery of defective goods. Although opinions are divided, the promisor is

²² Schlechtriem, p. 555

²³ Op. cit., p. 558

²⁴ CISG-AC Opinion No. 6, paragraph 3.1

²⁵ *OGH, 14 Jan., 2002; Nova Tool and Mold Inc. v. London Industries Inc; AG Mchen, 23 June 1995; Delchi Carrier S.p.A. v. Rotorex Corp.*,

²⁶ Secretariat Commentary, paragraph 7

as a rule liable for such loss of goodwill only if, at the time of the conclusion of the contract, the promisee pointed out the risk of that particular loss.²⁷

When a breach of contract has occurred and the promisee suffers loss, the amount of damage must basically be calculated in a way where only actual and definable losses are taken into account.²⁸ The liability to pay damages may not exceed the damage as been properly calculated: it must not result in a profit for the promisee. The CISG furthermore does not recognise a liability to pay restitutionary damages intended to diminish the profits which the promisor has gained through his breach of contract. The principle of full compensation of loss also justifies an approach of taking into account any advantages which the breach of contract brings to the promisee. This principle is implicit in article 74²⁹: the party entitled to damages does not suffer a 'loss' to the extent that the breach of contract also confers advantages on him which counterbalances the detriment he suffered.³⁰

Article 74 gives no indication of the time and place at which 'the loss' to the aggrieved party is to be calculated, but presumably it should be at the place the promisor delivered the goods and at an appropriate time, such as the moment the goods were delivered, the moment the promisee learnt about the non-conformity of the quality of the goods, or the moment it became clear that the defective goods would not be remedied by the seller.³¹ In the case of calculation it is logical for the calculation to be carried out as late as possible so that all relevant losses can be acknowledged, which naturally makes the date of judgement to be the relevant date. All consequences of loss are to be considered when calculating, both those which have occurred and also those which the court is convinced are yet to occur.³²

The recoverable losses explained above are sometimes referred to as the expectation interest which includes damages that have to satisfy the advantages associated with the performance of the contract; hence, the relief is to protect the promisee's expectation of full performance³³. Furthermore, a breaching party may also be held liable for the indemnity interest which is used to describe the interest a promisee has in avoiding damage to life, health, and property, thus the rights which he enjoys irrespective of the contract.³⁴ But, in the context of the CISG, a promisee's indemnity interest is limited to the avoidance of loss to property since article 5 explicitly states that a promisor can never be "(...)liable for death or personal injury caused by goods to any person".

²⁷ Schlechtriem p. 571

²⁸ Op. cit., p. 565

²⁹ Op. cit., p. 566

³⁰ Blase, Friedrich and Höttler, Philipp (2004) *Remarks on the Damages Provisions in the CISG, Principles of European Contract Law (PECL) and UNIDROIT Principles of International Commercial Contracts (UPICC)*

³¹ Secretariat Commentary, in footnote 2

³² Schlechtriem, p. 566

³³ Lookofsky, Joseph, *Article 74 Damages for Breach*; in part C

³⁴ Schlechtriem, p. 553

Article 74 does not explicitly say to what extent the aggrieved party must prove that he suffered a loss in order to recover damages. There have been discussions whether this is implicitly addressed by the CISG or whether this is a procedural issue to be resolved according to domestic applicable law³⁵. The latter has been rejected in the light of the need of uniformity under the CISG due to its international character, and the aggrieved party therefore bears the burden of proving with ‘reasonable certainty’ that he suffered loss as a result of the promisor’s breach of contract. Aligned with this, he also has the burden to proof the extent of damages, but does not need to do so with any mathematical precision.³⁶

2.3.3 LIMITATION

The party in breach of a contract is obliged to pay damages to the other party for loss caused by the breach of the contract, while it being irrelevant whether the damage was caused directly or indirectly by the breach.³⁷ Although that rule seem to endlessly extend the breaching party’s liability for paying damages, the promisor have the possibility of relying on the limitation enforced by the foreseeability rule.³⁸

The foreseeability rule in the second sentence of article 74 is the tool which to limit the promisor’s liability for damages. For the limitation to be taken into account, it is sufficient that the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract that the loss was a ‘possible consequence’ of the breach. But because there are difficulties in determining exactly what is foreseeable, this is not a precise rule and it is important to supplement the rule by considering the purpose and intention of the contract and all the other relevant circumstances surrounding the conclusion at the time of calculation.³⁹

The foreseeability rule in the CISG extends the liability of the party in breach by making him liable also for losses which he did not foresee, but which a reasonable person, a *bonus pater familias*, in his position would at the time of the conclusion. Though, this also enables liability to be restricted on the basis of the same principle. For example, if the particular circumstances of a contract show that the parties did not intend the contract to cover certain losses, in which case, even if they were actually foreseen by the party in breach or at least subjectively foreseeable, those losses fall outside his sphere of responsibility.⁴⁰ However, as an indication of what is ‘ought to have foreseen’, a *bonus pater familias* generally only considers the possibility of loss only with regard to developments which are not entirely unexpected.⁴¹

³⁵ *Delchi Carrier S.p.A. v. Rotorex Corp.; Helsingin Hovioketus*, 26 Oct. 2000; *Bezirksgericht der Saane*, 20 Feb. 1997; *ICC Court of Arbitration*, 23 Jan. 1997

³⁶ CISG-AC Opinion No .6, paragraphs 2.6 and 2.9

³⁷ Schlechtriem, p. 554

³⁸ Op. cit., p. 554-555

³⁹ Op. cit., p. 567

⁴⁰ Op. cit., p. 568

⁴¹ Op. cit., p. 567

The foreseeability of the loss is to be considered from the promisor's point of view at the time of the conclusion of the contract, taking into account the circumstances of which he was or ought to have been aware. Awareness of a possible risk of loss may be attributable from a reference by the other party. However, such awareness of circumstances which indicate a risk of an extraordinary loss flowing from the breach, which are communicated to the promisor after the conclusion of the contract, but before the breach, does not expand his liability of damages. A loss is foreseeable within the meaning of article 74 if the risk that has actually materialised is essentially the same as the risk which was foreseeable at the time of the conclusion of the contract. In general, it is not essential for liability that the party in breach could have foreseen the precise amount of the loss which has occurred. Moreover, if the extent of the loss considerably exceeds what was foreseeable, then, accordingly, a risk of loss has materialised which is different from the risk which was foreseeable at the time of conclusion.⁴²

Also, general factors, such as market conditions, may change after the conclusion of the contract, but those changes are part of the contractual risk assumed by the promisor at the time of the conclusion.⁴³ In sales of goods the fact that there are price fluctuations is well known and hence a promisor could only avoid payment of damages in cases where the price fluctuation has been unforeseen and so unusual that it could not have been foreseen by the party. Only where the increase of such an extraordinary amount that no one could reasonably have expected it, might the application of article 74 be justified to limit the loss.⁴⁴

This rule of limitation has a great relevance in regard to the limitation of recovery for consequential losses, including loss of profit. Such losses depend on the promisee's particular circumstances, the arrangements he has made, or the surrounding economic framework, and he has expected to mitigate his loss⁴⁵. The principle of '*bonus pater familias*' applies here as well, which in general means that these losses are recoverable only if the promisor knew of the relevant circumstances or if a '*bonus pater familias*' would. As a rule, the promisor is obliged to compensate a loss of profit which the promisee could have made on a resale of the goods if the contract had been properly performed, only where the promisor should have foreseen the resale. If the promisor sells tradable goods to a merchant or to an undertaking of such sort that would use the goods in its production process, the promisor is always regarded to have foreseen a loss of profit even if there were no other positive indications of a resale at the time of the conclusion of the contract.⁴⁶

In order for the promisee to recover full compensation, he is obliged to mitigate his loss in an appropriate manner. He is assumed to "take such measures as are reasonable in the

⁴² Schlechtriem, p. 569

⁴³ Op. cit., p. 570

⁴⁴ Zeller, Bruno, *Commodity Sales and the CISG*; under 'Non-delivery and Damages'

⁴⁵ Article 77 CISG

⁴⁶ Schlechtriem, p. 570

circumstances” in order to successfully claim damages. If he fails to mitigate his losses resulting from the breach, including loss of profit, the promisor may claim a reduction in the damages equal the sum the promisee should have mitigated.⁴⁷ In terms of the promisee’s obligation to mitigate his loss, this duty obligates him to mitigate with what would amount to a ‘reasonable step’. However, this should not be judged purely objectively, but be determined by taking into account the circumstances of which the promisee was aware, and it does not force him to take any measures which are unreasonably expensive.⁴⁸

2.4 LITIGATION EXPENSES

Article 74 does not explicitly address the payment of litigation expenses incurred by an aggrieved party in connection with seeking relief for the breach of contract. Although the principle of full compensation appears to support the promisee’s right to be recovered for litigation expenses in order to make him ‘economically whole’, such an interpretation is overruled by the principle of equality between sellers and buyers in articles 45 and 61⁴⁹. The ability to recover damages under article 74 is grounded on a breach of contract; thus, a successful respondent will not be able to recover its legal expenses if the claimant has not committed a breach of contract. To interpret this article in such way to create unequal recovery of damages between buyers and sellers is contrary to the intention of the CISG. However, article 74 does not preclude a court or likewise from awarding a party its litigation expenses when the parties utilized their freedom of contract and incorporated a clause for their payment in the contract.⁵⁰

⁴⁷ Article 77 CISG

⁴⁸ Schlechtriem, p. 570

⁴⁹ Which provide the general rights for the buyer resp. the seller to exercise his rights against the breaching party

⁵⁰ CISG-AC Opinion No. 6, paragraph 5.4

3. Section 53 SGA

3.1 INTRODUCTION

The predecessor to the SGA in force today was the Sale of Goods Act 1893. As originally drawn, it “endeavoured to reproduce as exactly as possible the existing law, leaving any amendments that might seem desirable to introduce in Committee on the authority of the legislature”. Substantial changes were in fact made during its passage through Parliament, so that the resulting enactment represented partly a rewording of existing law in ordered form and partly a departure from common law rules of sale. The Sale of Goods Act 1979, which replaced the 1893 Act and amending legislation, is a pure consolidation measure.⁵¹

3.2 FREEDOM OF CONTRACT

Parties who are free to create their own contractual obligations are also free to define the extent of the obligations which they have undertaken and to specify the consequences of a breach of those obligations. Thus contracting parties are free to agree on a maximum sum of damages for which the promisor will be responsible to pay in the event of a breach of contract.⁵² Though, this freedom of contract is not without restrictions. Not only will courts disallow contract clauses which infringe the criminal or civil law, or that are otherwise contrary to public policy or morals; they will also not enforce penalty clauses which to an extent are substantially divergent from the loss likely to be suffered as a result of the breach,⁵³ or clauses which exclude liability for the consequences of their own fraud⁵⁴. Any other restrictions on the freedom of contract are imposed by equity and by statute.⁵⁵

⁵¹ McKendrick, Ewan, *Goode on Commercial Law*, 4th ed, p. 205

⁵² Bridge, Michael, *Benjamin's Sale of Goods*, 8th ed, p. 980

⁵³ McKendrick, p. 104

⁵⁴ *S Pearson & Son Ltd v Dublin Corpn*

⁵⁵ McKendrick, p. 104

3.3 APPLYING SECTION 53

In contrary to the CISG, the SGA contains no specific section which defines a general rule of damages. Thus, it is spread and attached to the particular breach it concerns. As described in the prelude of the paper, the main focus is to clarify the contemporary situation regarding the promisor's obligation to pay damages to the promisee for delivering goods which are not complying with the contract in question. In this case I am to examine section 53 of the Sale of Goods Act which holds the explicit obligation and limitation to pay damages where a breach of warranty of quality has occurred. All breaches of contract give rise, in the absence of special provisions, to actions for damages, whether the contract subsists or is avoided.⁵⁶ Although, within the frames of this paper, where an examination of s.53 of the SGA is the main focus, I will no further explore the territory of damages in the case of an avoided contract since s.53 assumes the continuation of the contract of sale.⁵⁷

S. 53 SGA: Remedy for breach of warranty.

(1) Where there is a breach of warranty by the seller, or where the buyer elects (or is compelled) to treat any breach of a condition on the part of the seller as a breach of warranty, the buyer is not by reason only of such breach of warranty entitled to reject the goods; but he may—

(a) set up against the seller the breach of warranty in diminution or extinction of the price, or

(b) maintain an action against the seller for damages for the breach of warranty.

(2) The measure of damages for breach of warranty is the estimated loss directly and naturally resulting, in the ordinary course of events, from the breach of warranty.

(3) In the case of breach of warranty of quality such loss is prima facie the difference between the value of the goods at the time of delivery to the buyer and the value they would have had if they had fulfilled the warranty.

(4) The fact that the buyer has set up the breach of warranty in diminution or extinction of the price does not prevent him from maintaining an action for the same breach of warranty if he has suffered further damage.

⁵⁶ *Johnson v Agnew*

⁵⁷ Section 11(4) SGA

3.3.1 BASIC PRINCIPLE

Section 53(3) is stated to be the measure of damages for breach of warranty as to the quality of the goods, *viz* the goods do not comply with the standards agreed upon in the contract of sale.⁵⁸ This subsection is not often applied on its own because there may be consequential losses or injuries caused by the defective goods, in respect of which the promisee may also be claiming damages. The Court of Appeal emphasised in the *Hadley v Baxendale*⁵⁹ case the importance of section 53(2) to be exercised where the *prima facie* rule in section 53(3) should not be applied if the damages entitled to the promisee exceeds his true loss.⁶⁰

The explicit reading of section 53(3) refers to the difference in value between what the goods ought to have been worth if they had complied with the contract and what they in fact were worth at the time of delivery. Thus, it does not as such mention the market and it is not compulsory to use market values to determine the value difference although it is a common used reference.⁶¹

Because the issues of fixing the market value of the goods is similar to those existing in the case of damages for non-acceptance in s. 50(3) and non-delivery in s. 51(3), the cases on market value decided under these subsections should be applicable to the interpretation of s. 53(3).⁶² As previously mentioned, if s. 53(3) does not apply because there is no available market, the courts have to apply the general principle in s. 53(2).

Whenever a legal institution is to calculate damages they ought to consider as the liability for the breach stems from the contract, the extent of the promisor's liability should reflect the losses which it may fairly be presumed the promisor has agreed to bear.⁶³ In determining the extent of the promisor's liability for damages, the English courts have ever since 1854 been guided by the principles set out in the very influential case of *Hadley v. Baxendale*⁶⁴. Judge Baron Alderson stated:

"Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e. according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it. Now, if the special circumstances under which the contract was actually made were communicated by the

⁵⁸ Bridge, *Benjamin's Sale of Goods*, p. 1073

⁵⁹ *Hadley v Baxendale*

⁶⁰ Bridge, *Benjamin's Sale of Goods*, p. 1076

⁶¹ Bridge, Michael, *The Sale of Goods*, 2nd ed., p. 807

⁶² Bridge, *Benjamin's Sale of Goods*, p. 1076

⁶³ *Transfield Shipping Inc v Mercator Shipping Inc*

⁶⁴ *Hadley v Baxendale*

plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated. But, in the other hand, if these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances, from breach of contract.”

In the context of contracts of sale of goods, it has been said that the relevant section 53 is, among other sections of the SGA, a codification of the rule in *Hadley v Baxendale* and should be so interpreted.⁶⁵

Damages for breach of contract are designed to emulate what the promisee would have received if the promisor had performed his obligations. Hence, he is, as to in an economic context, to be placed in the same position as if the contract had been performed.⁶⁶ Thus, the purpose of damages in contract is to award the aggrieved party the value of his defeated contractual expectation, which gives him a right to be compensated not only for the expenses caused by the breach but also for the profits prevented by it. In addition, it consequently follows that if the promisee suffered no loss, he only has a right to nominal damages even if the promisor has profited from the breach.⁶⁷

3.3.2 CALCULATION OF LOSS

As the explicit meaning of the rule in section 53(3) for breach of warranty, the usual measure of damages is the difference between: 1) the value of the goods if they complied with the obligation, measured at the time and place of the delivery; and 2) the actual value of the goods, in their actual condition, at the same time and place.⁶⁸

In the absence of evidence as to the determination of the market value of goods which comply with the description and quality in the contract of sale, some courts have taken the contract price as the "value" of the goods⁶⁹. But the correct measure according to s. 53(3) is the value "at the time of delivery to the buyer", which should be used when it is shown to be different from the contract price.⁷⁰ The price at which the promisee had previously resold the goods is normally irrelevant to the ascertainment of their value at the time of delivery to the promisee, but in the absence of other evidence, the price at which a sub-buyer had agreed to buy the goods from the promisee before the defect was discovered

⁶⁵ *Parsons (Livestock) Ltd v Uttley Ingham & Co Ltd*

⁶⁶ *Robinson v Harman*

⁶⁷ Bridge, *The Sale of Goods*, p. 808

⁶⁸ Bridge, *Benjamin's Sale of Goods*, p. 1075-1076

⁶⁹ *Dingle v Hare; Minster Trust Ltd v Traps Tractors Ltd*

⁷⁰ Bridge, *Benjamin's Sale of Goods*, p. 1023

may be some evidence of their market value, as may the price at which an offer for the goods was made by a third person.⁷¹ Although, this is only true if the terms of the resale are substantially similar to those in the original sale⁷².

Section 53(3) speaks of the value of the goods "at the time of delivery to the buyer". In a case decided before the SGA 1893⁷³, the promisee received defective goods, but since the market price of the goods had risen at the time of his resale, he did not suffer much loss because the resale price was nearly equal to the contract price. The promisee was entitled to the rise in the market price between the contract and the delivery, and it was stated as irrelevant the price at which the promisee had actually resold the goods at a date later than the date of delivery. This approach of determining the time of which the damages are to be calculated, is clearly acceptable in the terms of section 53(3). And furthermore, if there were separate deliveries, the measure of damages in section 53(3) should be applied separately to each delivery.⁷⁴

In accordance with section 34 of the SGA, the promisor is bound to give the promisee the opportunity to examine the goods at the time of delivery. But, under the circumstances where this is not preferable because the promisor knows the goods are to be resold to another place and the goods are therefore packaged, the examination of the goods will not be taken place until the goods have reached the sub-buyer. The date at which this "postponed" examination is performed may be the date at which the market price should be taken to assess promisee's damages for the defective condition of the goods.⁷⁵

Section 53(3) lays down only a *prima facie* rule, from which the court may depart in appropriate circumstances⁷⁶. Where the market value of the defective goods cannot be ascertained, because there was no available market in which they could be disposed of, damages may be awarded on the basis of the cost of bringing the goods up to the contractual standard which would make them saleable⁷⁷.

Where it was within the reasonable contemplation of the parties that a defect in the delivered goods bought by the promisee was not unlikely to cause loss of, or damage to, other property belonging to him, his damages may include compensation for this loss or injury.⁷⁸ Physical injury to the promisee or his family is also recoverable if it was in the reasonable contemplation of the parties, at the time of concluding the contract, that the promisor's breach of warranty was not unlikely to cause that type or kind of injury.⁷⁹

⁷¹ *Grébert-Borgnis v J&W Nugent*

⁷² *Harlow and Jones Ltd. v Panex (International) Ltd.; Lazenby Garages Ltd. v Wright*

⁷³ *Jones v Just*

⁷⁴ *Slater v Hoyle and Smith Ltd*

⁷⁵ *Van den Hurk v Martens (R) & Co Ltd; Kwei Tek Chao v British Traders Ltd*

⁷⁶ *Bence Graphics International Ltd v Fasson UK Ltd*

⁷⁷ *Minster Trust Ltd v Traps Tractors Ltd; Mondel v Steel; Zuvella v Geiger*

⁷⁸ *Borradaile v Brunton; Randall v Newson; Wilson v Rickett Cockerell & Co Ltd; Parsons (H) (Livestock) Ltd v Uttley Ingham & Co Ltd*

⁷⁹ *Gedding v Marsh; Morelli v Fitch & Gibbons; Andrews v Hopkinsons*

3.3.3 LIMITATION

The SGA 1979 lays down the basic principle for limitation of damages, which also derive from the significant case of *Hadley v Baxendale*⁸⁰. But in subsequent case law⁸¹ it is indicated that the extent of a promisor's liability for damages should be calculated in terms of the kinds of losses to which it may fairly be presumed the promisor would have contemplated⁸² and which reflected the presumed intention of the parties⁸³. This is the reason why, in the absence of agreement to the contrary, damages are limited to those which may fairly and reasonably be considered as arising naturally according to the usual course of things⁸⁴.

Where special circumstances are communicated to the promisor, the assumption is generally that he undertakes to bear the special loss which is referable to those special circumstances⁸⁵, as it is usually reasonable to infer that the promisor accepts responsibility for the special losses because he has the opportunity to limit his liability when getting informed of the special circumstances.⁸⁶ Lord Hoffman in the case *Transfield Shipping Inc v Mercator Shipping Inc* stated that it was logical that liability for damages is found upon the intentions of the parties because contractual liability was voluntarily undertaken. The liability for damages is limited to events that are to be considered as presumable in ordinary circumstances.⁸⁷

Moreover, the promisee's damages will be assessed on the basis that he should have acted reasonably in mitigating his loss⁸⁸. If there is no available market for the goods in their condition, the promisee is entitled to deal with the goods "in any reasonable way", for example to adapt them to suit another customer. The promisee's damages will then include the cost of the adaption, as well as the loss of profit on the first sale.⁸⁹ However, in these circumstances, the question arises whether the promisee is not only entitled to, but is obligated, under his "duty" to mitigate, to spend money to adapt the goods to make them suitable for resale.⁹⁰

Also, where the promisee claims damages for his loss of profit or other consequential damages caused by the defective quality of the delivered goods, the promisor may show that the promisee ought reasonably to have mitigated his loss by acquiring substitute

⁸⁰ The main proposition can be read in the first half of the quoted paragraph of *Hadley v Baxendale* above.

⁸¹ *Transfield Shipping Inc v Mercator Shipping Inc*

⁸² *Victoria Laundry (Windsor) v Newman Industries*

⁸³ *Transfield Shipping Inc v Mercator Shipping Inc*

⁸⁴ Section 53(2) SGA

⁸⁵ *Jackson v Royal Bank of Scotland*

⁸⁶ Bridge, *Benjamin's Sale of Goods*, p. 981

⁸⁷ Op cit., p. 993

⁸⁸ *Gebrüder Metelmann GmbH & Co KG v NBR (London) Ltd.*

⁸⁹ *Vic Mill Ltd, Re*

⁹⁰ Bridge, *Benjamin's Sale of Goods*, p. 1023

goods⁹¹, although it is useful to point out that this is a question of fact and depending on the circumstances of the particular case whether the promisee acted reasonably⁹².

Even though the promisee may not have a duty to mitigate his loss in this way, when his action had in fact diminished the loss, his claim for damages for the cost of, for example, installing the substitute goods must take account the extra profit, including the saving of expenses, resulting from this action⁹³. Accordingly, if this extra profit exceeds the cost of the substitute, the promisee cannot recover the cost. The decision to substitute the goods is not rarely considered to be a reasonable action which quite naturally arises out of the circumstances in which the promisee is placed by the breach of the contract.⁹⁴

3.4 LITIGATION EXPENSES

The regulation regarding litigation expenses is not to be found in the SGA, but by section 44.3(1) CPR. This provision confers a general discretion to the courts to decide which party is to pay for litigation costs. The general principle is that the losing party will be ordered to pay the costs of the successful party. However, this is not imperative, and the court can make a different rule when it considers all the circumstances of the case. The main circumstances contemplated by the courts are the conduct of the parties before and during the proceedings, and whether the party was only partially successful.⁹⁵

⁹¹ Bridge, *Benjamin's Sale of Goods*, p. 1080

⁹² *Op. cit.*, p. 1054

⁹³ *Erie County Natural Gas and Fuel Co Ltd v Carroll*

⁹⁴ Bridge, *Benjamin's Sale of Goods*, p. 1054

⁹⁵ McKendrick, p. 1292

4. Differences and Similarities

4.1 INTRODUCTION

Of course, the clearest difference between the CISG's provision on damages for defective goods and the English equivalence is the system of law it is based on. The CISG is an international convention and is accordingly a compromise of different legal systems and different approaches to certain legal principles. The CISG is in the regards of damages for contractual breaches more complying with the civil law system rather than the common law system which is the base of English law.

The English rely on the system of common law. This system differs from the civil law system, which is used in Sweden for instance. Practisers of common law rely on the judges in their courts to develop precedence law using case law as a tool for this, rather than exercising law through coded statutes as do practisers of civil law.

4.2 FREEDOM OF CONTRACT

The discussions in this paper are premised on the assumption that the parties have not chosen some other remedy or remedies within their contractual relationship. As has been given account for in previous chapters, both the CISG and the SGA give the parties the authority to determine in their contract all of the remedies to which they will enforce upon breach⁹⁶. While the SGA recognises the same general concept of freedom of contract, which is a fundamental aspect of English contract law, the scope of the equivalent provision in the SGA, in comparison to the CISG, is somewhat narrower.⁹⁷

Under the CISG, there is no limit on the amount of compensation that may be agreed to be paid upon breach of a contract. In contrast, English common law draws a distinction between genuine pre-estimates of damage (referred to as "liquidated damages") versus clauses viewed as penal.⁹⁸ Penalty clauses which are imposing a sum too great considering the actual circumstance are considered invalid and will not be enforced by an

⁹⁶ Article 6 CISG resp. section 55(1) SGA

⁹⁷ Piliounis, Peter A. (1999) *The Remedies of Specific Performance, Price Reduction and Additional Time (Nachfrist) under the CISG: Are these worthwhile changes or additions to English Sales Law?*; under part 3

⁹⁸ Op. cit.

English court.⁹⁹ So while the parties are generally free to choose their own remedies, English law will not enforce all of the remedies, at least not to the same degree.

Although the CISG does give the parties the freedom to choose their own remedies, it is not necessarily clear that these remedies will be enforced the same way in every country, if at all. Whether a damages clause was enforced would likely depend on whether penalty clauses were considered a question of validity under article 4 of the CISG or whether the freedom of choice granted by article 6 overrode article 4.¹⁰⁰ Some commentators have suggested that whether a particular predetermined damages clause is unenforceable as a penalty clause is based in public policy and therefore a question of validity of the particular clause.¹⁰¹ Under such an analysis, the parties' freedom of choice would be overridden by the applicable (domestic) law in some jurisdictions, but not others.¹⁰²

So, although both laws do acknowledge the fundamental principle of freedom of contract, its application in English law is somewhat more restricted than in the CISG. The similarities coincide in the way that both laws allow the parties to claim their free choice of law and to deviate from the specific provisions set out in each statute. The differences appear in consideration of the use of penalty clauses in the contract. As the English law regards some penalty clauses as invalid, the CISG does not.

4.3 CALCULATION OF LOSS

The *Hadley* rule, which is the predecessor to section 53, like article 74 of the CISG, may be described as "a general rule for the calculation of damages for every loss suffered as a consequence of a breach of contract."¹⁰³ Relief to the promisee is to be measured by his expectation, sometimes called "the benefit of the bargain," and the attempt is therefore to put him in the position in which he would have been had the contract been performed.¹⁰⁴

The method of calculation the damages attributable to the promisor's breach of contract concerning defective goods does not differ in the two laws. Although this is generally the truth, differences may illuminate. There is no question as to the method used in the SGA, but, since the ambiguous language in article 74 grants courts flexibility in regards of determining the amount of payable damages, a different outcome is not impossible. With

⁹⁹ McKendrick, 104

¹⁰⁰ Piliounis, *The Remedies of Specific Performance, Price Reduction and Additional Time (Nachfrist) under the CISG: Are these worthwhile changes or additions to English Sales Law?*; under part 3

¹⁰¹ Farnsworth, E. Allan, *Damages and Specific Relief*; under 'First Tenet; Relief'

¹⁰² Piliounis, *The Remedies of Specific Performance, Price Reduction and Additional Time (Nachfrist) under the CISG: Are these worthwhile changes or additions to English Sales Law?*; under part 3

¹⁰³ Murphy, *Consequential Damages in Contracts for the International Sale of Goods and the Legacy of Hadley*; under part II

¹⁰⁴ Farnsworth, *Damages and Specific Relief*; under 'Introduction'

that being said, the risk of differences should not outshine the fact that the general interpretation of article 74 is in accordance with the method expressed in section 53.¹⁰⁵

Both laws typically measures damages by using the market value which entitles the aggrieved party of the benefit of which he has been deprived through the breach, or by using the costs of reasonable measures to bring about the situation that would have existed if the contract had been properly performed. Accordingly, both recognize the full compensation of loss of profit and any other expenses incurred on the promisee in connection with the breach of contract.

In regards of applying the CISG, a court may find it difficult to estimate the amount of compensatory damages, that is, the additional cost to the promisee of substitute goods, the difference in value between the contract goods and the available substitutes, and any other losses caused by the breach. This risk of error by the judges is particularly acute in cases involving international sales, because identical products are not common in the international market. If a promisor has breached, for example, and the promisee is unable to find an exact substitute, then the court must estimate any difference in value to the buyer between the original contract item and the closest substitute. Numerous types of product differentiation are likely. Purchases from alternative suppliers may for example come with reduced warranties, less brand name recognition, or diminished quality. The diminution in value caused by these differences is difficult to prove with certainty and difficult for a court to evaluate.¹⁰⁶

The time variables used for calculating damages, *viz.* the time for determining what is foreseeable or contemplated, is the same time in the CISG as that set out in the *Hadley* rule, and therefore there is no room left for discussion about possible differences.

4.4 LIMITATION

Since the intention of this paper is to investigate if the amount of payable damages for defective goods differs when applying article 74 of the CISG or section 53 of the SGA, a focus on the rule of limitation is undeniable.

The award of damages should not include compensation for loss that could not reasonably have been foreseen by the party in breach at the time he made the contract¹⁰⁷, according to article 74. On the contrary, the wording used in the *Hadley* case, which section 53 is a codification of, is “in the contemplation of both parties”. Accordingly, the limitations referable to respective provision differs in two ways in relation to each other. First, the CISG adopts the word ‘foreseeable’ as to limit liability for damages, while SGA uses “in the contemplation”. Secondly, the CISG only imposes the breaching party with

¹⁰⁵ CISG-AC Opinion No. 6

¹⁰⁶ Kastely, Amy H., *The Right to Require Performance in International Sales: Towards an International Interpretation of the Vienna Convention*; under part I.A

¹⁰⁷ Farnsworth, *Damages and Specific Relief*; under ‘Introduction’

the requirement to have foreseen the loss, but the SGA implies that both parties to a contract had a future possible loss in the contemplation. The language in article 74 reflects the view that the focus should be on the party who will have to answer for the amount of the loss. No case has been found in which recovery was denied because the injured party did not foresee the loss.¹⁰⁸ This gives an indication that the different wording, in this regard, in the two provisions does not suggest a different outcome in comparison to each other.

The choice of "foresaw" and "ought to have foreseen" instead of Hadley's "in the contemplation of the parties" is especially significant in light of English cases. For example in a particular case¹⁰⁹, Lord Denning found it difficult to draw a distinction between the word "foreseeable" and "contemplated", and question is if a choice between the two would make a difference in the scope of liability. A plain reading of the words suggests that a difference is intended; under Hadley, the damages must actually be "contemplated" and not merely "foreseeable." Thus, a rule that provides that damages only need to be "foreseeable" surely, in comparison, ought to narrow the limitations of Hadley and therefore widen the scope of recovery. Indeed the House of Lords in *The Heron II*¹¹⁰, thought that such a term would do so and explicitly rejected the word "foreseeable", in favour of the "contemplation" test. The reason was that "foreseeable" was the test for damages in torts, not breaches of contract, and that "foreseeable" was a different concept from "contemplated." When *The Heron II* rejected the use of "foreseeable", it adopted an English rule which makes it less likely that the promisor will have to pay damages, holding that if "foreseeable" and "in contemplation of" are measures of result, cases under article 74 should provide more favourable recoveries.¹¹¹

The foreseeability rule is set out in the second sentence of article 74 which provides that the damages recoverable "may not exceed the loss which the party foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known as a possible consequence." Thus, not only will the party in breach be liable for any loss which he actually foresaw as a possible consequence of his breach, but he will also be liable for consequences which he ought, as a reasonable person, to have foreseen. The practical effect of this provision is thus two-fold. First, it imposes liability on the defendant for what one might call the usual, possible consequences of breach, that is to say: the consequences of which the party in breach ought to have been aware given the nature and purpose of the contract he had entered into, the business or trade in which the parties operated, and any other matter which ought to have been known by a reasonable person in his position. Secondly, it has the effect of imposing liability for 'unusual' risks where the party in breach was aware of

¹⁰⁸ Murphy, *Consequential Damages in Contracts for the International Sale of Goods and the Legacy of Hadley*; under part VII(a)

¹⁰⁹ *Parsons (Livestock) Ltd. v Uttley Ingham & Co.*

¹¹⁰ *Koufos v Czarndnikow (C) Ltd (The Heron II)*

¹¹¹ Murphy, *Consequential Damages in Contracts for the International Sale of Goods and the Legacy of Hadley*; under VII(c)

those risks, usually no doubt because these were drawn to his attention by the other party.¹¹²

The wording of the CISG is undoubtedly more favourable to promisees than is English law. The case of *Hadley* uses the wording of the requirement that the loss must have been 'not unlikely' to occur, or a 'serious possibility'. The CISG requires only that the loss must have been foreseeable as a 'possible consequence' of the breach.¹¹³

Furthermore, any advantages and profits the promisee gains due to the promisor's breach must be subtracted from the damages he is entitled to, according to both the CISG¹¹⁴ and the SGA¹¹⁵.

The award of damages should not include compensation for loss that might reasonably have been avoided by the promisee.¹¹⁶ This rule of mitigation in regards of breach of contract applies to the promisee in accordance with both the CISG¹¹⁷ and the SGA¹¹⁸, and there should be no way in which they would bring different results when limiting the payable damages to the promisee.

The recoverable damage for the promisee's indemnity interests in the CISG clearly differs from the regulation in English law. The CISG does not under any circumstances allow the breaching party to be responsible for death or injury caused to physical persons.¹¹⁹ According to the CISG, the promisor can only be liable for injury to property caused by his defective goods. Though, the rule of limitation must apply, and he is therefore only obliged to pay damages for injuries he reasonably could have foreseen at the time of the conclusion of the contract. This principle deviates from the one in force in English law. The promisor is to be held liable for all injuries caused by his defective goods, whether it is injury to property or physical persons, if he reasonably could have contemplated the injury when concluding the contract.¹²⁰

4.5 LITIGATION EXPENSES

Differences in the laws are also found in regards to the obligation to pay for litigation expenses. The English approach usually points out the losing party as the one to pay for both party's attorneys' fees and litigation costs, and leaves discretion for the courts to

¹¹² Mullis, *Twenty-Five Years on -- The United Kingdom, Damages and the Vienna Sales Convention*; under part II.2

¹¹³ Op. cit., in footnote 47

¹¹⁴ Blase, and Höttler, *Remarks on the Damages Provisions in the CISG, Principles of European Contract Law (PECL) and UNIDROIT Principles of International Commercial Contracts (UPICC)*; under part 3(a)

¹¹⁵ *Erie County Natural Gas and Fuel Co Ltd v Carroll*

¹¹⁶ Farnsworth, *Damages and Specific Relief*; under 'Introduction'

¹¹⁷ Article 77 CISG

¹¹⁸ *Gebrüder Metelmann GmbH & Co KG v NBR (London) Ltd.*

¹¹⁹ Article 5 CISG

¹²⁰ *Gedding v Marsh; Morelli v Fitch & Gibbons; Andrews v Hopkinsons*

decide what amount is fairly to be paid. On the contrary, CISG does not impose an obligation for any party to pay litigation expenses for the other party, whether they win or lose.

5. Conclusion

A contract could specify, for example, that the parties choose to be governed by the SGA rather than the CISG. The aim of this paper was to clarify to commercial actors if this actually is preferable in regards of the damages provisions of breach of warranty. After having conducted a comparative analysis of the two laws' perspective on damages for defective goods I can with certainty say that when it comes to designating one law as preferable over the other; it depends. As always.

Since one law does not have a clear advantage over the other, commercial actors have to take all the similarities and differences into consideration and from there make proper decision in their choice of law. One law does not unconditionally impose a greater risk of a large amount of payable damage, than the other in the case of a breach of contract.

For instance, the principle of freedom of contract is given more scope in the CISG than in the English law since CISG does not regard penalty clauses as invalid. If a contract is not negotiated to one's advantage, a penalty clause can be costly.

As to the method of calculation, the choice of law should not give effect to great differences since both laws generally apply the same method. The method at use might differ if choosing the CISG as applicable law, because the courts are free to amend their method of calculation as to fit domestic law. Hence, the country in which the court is situated is of great importance. Obviously, this ambiguity and uncertainty in application rather than resulting in a consistent legal regime can be seen either as an advantage or a disadvantage. Although, commercial trade involves different considerations and raises fundamentally different concerns for the contracting parties, and certainty, it is thought, is what traders and business people want and English law gives them that certainty.¹²¹ But since the same method generally is used, the amount of payable damages should only differ in regards of their different wording in their rules of limitation. The difference between 'foreseeable' and 'in contemplation' might only appear to be of a semantic matter, but the language does indicate on different limitations, and the risk of paying a larger amount of damages seems to be apparent to the CISG. These differences between the CISG and the English approach are due to one main factor; the CISG has been

¹²¹ Mullis, *Twenty-Five Years on -- The United Kingdom, Damages and the Vienna Sales Convention*; under part I

especially designed for international sales.¹²² As opposed to SGA, CISG does not allow for a breaching party to pay damages for injuries caused to physical persons. Hence, a party delivering defective goods clearly suffers a risk of paying a greater amount of damages if applying English law on their contract, rather than if they used CISG.

In the regard of litigation expenses, it is difficult to say which law is preferable since the payable sum could differ tremendously. If using CISG as the applicable law, one is responsible for their own costs, but if choosing English law, one might pay nothing, for both parties, or for something in between.

If the given information in this paper is to be looked at objectively, it is not without difficulty that a commercial actor has to make his decision on which law to choose to be applicable on his contract of sale. Because the advantages differ a lot due the circumstances in each case, an observation of these must be made in order to make the right decision.

As a final remark on the rule of limitations, the CISG does appear to grant the promisee damages for defective goods a bit easier than does the SGA. Since the losses limited to be recoverable are similar, the difference in limitation is due to the different language used in their provisions.

¹²² Williams, Alison E. (2002) *Forecasting the Potential Impact of the Vienna Sales Convention on International Sales Law in the United Kingdom*; under part IV.C

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