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Precontractual Damages as a Result of an Irrevocable Offer – A Resolution Within the CISG

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Precontractual Damages as a Result of an Irrevocable Offer – A Resolution Within the CISG

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ABSTRACT

This paper is written in response to the arguments that have been put forward by Anne Rossen, Maria Pedersen, and Thomas Neumann, titled “How far does the dynamic doctrine go? Looking for the basis of precontractual liability in the CISG”. On the backdrop of this paper, it is worth noting that the United Nations Convention on Contracts for the International Sale of Goods (CISG) is one of the most successful international commercial law treaties ever devised. It has been ratified by most of the world's important trading countries and has become a template for the drafting of commercial law treaties. The CISG is considered a self-executing treaty, as it creates a private right of action in federal court under federal law. It provides the default set of rules that govern contracts for the sale of goods between parties located in different Contracting States. In some cases, the CISG also addresses situations in which only one of the parties is located in a Contracting State.

This article argues that the CISG can accommodate breaches of precontractual conditions through the same procedure applied to breaches of contract. It is a controversial issue but, nevertheless, it is arguable that the CISG can cover the internal gap via general principles embedded within its four corners. For this reason, this article will look at Article 16(2). In particular, the following issues will be relevant: the revoking of an irrevocable offer; the effects of Article 4; and the effects of Articles 71-77.

1. INTRODUCTION

This paper is written in response to the article “How far does the dynamic doctrine go? Looking for the basis of precontractual liability in the CISG?”, by Anne Rossen, Maria Pedersen and Thomas Neuman.² Therefore, two preliminary points need to be raised in relation to article 16. First, article 16(2), once applied, creates a situation of reliance. Secondly, the UNCITRAL Principles (UPICC), in the 2016 edition, note that article 2.1.4 has been directly copied from the CISG. The comment points to the core problem of article 16 and, hence, article 2.1.4, UPICC, by noting that there is no prospect of reconciling the civil and common law divide on this issue. Thus, the main rule is included, followed by the

² Anne Rossen, Maria Pedersen, Thomas Neuman, ‘How far does the dynamic doctrine go? Looking for the basis of precontractual liability in the CISG?’ [2020] *Nordic Journal of Commercial Law* 1.

exception.³ It follows that there is a strong argument to suggest that, in retaining the article, UPICC must have recognised its importance and usefulness, and has seen the need to harmonise the law on this issue. This importance is highlighted by the fact that the differences among underlying legal traditions are, on this issue, irreconcilable.

Another issue is relevant. Namely, the argument presented by Rossen *et al* that “*it would be wrong to let the CISG expand in scope and to reintroduce such issues into the CISG. Expanding the scope of the CISG to encompass precontractual liability may, therefore, be ‘overstepping the spirit of the international consensus’*”⁴

Two points are to be made. Firstly, Article 7(2) “*itself implies, by referring to general principles on which the Convention is based, that it is admissible to go beyond the text itself*”.⁵ The second point to be made is that, though international consensus is the driving force in the construction and interpretation of the CISG, many issues, such as penalty clauses and the interpretive methodology in article 8 are not based on consensus. Rather, many principles are either based on common law or civil law. Hence, a choice had to be made. Consensus is not the issue; it is harmonisation of sales laws which is the important point. Comments made by Kastely in 1988 are still important. Namely: “*The text of the Convention seeks to establish, in short, a rhetorical community in which readers first assent to the language and values of the text itself, and then use language and values to inform their relations with one another*”.⁶

UPICC is clearly demonstrating that assent to values as contained in the text leads to harmonisation of transnational contract law. The text of UPICC also demonstrates that harmonisation is the aim of drafting a transnational instrument. Consensus between transnational law instruments is only possible through harmonisation. Therefore, whenever possible, issues must be decided within the CISG and the otherwise governing domestic law must be the last resort. After all, consensus is a compromise between different views, which is the point in the debate on article 16. Hence, the consensus must be CISG-based and not civil or common law-based, which, in the execution, produces different results.⁷

³ UNIDROIT Principles 2016, International Institute for the Unification of Private Law, 39.

⁴ Rossen *et al* *How Far* (n 2) 10.

⁵ Gert Brandner, *Admissibility of Analogy in Gap-filling under the CISG*, <http://cisg.law.pace.edu/cisgbiblio/brandner.html> (accessed 4 June 2020).

⁶ Amy Kastely, ‘Unification and Community: A Rhetorical Analysis of the United Nations Sales Convention’, [1988] *Northwestern Journal of International Law and Business* 574.

⁷ Rossen *et al* *How Far* (n 2) 11-12.

The ideal outcome of any business negotiations should be the successful completion of a contract. However, not all negotiations culminate in the creation of a binding contract. Business negotiations can be classified into three stages:

*The first stage involves preliminary negotiations in which each party feels free to withdraw, the second stage in which agreement 'in principle' has been reached, and the third where that agreement often being expressed in a 'letter of intent' and a stage in which the contract is complete.*⁸

The question is: at what stage do legal obligations arise? Two points are clear. First, no legal obligations are expected to arise in the stage of preliminary negotiations. Second, once the third stage is reached - that is, a contract is completed -, a legal relationship has been concluded. However, at the second stage - where the parties anticipate the signing of a contract and all activities are directed towards the performance of the intended economic activity, the matter becomes unclear.⁹ The problem is that “[...] *the parties are no longer strangers to each other as presumed by tort law, nor are they parties to a contract which contract law requires to trigger all the rights and duties [...]*”.¹⁰

Rossen *et al*, in their excellent paper, argue that “*the Convention is generally not able to deal with all situations of precontractual liability as the legal grounds for allowing it is too erratic. For situations not covered by Art. 16, one must therefore rely on the otherwise applicable domestic law.*”¹¹ This paper argues that the CISG does cover this issue, as the solution is to be found in the application of the general principle of recovery of damages.

Moreover, it is undisputed that, in general, the issue is one of the legal treatments of an offer. There is no doubt that legal obligations arise once an offer is made. The CISG, in Part II, sets out requirements in relation to an offer in articles 14 to 18. In essence, the rule of the CISG is that an offer, once accepted, generates the legal obligations of a contract. It also clearly regulates the issues surrounding the validity of an offer - that is, either acceptance or revocation. Article 16(2)(a), however, treats an irrevocable offer differently. Simply put, it can only be revoked by the

⁸ Michael Spence, *Protecting Reliance: The Emergent Doctrine of Equitable Estoppel*. (Bloomsbury, 1999) 83.

⁹ Bruno Zeller, *Protecting Reliance: Equitable Estoppel and the CISG – a Comparative Analysis* [2007] 9 *European Journal of Law Reform* 4, 641.

¹⁰ Ingeborg Schwenzer, Pascal Hachem and Christoffer Kee, *Global Sales and Contract Law* (Oxford University Press 2012) 275.

¹¹ Rossen *et al* *How Far* (n 2) 31.

buyer, either through rejection or lapse of time. The seller, during the stipulated period, is bound by the offer.

An interesting problem arises when the buyer, during the fixed period of the offer, incurred costs in preparation of the acceptance or rejection as the case might be. If the buyer rejected the offer, that would be the end of the matter, but if the seller withdraws the offer, a problem does arise. Namely, the seller is in breach of article 16 - revoking an irrevocable offer. The question of damages is now an issue. However, it must be noted that it is obvious that, if no damages have accrued, there is only a moral breach, which is not discussed in this paper. Nonetheless, as Malik noted already in 1985, this issue is a controversial one. The controversy arises from the fact that

*“The issue is treated in a different manner in different legal systems. In some legal systems (e.g., English) an offer is generally revocable, while in some others (e.g., German and Swiss) it is irrevocable. To further complicate the issue there are number of countries whose legal systems evidence a middle course between revocability and irrevocability of offers (e.g., French, and U.C.C. to a certain extent).”*¹²

Nonetheless, Article 16 of the CISG has accepted the compromise rule on the issue of irrevocable offers. The issue, therefore, concerns what will happen if an irrevocable offer has been revoked. It is clear that there is a breach, as a rule has been broken. The simple point is that the very inclusion of article 16 produces a situation where a right has been created and no remedy has been provided. More importantly, one fact that is indisputable has been outlined by Malik, who argues the revocation of an irrevocable offer is a legal nullity. Hence, “[t]he offeree may ignore the ‘revocation’ and communicate his acceptance to conclude the contract and in the event of non-performance, proceed to claim damages”.¹³ Therefore, the “nullity” is founded on the fact that article 16(2) mandates that the offer cannot be revoked. The fact that the offeree is entitled to accept the offer is thus undisputed.

The alternative is that the buyer might not wish to conclude the contract for whatever reasons he might have but, rather, sue on the breach of article 16. It will be argued that, because of the two choices a buyer has, both must be governed by the CISG and not the otherwise governing law. The question in this case regards how an aggrieved party can seek redress,

¹² Shahdeen Malik, Offer: Revocable or Irrevocable. Will Art. 16 of the Convention on Contracts for the International Sale Ensure Uniformity? (<http://www.cisg.law.pace.edu/cisg/biblio/malik.html>) (accessed 2 June 2020).

¹³ Malik (n 14).

specifically if they have incurred losses, such as preparation of plans for the installment of a machine. The problem of how damages can be obtained within the CISG or whether the matter must be resolved by the otherwise governing law is the first issue to be resolved. The otherwise governing laws are only applicable if there is a gap in the CISG or if the CISG explicitly excluded its application. “*Given the invitation to courts to fill in the gaps in the CISG by reference to its underlying principles and to interpret its provisions in a manner that promotes good faith in international trade, this leaves open the possibility that such terms could be construed quite broadly.*”¹⁴ Hence, the problem which needs to be overcome is whether article 4 along with articles 71 to 77 are applicable.

The buyer, in essence, has incurred the losses in good faith. A comparative solution was offered by the Supreme Court in Denmark. The court elicited a general principle found not only in article 16(2)(b) but also in cases where the seller rejected a valid fundamental breach, thereby giving weight to the fact that the issue of damages extends beyond breaches of contract, also touching upon precontractual issues. The court noted:

*But as the seller had unjustifiably refused to accept the buyer's avoidance, the buyer was entitled to revoke its avoidance in accordance with CISG general principles, articles 7(2) and 16(2)(b) CISG. The buyer was then entitled to repair the machine and recover damages for the expenses incurred, article 74 CISG.*¹⁵

Professor Lookofsky, in his editorial remarks, referred to the comments of Professor Schlechtriem, who noted:

*“Professor Schlechtriem has persuasively argued that the ‘matter’ of whether a declaration of avoidance is binding upon the declaring party is “governed but not settled” by the Convention and that “estoppel,” a CISG general principle, can be used to ‘settle’ it.”*¹⁶

The question, therefore, is whether the expectation interest which can be recouped under article 74 is unquestionably applicable also in cases of precontractual breaches. As noted above, in common law, a party can

¹⁴ Donald J. Smythe, “The Road to Nowhere: Caterpillar V. Usinor and Cisc Claims by Downstream Buyers against Remote Sellers”, 2 Geo. Mason J. Journal of International Commercial Law, (2011) 143.

¹⁵ Djakhongir Saidov, Research Handbook on International and Comparative Sale of Goods Law, <https://iicl.law.pace.edu/cisg/case/denmark-h%C3%B8jesteret-supreme-court-denmark> (accessed 2 June 2020).

¹⁶ Saidov (n 17).

rely on the principle of equitable estoppel. However, as Schlechtriem noted, “estoppel” is a general principle under the CISG, it is important to understand in brief the meaning of estoppel in common law. The importance is that Schlechtriem certainly did not have in mind that common law estoppel is to be used in CISG cases. No doubt, he merely referred to a principle which has no actual ‘name’ in the CISG but, for simplicity sake, can be referred to as having the same effect as the common law estoppel. This paper therefore will provide a brief analysis of the common law principle of equitable estoppel in part II, followed by part III, where the applicability of the CISG in relation to governing precontractual liability is discussed. Part IV will conclude the paper.

2. EQUITABLE ESTOPPEL - A BRIEF ANALYSIS

Simply put, equity supplements the common law, providing a separate and distinct body of principle that mitigates its rigours. In *Legione v Hateley*,¹⁷ Mason and Deane JJ identified three general classes of estoppel: estoppel of record, estoppel of writing, and estoppel in pais, which they described in the following terms:

“Estoppel in pais includes both the common law estoppel which precludes a person from denying an assumption which formed the conventional basis of a relationship between himself and another or which he has adopted against another by the assertion of a right based on it and estoppel by representation which was of later development with origins in Chancery. It is commonly regarded as also including the overlapping equitable doctrines of proprietary estoppel and estoppel by acquiescence or encouragement”.¹⁸

However, Brennan J stated the problem in the following way:

*“...the unconscionable conduct which gives rise to the equity [is] the leaving of another to suffer detriment occasioned by the conduct of the party against whom the equity is raised.”*¹⁹

Spence, in essence, noted four conditions which must be established before a party can rely on estoppel. First, a representation is made; second, the aggrieved party relies on the representation; third, the party is worse off. Fourth, it would be unconscionable for the representor to go back on

¹⁷ *Legione v. Hateley* 1983 152 CLR 406. High Court of Australia.

¹⁸ *Legione v. Hateley* 1983 152 CLR 406. High Court of Australia, [430].

¹⁹ *Waltons Stores (Interstate) Ltd. v. Maher* (1988) 164 CLR 387, at 427. Australian High Court.

his promise without compensation.²⁰ Of interest is the decision in *Verwayen*, where the court noted that a promissory estoppel is also “applicable to parties in a pre-contractual relationship.”²¹

In this context, *British Steel Corporation v. Cleveland Bridge and Engineering Co Ltd*²² is also of interest. The facts are simple. An engineering company was asked to fabricate steel constructions suitable for a building. The plaintiffs were iron and steel manufacturers. The defendant, Cleveland Bridge, approached the plaintiff to produce a variety of cast-steel nodes for the project. Cleveland Bridge subsequently sent a letter of intent to the plaintiff, British Steel. In that letter, they indicated that a contract was to be concluded. The terms to be agreed upon were included in the defendant's standard form contract. Furthermore, Cleveland Bridge requested British Steel to commence work immediately, “pending the preparation and issuing to you of the official form of sub-contract.”²³

Goff J noted:

*“In most cases, where work is done pursuant to a request contained in a letter of intent, it will not matter whether a contract did or did not come into existence, because, if the party who acted on the request is simply claiming payment, his claim will usually be based on a quantum meruit, and it will make no difference whether that claim is contractual or quasi-contractual.”*²⁴

There was no formal contract concluded but, in this case, the defendant insisted on the manufacture of nodes. Arguably, the fact that work was done either with the knowledge or implied knowledge of the defendant would not have made any difference. Hence, by analogy, the situation could have been the same as under article 16.

Two arguments are possible. First, as Spence observed, a claim for precontractual performance was successful because the court assumed that there was an implied contract collateral to the one which was the subject of the negotiations.²⁵ The second argument is based on the fact that compensation is possible, as it relies on a contract-like doctrine which

²⁰ Michael Spence, *Protecting Reliance: The Emergent Doctrine of Equitable Estoppel* (Bloomsbury, 1999). chapters. 2 & 3.

²¹ *Commonwealth v. Verwayen* (1990) 170 CLR 394, [454].

²² *British Steel Corporation v. Cleveland Bridge and Engineering Co Ltd* [1984] 1 All ER [504].

²³ *British Steel Corporation* [504].

²⁴ *British Steel Corporation* [510].

²⁵ Michael Spence, (n 22) 90.

is concerned with fulfilling the parties' reasonable expectations.²⁶ The expectation is founded on the principle of quasi-contracts:

*“The court will look at the true facts and ascertain from them whether or not a promise to pay should be implied, irrespective of the actual views of intention of the parties at the time when the work was done, or the service rendered.”*²⁷

Arguably, the CISG does not include a principle of quasi-contract, as, first, the principle of consideration is not part of the CISG, and, second, article 8 would resolve the issue of the actual intent of the parties. The argument is best put by the Federal District Court [New York] noting:

*“The fact that Article 16(2)(b) appears to employ a modified version of promissory estoppel suggests that if a plaintiff were to bring a promissory estoppel claim to avoid the need to prove the existence of a ‘firm offer’, that claim would be pre-empted by the CISG. The CISG establishes a modified version of promissory estoppel that does not appear to require foreseeability or detriment, and to apply an American or other version of promissory estoppel that does require those elements would contradict the CISG and stymie its goal of uniformity”.*²⁸

A further US case²⁹ demonstrates the difficulty in deciding the issue of whether equitable estoppel once pleaded ought to be entertained when there is a breach of article 16. In the end, the court decided to follow *Geneva Pharmaceuticals Tech. Corp* and in maintaining that the CISG will deal with the issue and not *Caterpillar, Inc. v. Usinor Industeel*.³⁰

Based on the above and in summary, it is clear that the CISG can only govern business relationships which are founded on a contractual relationship. This is made abundantly clear in article 4 and 71 to 77. By the same token, it can also be seen that the CISG, in essence, embraces the general thought behind equitable estoppel – namely, the principle of good faith as noted in article 7(1) – and, arguably, the reasoning behind article 16 in the CISG and article 2.1.4 in the UNIDROIT Principles

²⁶ Spence (n 27) 90.

²⁷ *William Lacey (Hounslow) Ltd., v. Davies*, [1957] 2 All E.R. 712, at 718.

²⁸ *Pharmaceuticals Tech. Corp. v. Barr Labs. Inc* Nos. 98 Civ. 861 (RWS) and 99 Civ. 3607 (RWS), (S.D.N.Y. Sep. 27, 2002)

²⁹ *Asia Telco Technologies v. Brightstar Int'l Corp.* U.S. District Court for the Southern District of Florida, 15-20608-Civ-Scola.

³⁰ *Caterpillar, Inc. v. Usinor Industeel* 393 F. Supp. 2d 659, (N.D. Ill) [676].

(UPICC). A powerful argument, as advocated by Schlechtriem,³¹ is that the CISG, through the notion of good faith, has embedded into the convention that unconscionable conduct in any form results in a breach and is governed by the CISG unless explicitly excluded. In other words, if a particular issue is not explicitly excluded, the starting point of any discussion or analysis must be that the CISG governs the issue. Any discussion must also be aware of the requirements set out in article 16(2) which states

*"reflects the judgment ... that in commercial relations, and particularly in international commercial relations, the offeree should be able to rely on any statement by the offeror which indicates that the offer will be open for a period of time."*³²

3. ARTICLE 16 - THE DISCUSSION

To start with, it is interesting to note that Honnold predicted that article 16 of the CISG would lead to an interpretation challenge. He pointed to the crucial issue – namely, that the CISG certainly governs the revocation of offers but, because the CISG only governs breaches of contracts, the remedies available under the CISG only pertain to breaches of contract and not breaches of article 16.³³

Not surprisingly, some academics argue that any damage emanating from a breach of article 16 is outside the sphere of the CISG. The criticism was based on a Russian arbitral decision where the court stated:

*"in accordance with Article 7 CISG and the requirements of 'observance of good faith in international trade' the international arbitration practice has concluded to apply to contracts for international sales the Anglo-American principle of estoppel."*³⁴

Although this decision is dated, it was not a correct application of the CISG, as it is established - and contained within Article 7 - that

³¹ See Schlechtriem in Schlechtriem & Schwenzer, Commentary, Art. 27, para. 14; accord Müller-Chen, *id.*, Art.45, para. 15(bb).

³² Secretariat Commentary cmt.
<http://www.cisg.law.pace.edu/cisg/text/secomm/secomm-I 6.html> (accessed 5 June 2020).

³³ John Honnold, Uniform Law For International Sales under the 1980 United Nations Convention (Kluwer Law and Taxation Publishers, 1991), 212.

³⁴ Russia, Tribunal of International Commercial Arbitration at the Russian Federation Chamber of Commerce and Industry, Case No 302/1996, 27 July 1999, <http://cisgw3.law.pace.edu/cases/990727rl.html> (accessed 5 June 2020).

domestic principles cannot be applied to a contract governed by the CISG. This was confirmed in *Caterpillar v Usinor Industeel*,³⁵ where the court stated that "*the CISG pre-empts Plaintiff's UCC and promissory estoppel claims only if such claims fall within the scope of the CISG.*"³⁶ The crucial issue in the CISG always hinges around the intent of the parties, bringing article 8 into play. The question is whether the influence of Article 8 can be extended to include the interpretation of precontractual duties. Considering that Article 8 requires the parties to be aware of their intentions, a contract is not only interpreted in an objective fashion but also with the subjective intent of the parties in mind. Thus, certain pre-contractual duties must be drawn within the sphere of application of the CISG.

Schlechtriem argues that pre-contractual duties compel the parties to disclose relevant information to each other; specifically, matters which pertain to conditions or conformity of goods.³⁷ That said, it can be argued that article 8 only comes into play if Article 16(2)(b) is pleaded - that is, if an implied time is fixed. However, with the increased use of the CISG, a mature view of the ability and breadth of application of the CISG has been developed. This paper rejects the idea that the drafting history carries weight in the interpretation of the CISG, as if it were essentially "frozen in time". Rather, the CISG is a living document³⁸ and moves with the time. With the increased use and practical experience, new insights are gained, "*therefore, what the drafters discussed may generally carry little weight when assessing the understanding and extent of good faith*"³⁹, and other relevant sources must be consulted."⁴⁰ Hence, a look at the problem - using sources within the CISG - of article 16 needs to be examined again.

³⁵ *Caterpillar, Inc. and Caterpillar Mexico, S.A. v. Usinor Industeel, Usinor Industeel (U.S.A.), Inc. and Leeco Steel Products, Inc.*, US Dist Ct (Illinois), 30 March 2005, <http://cisgw3.law.pace.edu/cases/050330ul.html>, CISG-online No 1007.

³⁶ *Ibid.*

³⁷ P. Schlechtriem, 'Intro to Arts. 14-24', in P. Schlechtriem & I. Schwenzer (eds.) *Commentary on the UN Convention on the International Sale of Goods (CISG)* (Oxford University Press, 2005), para 6b.

³⁸ Bruno Zeller, 'The Observance of Good Faith in International Trade' in André Janssen and Olaf Meyer, *CISG Methodology* (Sellier. European law publishers, 2009) 138.

³⁹ *Ibid.*

⁴⁰ Rossen et al *How Far* (n 2) 16.

3.1. ARTICLE 16

The starting point needs to be Article 16 which states:

(1) Until a contract is concluded an offer may be revoked if the revocation reaches the offeree before he has dispatched an acceptance.

(2) However, an offer cannot be revoked:

(a) if it indicates, whether by stating a fixed time for acceptance or otherwise, that it is irrevocable; or

(b) if it was reasonable for the offeree to rely on the offer as being irrevocable and the offeree has acted in reliance on the offer.

As far as irrevocable offers are concerned, Article 16 is usefully divided into two segments. First, subsection (2)(a) notes that an offer cannot be revoked if it states a fixed time for acceptance. The offeror does not need to do this expressly but, rather, his intent to be bound can be deduced from the circumstances relevant to the interpretation of the offer and, particularly, from his setting a fixed period during which the offer is open (Article 16(2)(a)).⁴¹ Secondly, the offer also cannot be revoked if “it was reasonable for the offeree to rely on the offer as being irrevocable and the offeree has acted in reliance on the offer.”⁴² It is obvious that the words “cannot be revoked” denotes a right and, hence, it also requires remedies to safeguard that right. The provision is designed to cover those cases in which not just the offer itself but other conduct by the offeror or the special circumstances and exigencies of the proposed transaction enable and necessitate the offeree's presumption that the offer would be valid for a certain length of time, such as when calculations or cover transactions had to be and actually were made.

The starting point is the seminal case of *Geneva Pharmaceuticals v. Barr Labs. Inc.*⁴³, which ruled specifically on article 16(2)(b). The court noted that “Commentary on the CISG has not specifically addressed the issue

⁴¹ Ibid.

⁴² Article 16(2)(b).

⁴³ *Geneva Pharmaceuticals Technology Corp. v. Barr Laboratories, Inc.*, U.S. District Court for the Southern District of New York, May 2002 Case no./docket no.99CIV3607(RWS).

of whether it should preclude a claim for promissory estoppel.”⁴⁴ In addition, a commentary by Henry Mather was noted, namely:

*“Paragraph 2(b) looks very much like American promissory estoppel doctrines, although it does not expressly require that the offeree's reliance must have been foreseeable to the offeror and does not expressly require that the offeree's reliance be detrimental. Despite these omissions, we can expect that many tribunals will apply paragraph 2(b) in much the same fashion as American courts have used promissory estoppel”.*⁴⁵

The problem with this observation was that it encouraged the homeward trend which is specifically disallowed in Article 7. However, the court recognised the error and stated:

*“The CISG establishes a modified version of promissory estoppel that does not appear to require foreseeability or detriment, and to apply an American or other version of promissory estoppel that does require those elements would contradict the CISG and stymie its goal of uniformity”.*⁴⁶

The subparagraph (2)(b) must be read in conjunction with article 8, establishing that the intentions of the parties will determine whether it was reasonable for the offeree to rely on the offer as being irrevocable. Thus, the facts in each case would determine whether the reasonable person would have assumed that an offer is irrevocable. The issue which appears to be unresolved, therefore, is whether the CISG excludes any form of precontractual liability from its scope. Put differently, whether the gap - which is evident - can be filled by general principles or whether there is a need to rely on the otherwise applicable domestic law.

3.2. ARTICLE 4

Article 4 only governs the formation of the contract and the rights and obligations of the seller and buyer arising from such a contract. Because article 4 governs the formation of the contract, article 16 forms part of the process of forming a contract. Hence, embedded in article 16, is that a fixed time, when the offer is irrevocable, forms part of the formation of contract and, therefore, is governed by the CISG. This is not controversial; it is obvious. However, when there is a breach of article 16, the question is whether this is still within the sphere of the CISG. This

⁴⁴ Ibid.

⁴⁵ Henry Mather, ‘Firm Offers Under the UCC and the CISG’, 105 Dick. L.Rev. 31, 48.

⁴⁶ Geneva (n 43).

paper argues that this question is part of article 4, as the breach has been committed within the stage of contract formation and, hence, article 4 is not applicable - that is, article 4 does not mandate that a revocation of a fixed term needs to be governed by the otherwise applicable law. Rossen *et al* agree on this point, as they note that it “cannot be concluded that precontractual liability is excluded from the scope of the Convention merely from the wording of Art. 4 and the wording ‘*formation of contract*’.”⁴⁷

It is argued that the CISG can fill the gap as, in essence, a contract has been formed, as there was an offer of a fixed time and an acceptance, and no revocation is present. It is further argued that the first contract then can be subsumed into the formal contract of delivery of goods. In English common law, a fixed term is only valid if it is supported by consideration. In essence, an offer has been made which has been accepted and is supported by consideration.

The same argument can be applied in relation to the CISG. As the CISG does not require consideration, only an offer and an acceptance are required in order to support a fixed term. The offer not only concerns the supply of goods - it is also, by implication, providing a fixed time in which the offer must be accepted or rejected. The point is that there is no material difference between article 16(1) and (2). Subsection 2 follows the general principle that the conduct of a party to the contract can be relied upon as noted in article 8. In the case of article 16, this principle is reinforced by article 9(2) which builds on article 8 and notes:

(2) The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.

The usage in question is article 16 - namely, the irrevocable offer. It is argued that, if the offer is not a precondition to the actual offer, why draw a distinction between an actual or implied event, as noted by the two subsections? As Malik has noted, the revocation of an irrevocable offer is a legal nullity.⁴⁸ This is so as the offer is irrevocable. Hence, revocation is not possible without a remedy. It follows therefore that the aggrieved party can accept the offer within the allocated time and subsequently

⁴⁷ Rossen et al *How Far* (n 2) 7.

⁴⁸ Malik (n 14) 2.

enliven, if necessary, the breach regulations within the convention. In essence, an implied contract has been created by article 16(2) and acceptance closes the circle. As the breaching of article 16 is a nullity the contract is still afoot, and the question of breach and remedies must be addressed.

3.3 BREACH AND REMEDIES FOR DAMAGES

It is clear that a breach of article 16(2) is not a breach of a contract of sale, but a contract, as noted above. The issue, therefore, is whether Articles 71 to 77, though not applicable, support a principle to claim damages for a breach of article 16. The principles underlying articles 71 and, more specifically, article 72(2) arguably support a remedy for a breach of article 16.⁴⁹ Article 71, as an example, states:

- (1) A party may suspend the performance of his obligations if, after the conclusion of the contract, it becomes apparent that the other party will not perform a substantial part of his obligations as a result of:
 - (a) a serious deficiency in his ability to perform or in his creditworthiness; or
 - (b) his conduct in preparing to perform or in performing the contract.

However, this article is not relevant, as the aggrieved party - namely the buyer - is not in any position to suspend any performance. It is the seller who can suspend his performance, which is the breach of article 16. The argument in relation to anticipatory breach is somewhat different and, here, Article 72(1) comes into play. It states:

“(1) If prior to the date for performance of the contract it is clear that one of the parties will commit a fundamental breach of contract, the other party may declare the contract avoided”.

On the backdrop of the above, the fact that the breaching party attempted to revoke the irrevocable offer makes it clear that the party has committed a fundamental breach. To repeat the argument above, an offer has been made – namely, the observance of a strict time limit -, and the

⁴⁹ Ibid.

seller has breached that undertaking, hence committing a fundamental breach before the buyer could accept the offer. Therefore, he is deprived of a chance to gain income. The Oberlandesgericht Jena⁵⁰ confirmed that a breach of article 16(2) is a fundamental breach pursuant to article 25 and damages relying on article 74 are allowed.

Simply put, performance must be widely interpreted, and the emphasis must be put on “prior to performance” as noted in article 72(1). Logically, therefore, the right to damages is not dependent on a contract. The principle that can be derived from Article 71 and 72 is that if a contract cannot be performed, the breaching party is liable to pay compensation - that is, damages. A breach of article 16 also falls into the category that a contract cannot be made and, hence, by analogy, the effects are the same as if the contract had been performed. In other words, damages have accrued.

It must be remembered that article 16 does not allow the seller to breach his undertaking. Therefore, as noted above, the buyer can simply accept the offer. However, it would be irrational to ask the buyer to accept the contract first and then wait for the seller to breach the contract before he can sue for breach of contract. No doubt the CISG has not contemplated such an action, as it is fraught with danger.

Hence, in relation to recovering the losses, the same principles as discussed above apply. Namely, that the aggrieved party can rely on principles contained in Article 81(2), which notes:

“(2) A party who has performed the contract either wholly or in part may claim restitution from the other party of whatever the first party has supplied or paid under the contract. If both parties are bound to make restitution, they must do so concurrently”.

The aggrieved party has indeed performed a preliminary part in the overall obligation if money is spent in preparation of the acceptance. Hence, Article 81 is applicable. It needs to be noted again that the party who performs preliminary but essential parts of a contract is the party who does so in reliance of its ability to accept the contract.

In addition, Article 74 is not negatively affecting the ability to ask for damages in case of a breach of Article 16. Schlechtriem notes that damages are always monetary compensation in accordance with Article 74 (1). Moreover, the loss to the party affected must have been caused by the other party's breach, whether this was a result of a late or non-conforming

⁵⁰ MITEC Automotive AG v. Ford Motor Company, 5 U 1042/12, December 8, 2015.

performance or a result of no performance at all. He goes on to say that the only damages that must be compensated are those which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract. Thus, the reason is that a “breach” must be interpreted within the four corners of the CISG. One important issue is that interpretation cannot be executed without taking note of Article 7 and, in this case, the principle of good faith is applicable. It is certainly a breach of good faith to cancel an irrevocable offer upon which the other party, relying on its mandatory character, incurred expenses.

The effects of breaching a contract are not dissimilar, in character, to breaching Article 16. In both cases, the affected party relied on the promise and, hence, any breach of a CISG article is, in nature, the same. Rosenberg *et al* also commented that the Convention did intend to govern breaches of article 16(2) and that “*the principle underlying article 74 (that damages be available to the innocent party) should enable the buyer to recover damages for its reliance expenditure.*”⁵¹ Therefore, Article 74 becomes applicable, but only insofar as the damages do “not exceed the loss which the party in breach foresaw or ought to have foreseen” at the conclusion of the binding promise. Whether it is the contract or article 16 is irrelevant. Both are binding in character. Thus, it is reasonable that only losses which are a direct consequence of the breach are claimable, thereby excluding loss of profit.

In addition, UPICC will also be useful in determining this issue. Rossen *et al* also noted that “*In this regard UPICC, ... provide helpful tools to fill out the missing details in the CISG, but only to the extent that such does not expand the scope of the CISG.*”⁵² It is correct that missing details can be filled by taking recourse to UPICC, but to argue that it cannot expand the scope is troublesome, as any clarification supplied by UPICC will, in essence, widen the scope of the CISG. It must be noted that Bergsten argued that UPICC is “*in many respects a further development of the CISG itself.*”⁵³ This is highlighted by the fact that UPICC included, in essence, article 16 into their own regime. The question is why including a principle into the 2016 edition if the drafting history, as noted by Rossen *et al*, was, to say the least, troubled in the drafting of article 16. It is a strong argument to suggest that the drafters of UPICC did see a solution and did not simply copy a “mistake”

⁵¹ Mark Rosenberg, ‘The Vienna Convention: Uniformity in Interpretation for Gap-Filling – an Analysis and Application’, [1992] Australian Business Law Review 442, 460.

⁵² Rossen *et al* *How Far* (n 2) 30.

⁵³ Eric Bergsten, in John Felemegas (ed.) *An International Approach to the Interpretation of the United Nations Convention of the Contracts for the international Sale of Goods*, (Cambridge, 2007), ix.

as this paper has demonstrated. The “mistake” would be to include a rule into the CISG which, in effect, needs to be referred to the otherwise governing law when it could have been simply left out. UPICC included article 2.1.15 which supplies the answer. It notes:

(1) A party is free to negotiate and is not liable for failure to reach an agreement.

(2) However, a party who negotiates or breaks off negotiations in bad faith is liable for the losses caused to the other party.

(3) It is bad faith, in particular, for a party to enter into or continue negotiations when intending not to reach an agreement with the other party.

Simply put, this article confirms the principle of freedom of contract but, at the same time, bad faith in breaking off negotiations like a breach of article 16 CISG or article 2.1.4 UPICC. Rossen *et al* did discuss the application of good faith at length. However, this paper, understanding the solution of UPICC in relation to a fixed time, argues that, by analogy, the application of good faith, which is also contained in the CISG in conjunction with other arguments, will supply the answer. Namely, a breach of article 16 can be resolved within the CISG, as UPICC does not widen the scope but merely supplies a confirmation that good faith, in conjunction with other principles, can resolve the issue. This is in line with the fact that the general principle in the CISG is “*contracting cost reduction, which requires contracting parties to reduce the cost of executing and performing under CISG contracts.*”⁵⁴

4. CONCLUSION

It is obvious that article 4 is clear in noting that the CISG only governs “*the formation of the contract of sale and the rights and obligations of the seller and the buyer arising from such a contract.*” It is also clear that article 16 is only an offer and, hence, a contract has not been formed but, as Malik argues, the revocation of an irrevocable offer is a legal nullity. Therefore, “[t]he offeree may ignore the “revocation” and communicate his acceptance to conclude the contract and in the event of non-performance, proceed to claim damages.”⁵⁵ Any damages emanating from revoking the

⁵⁴ Steven D. Walt, ‘The Modest Role of Good Faith in the CISG’ [2015]33 Boston University International Law Journal 41.

⁵⁵ Malik, (n 14) n 2.

offer within the irrevocable time does not enliven articles 71 to 77, as these articles and others for that matter are only relevant upon breach of a contract.

Consequently, there are only two possible avenues for an aggrieved party that seeks to recoup their losses. First, to overcome this issue, it can rely on the otherwise applicable domestic law, which will fill the perceived gap. Second, can rely on general principles within the CISG, which is the proper law to govern this issue. Moreover, a breach of article 16 creates a nullity - that is, a revocation of the offer is not permitted. This action therefore must be treated as it has not occurred. This leaves the option of accepting the offer open.

To argue that the application of good faith might produce different results and, hence, bring uncertainties to the CISG⁵⁶, is a dangerous argument, as good faith as noted in article 7 must be observed in the interpretation of the CISG.

The breaching party has already indicated, by falsely revoking the irrevocable offer, that at least doubts as to their willingness to perform the contract are present. This brings Article 72(1) into play and the aggrieved party can avoid the contract. After avoidance, Article 81(2) will assist to recoup the losses, as the aggrieved party has partially performed the contract. This is indicated by the fact that the aggrieved party has incurred expenses which they would not have without the knowledge that they still have the option to accept.⁵⁷

By treating the revocation as a nullity, all options as to a formation of the contract are opened and full compensation can be sought. Arguably, this analysis is supported by the principle of good faith, as the aggrieved party would not have incurred expenses if they would have had any doubt as to the unwillingness of the other party to execute the contract. After all, having an irrevocable offer puts the offeree in a position to accept the offer and, hence, form a contract.

In conclusion, the CISG is able to compensate an aggrieved party because the revocation of the offer still leaves the aggrieved party in a position to conclude the contract and, thereby, take full advantage of the CISG. Hence, it does not have to rely on the otherwise governing law, as no gap exists. Importantly, gap-filling specifically by UPICC preserves “*the advantage of uniform law: it avoids the dependency on the forum which allows the parties to know which law to applies.*”⁵⁸ This is especially important in breaches of

⁵⁶ Rossen et al *How Far* (n 2) 12.

⁵⁷ It goes without saying that - should they not accept the offer - all expenses which they incurred cannot be recovered as no contract has been formed.

⁵⁸ Brandner *Admissibility of Analogy* (n 6).

article 16, as domestic law is divided on this issue and commercial certainty is achieved.