CHAPTER-4

IS THE UNITED NATIONS CONVENTION ON THE INTERNATIONAL SALE OF GOODS ADEQUATE TO ASSIST SMES AND START-UPS?

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I INTRODUCTION

It is a great pleasure to contribute to the United Nations Commission on the International Trade (UNCITRAL) Regional Centre for Asia and the Pacific and the Faculty of Law, University of Macau, UNCITRAL-UM Joint Conference to discuss the importance of modernization of National Commercial Laws and the role of Legal Harmonization in International Commerce. As we are all aware, this year marks the fiftieth anniversary of the UNCITRAL, which has been working to reduce disparities in national and regional regulations that impact international trade. The Commission continually seeks to promote international trade.

It is a pleasure to attend the University of Macau. It is also good to be in a part of the world that is vibrant and will form an important link as part of the Chinese initiative to promote the 21st Century Maritime Silk Road. This initiative will only enhance trade; the movement of people, goods and services across the Asia and Pacific Region for the small and medium enterprise and start-up sectors.

I would like to thank Professor. Dr. Bruno Zeller, from the University of Western Australia, for allowing me to work with him and present this to you all today. Professor Zeller has two decades experience and expertise in commercial international trade law and arbitration. More specifically, Professor Zeller, has intimate knowledge and has written extensively on the United Nations Convention on Contracts for the International Sale of Goods and the International Institute for the Unification of Private Law's (UNIDROIT) Principles of International Commercial Contracts.

This chapter will demonstrate how the United Nations Convention on the International Sale of Goods (CSIG) is sufficiently adequate to assist the small and medium sized enterprises (SMEs) and the start-up sector. The economy is rapidly changing from the former manufacturing and industrial base to digital, technology and services. The CSIG, due to the exclusion of services

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pursuant to Article 3 needs to be augmented by the UNIDROIT Principles as a contractual clause. This will need to be all inclusive to cover contract law and not only sale of goods laws. The structure of the Cape Town Convention is followed, where the Convention on Contracts for the International Sale of Goods (CISG) forms the overall umbrella with the UNIDROIT Principles as the pillar supporting the CISG by covering the gaps and exclusions within the CISG.

The CISG, UNIDROIT and Principles of International Commercial Contracts (PICC)[2] have been essential in the effort to modernize and harmonize international contract law.[1] However, at recent sessions of the United Nations Commission on International Trade Law (UNCITRAL), the adequacy of the CISG and the PICC has been the subject of substantial debate, with some calling for the development of an entirely new framework to harmonize general contract law.[2]

The future economic growth has been reported to be in areas of start-ups, small and medium business more so than in multinational corporations. Governments across the Asia Pacific Economic Forum (APEC), Association of South East Nations (ASEAN) and European Union (EU),[3] all recognize that small businesses play an important role in the economy and account for the bulk of business. The OECD (Organization for Economic Cooperation) has highlighted that SMEs account for 60 to 70 per cent of jobs in most OECD countries. SMEs will account for a disproportionately large share of new jobs, especially in those countries, which have displayed a strong employment record. The OECD reports that less than one-half of start-ups survive for more than five years and only a fraction develop into the high-growth firms, which make important contributions to job creation. One way to ensure start-ups thrive and are sustainable is to ensure they are afforded the optimal legal framework to ensure they can rapidly expand into other countries, from their country of origin. To achieve it, this sector can look to the CISG, particularly when this sector is entering into cross border international contracts for the sale of goods and services.

With current and future growth expected to be steady throughout the Asia Pacific Region, and to a lesser extent across the EU over the next decade, it is likely SME's located in Australia, Singapore, Malaysia, Indonesia, Switzerland and Slovenia will continue to expand their market reach. A major obstacle to the success and expansion of SMEs and start-ups is national regulatory burden.[4] The OECD points out that access to information about regulations should be made available to SMEs at minimum cost. Policy makers must ensure that the compliance procedures (e.g. research & development, and new technologies) are not costly, complex or lengthy. Transparency is of particular importance to SMEs, and information technology has great potential to narrow the information gap. It is argued that many star-ups and SMEs would not understand or possibly know the CSIG or UNIDROIT Principles exists, and how they can utilize the provisions to minimize the risk when developing contracts that span different countries.

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[1] Michael Dennis, 'Modernizing and Harmonizing International Contract Law: The CISG and the UNIDROIT Principles continue to provide the best way forward' (2014) Uniform Law Review 114.
[2] Ibid.
[3] Small Business, Job Creation and Growth: Facts, Obstacles and Best Practices, 'Organization for Economic Development and Co-operation'< https://www.oecd.org/cfe/smes/2090740.pdf> accessed 2 November 2017.
[4] M Dennis (n 1) 114–151.

The principle of "legal certainty" is important for economic development and growth both domestically and in international trade. Legal certainty is nothing new[5] as it is a *sine qua non* condition for a democratic society or a state governed by the rule of law.[6] For SMEs legal certainty creates the conditions necessary for attracting investment and encouraging economic development and growth through trade. Legal certainty requires that laws are accessible, operable, legible, intelligible and up-to-date, and it can be seen as the inherent object of the law itself, by defining its purpose. From an international trade perspective, legal certainty is the quality of the law so as individuals and entities and specifically SME's can easily ascertain contractual obligations and rights.

The traditional notion of contract formation is well entrenched in common and civil law countries. That is, the offer and subsequent acceptance form part of a meeting of the minds. In effect contractual parties, specifically SME's, do not have the legal resources to decide specific complicated contracts but rather wish to have simply but effective contractual obligations governing their sales. For some time in the area of international trade, legal certainty has existed, and has been strengthened by the CISG and UNIDROIT Principles.

Section two discusses the Cape Town Convention and the CSIG and how it has been recognized by 87 countries among them Australia, Indonesia, Switzerland, Singapore, Slovenia and member states of the European Union. Section three highlights the application of the CSIG for SMEs, and in particular the services sector. Section four discusses how the CISG, Principles 2010 and Model Clauses, are considered to be "soft law" and hence not binding on courts. Section four also discusses the application of the UNIDROIT Principles of International Commercial Contracts and Model Clauses, and how they have been successfully applied to overcome any gaps in the CISG. Section five provides an example of the intersect between the CISG and UNIDROIT Principles in relation to a breach of contract. The final section confirms the CISG is sufficiently strong to cater for the needs of the SME and start-up sector, as part of the new digital and technology economy.

II INTERNATIONAL FRAMEWORK AND THE UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS [CISG]

The Cape Town Convention as a framework has established a set of protocols that allow countries to adopt and currently the aviation, rail and space protocol exists.[7] A country accepts the Convention and then can decide which of the protocols they wish to accept and implement. This process is a good explanation of how the process of the interaction between the CISG and the UNIDRIOT Principles can be achieved. The Convention – the CISG – is supported by the inclusion of the PICC as part of the contractual terms not as a governing law. It will take its force of law as being part of the contractual terms.

The issue for many SME's is that they are engaged in the supply of services which have been excluded by the CISG. To change the CISG is not possible as already shown by Switzerland's

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[5] Gustav Kalm, 'Building Legal Certainty Through International Law: OHADA Law in Cameroon', Institut d'Études Politiques (Sciences Po) (October 2011) Buffett Center for International and Comparative Studies Working Paper Series, Working Paper No. 11-005.

[6] Georges Vedel, 'Proceedings of the Conference L'Etat de droit au quotidien', 65, cited by D. Labetoulle, 'Principe de l galit et principe de s curit ', in *M langes en l'honneur de Guy Braibant* Dalloz, (1996) 403.

[7] There are three protocols to the Convention that includes aircraft equipment 2001, railway rolling stock 2007, and space assets 2012. Kalm (n 5).

failed attempt to change the CISG into a contract law. However, the possibility is that a different aspect is explored namely the inclusion and adoption of the UNIDROIT Principles to fill gaps which are apparent in the CISG and hence the issue of services can also be covered. This option will be further discussed below.

The application and adoption of the CISG in the countries discussed in this chapter varies greatly. Firstly, there are only 87 countries that have signed the Convention.[8] Australia, Singapore, Malaysia and Indonesia, Switzerland, Slovenia and the European Union just to mention a few. Currently Indonesia and Malaysia are not a contracting party to the CSIG. Singapore[9] has implemented the CSIG through the *Sale of Goods (United Nations Convention) Act* 1996. Interestingly, Singapore and Vietnam are the only members of the ASEAN who have adopted the CSIG. Furthermore, there are approximately 195 countries in the world, and with such a limited number of countries adopting the CISG, the question arises – is it time that SMEs and start-ups are informed of the international instruments available to them to strengthen and enhance their trading opportunities, for both the manufacturing and service sectors? That is, and while out of scope of this discussion, it is our view that more needs to be done to promote the current international legal framework (the CISG, UNIDROIT Principles and Model Clauses) for international trade in general but particularly as the new digital-technological economy develops. Promoting this framework could result in more countries adopting the Convention, CSIG, PICC and model Laws. Doing so will strengthen the certainty for the small and medium sized sector who want to trade across international borders, particularly as the geopolitical landscape changes, nationalism and protectionism is on the rise.

III APPLICATION TO SMES THAT PROVIDE SERVICES

The CISG does not cover all sales. Article 2 states that the Convention does not apply to sales of goods bought for personal, family or household use, unless the seller, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the goods were bought for use by auction, execution or otherwise by authority of law, stocks, shares, investment securities, negotiable instruments or money, ships, vessels, hovercraft or aircraft or electricity. This provision identifies an exhaustive list[10] of sales that are excluded from the Convention's sphere of application. The exclusions referred to in article 2 are of three types: those based on the purpose for which the goods were purchased; those based on the type of transaction; and those based on the kinds of goods sold.[11]

It is well understood that Article 3 applies to contracts for the supply of manufactured goods. Article 3(1) of the CISG states that contracts for the supply of goods to be manufactured or produced are to be considered sales unless the party who orders the goods undertakes to supply a substantial part of the materials necessary for such manufacture. In interpreting the words "substantial part" under Article 3(1) CISG, primarily an "economic value" criterion should be used. An "essential" criterion should only be considered where the "economic value" is impossible or inappropriate to apply, taking into account the circumstances of the case. "Substantial" should not

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[8] Table of contracting states< https://www.cisg.law.pace.edu/cisg/countries/cntries.html> accessed 2 November 2017.
[9] Sale of Goods (United Nations Convention) Act 1996.
[10] Oberlandesgericht Schleswig-Holstein, Germany, 29 October 2002, English translation available on the Internet at <http://cisgw3.law.pace.edu/cases/021029g1.html> accessed 5 November 2017.
[11] United Nations Conference on Contracts for the International Sale of Goods, Vienna (adopted 10 March-11 April 1980) Official Records, Documents of the Conference and Summary Records of the Plenary Meetings and of the Meetings of the Main Committee (1981) 16.

be quantified by predetermined percentages of value; it should be determined on the basis of an overall assessment. The supply of services necessary for the manufacture or production of the goods is covered by the words "manufactured or produced" of Article 3(1) CISG and is not governed by Article 3(2) CISG. The words "materials necessary for such manufacture" in Article 3(1) CISG do not cover drawings, technical specifications, technology or formulas, unless they enhance the value of the materials supplied by the parties. In the interpretation of Article 3(1) CISG, it is irrelevant whether the goods are fungible or non-fungible, standard or custom-made.

It has been held by the courts that work done to produce the goods is not to be considered the supply of services for purposes of Article 3(2).[12] Furthermore, factors other than purely economic ones, such as the circumstances surrounding the conclusion of the contract,[13] the purpose of the contract[14] and the interest of the parties in the various performances,[15] should also be taken into account in evaluating whether the obligation to supply services is preponderant.[16] The essential purpose of the contract as a criterion relevant to determining whether the Convention was applicable. The party who relies on Article 3(2) to exclude the application of the Convention to a contract in which the party who has to furnish the goods also has to supply services and bears the burden of proving that the supply of services constitutes the preponderant part of the obligations. This has been reinforced by the Commercial Court in Switzerland,[17] whereby the court stated that Article 3 contracts do not apply where the preponderant[18] part of the obligation of the party who furnishes the goods consists in the supply of a service. While one court stated that turn-key contracts are governed by the Convention except when the obligations other than that of delivering the goods prevail from an economic value point of view, several courts stated that turn-key contracts are generally not covered by the Convention, because turn-key contracts "do not so much provide for an exchange of goods against payment, but rather for a network of mutual duties to collaborate with and assist the other party". However, courts have stated that turn-key contracts are generally not covered by the convention, because turn-key contracts do not so much provide for an exchange of goods against payment, but rather for a network of mutual duties to collaborate with and assist the other party.

If the economic value of a service is more than 50% of the total sales price, the CISG is not applicable. What the court was saying is that where the predominant contractual obligations lie with performing services that contract will not meet the requirements of Article 3. Nonetheless, the courts have provided guidance on where contractual obligations commence and conclude. For example, it is well accepted that Article 3 contracts apply to manufactured goods, however, there may be an obligation to install the manufacture product. The courts have accepted that installing

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[12] Austria Oberster Gerichtshof 14 January 2002<https://www.cisg.law.pace.edu/cisg/text/digest-2012-03.html#11> accessed 20 October 2017.
[13] Ibid 4-7.
[14] Ibid.
[15] Ibid.
[16] Ibid.
[17] Commercial Court of the Canton of Zurich (*Turnkey Plant case*) 9 July 2002 (HG000120/U/zs) <http://cisgw3.law.pace.edu/cases/020709s1.html> accessed 30 October 2017.
[18] Ferrari F, 'Specific Topics of the CISG in the light of Judicial Application and Scholarly Writing' (1995) 15 Journal of Law and Commerce in Bruno Zeller, 'Is the Sale of Goods (Vienna Convention) Act the Perfect Tool to Manage Cross Border Legal Risks Faced by Australian Firms?' (1999) 6 Murdoch University Electronic Journal of Law 28; Obergericht Aargau, Switzerland, 3 March 2009 <http://globalsaleslaw.com/content/api/cisg/urteile/2013.pdf> 25 CLOUT case No. 881 (Handelsgericht Zürich, Switzerland, 9 July 2002), accessed 28 October 2017.

products are a minor relevance to the overall obligations under Article 3.[19] The point is that installation is not considered a service. Therefore, in the new digital economy, where SMEs and start-ups are rapidly providing access to products across international borders, they can under contract rely on Article 3 for the manufacture, sale and installation of the product. Arguably, the issue arises in the new digital economy when there is a contract for the sale, dissemination or transfer of data and/or information across international borders by 2nd, 3rd or 4th parties. That is, these parties have not produced (manufactured) the original data (information) set. In this scenario, it is argued that the parties beyond the first provider are actually selling or providing a service that would not fall within Article 3 of the CISG. This could be a major constraint for the SME and start-up sectors, when only applying the CISG to contracts. However, as this chapter will highlight, the UNIDRIOT Principles provide the basis to fill the gaps within the CISG, and therefore, there is no need to modify or even develop and new framework specifically for SMEs.

Where the contract cannot rely on the provisions of the CISG, the UNIDROIT Principles and the suggested Model Clauses[20] can be applied. To reinforce this point, Professor Zeller notes that the CISG generally deals only with sales contracts, whereas the UNIDROIT Principles govern commercial contracts. Thus, in effect, they may in many cases provide a solution for ambiguities or gaps in the CISG.[21] It is left to the parties to include the governing law into their contracts and hence a Model Clause will assist in this respect. Combining the application of these instruments provides the basis for contracts to also include services.

Furthermore, this will assist the development and expansion of the future digital and technological based economy, across the Asia Pacific Region. The next section highlights the interrelationship between the CISG, UNIDROIT Principles 2010 and Model Clauses. The Model Clause as suggested by UNIDROIT brings the PICC into the contract, otherwise the PICC cannot be relied upon.

IV UNIDROIT PRINCIPLES [THE PRINCIPLES]

In order to demonstrate the relationship between the CISG, Principles 2010 and Model Clauses, it needs to be understood that the Principles have been considered to be "soft law" and hence not binding on courts.[22] Professor Bonell highlights that 'soft law' is understood as referring in general to instruments of a normative nature with no legally binding force, and which are applied only through voluntary acceptance.[23] Given the increased globalization of the world economy, the development of international commercial law has had an exponential growth, and as such, soft law has been an important part of this development.[24] These are generally established legal rules that are not positive law and are therefore not judicially binding.

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[19] Canton Appellate Court (*Obergericht*) Zug <http://cisgw3.law.pace.edu/cases/061219s1.html>.

[20] Model Clauses for the Use of the UNIDROIT Principles of International Commercial Contracts <http://www.unidroit.org/contr-modelclauses-overview> accessed 12 December 2017.

[21] John Felemegas, *An International Approach to the Interpretation of the United Nations Convention on Contracts for the International Sale of Goods (1980) as Uniform Sales Law* (Cambridge University Press 2007).

[22] Ole Lando, 'Principles of European Contract Law and UNIDROIT Principles: Moving form Harmonization to Unification?' (2003) 8 UNIF. L. REV. (n.s.) 123.

[23] Michael Bonell, 'Soft Law and Party Autonomy: The Case of the UNIDROIT Principles' (2005) 51 LOY. L. REV. 229.

[24] Henry Gabriel, 'The Advantages of Soft Law in International Commercial Law: The Role of UNIDROIT, UNCITRAL, and the Hague Conference' (2009) 34:3 BROOK. J. INT'L L. 666.

Professor Gabriel has informed us that the various soft law instruments in international commercial law include model laws, a codification of custom and usage promulgated by an international non-governmental organization, the promulgation of international trade terms, model forms, contracts, restatements by leading scholars and experts, or international conventions.[25] Although soft law principles do not begin as positive law, they can become positive law both by adoption by courts or tribunals or by adoption in the agreements of transactional parties.[26]

Generally, lawyers appreciate the difference between a choice of law provision and the incorporation of the Principles as terms to an agreement, and it is quite easy to choose the Principles as governing the contractual relationship if parties wish. As Professor Gabriel has demonstrated there are advantages to soft law because in many circumstances, particularly in the area of private international law, soft law instruments, such as the Principles, have advantages over conventions and treaties. For example, non-binding general principles can achieve the goal of uniform, or at least harmonized law because there is less necessity to accommodate various legal traditions or domestic laws. Also, they may be adopted in part as well as a whole, thereby providing flexibility for an easier basis for adoption in a given court or arbitration because there is less conflict between the international and the domestic law as there would be in the case of a binding Convention. In addition, because there is no need to have principles adopted by a given jurisdiction, the principles are more easily and readily available for use. Since these principles are not binding, their likely effect is more to set norms instead of hard and fast rules, while still achieving the goal of creating broad international standards.[27] Once completed, a soft law instrument is ready for adoption by the parties as part of their agreement or ready for use as an interpretive document by courts and arbitrators. Nevertheless, soft law instruments, have been used by courts and arbitrations as a basis for forging new legal rules as well as interpreting existing ones. In the common law world, courts have long relied upon soft law as a source of law.[28] Moreover, arbitration tribunals, which are generally not bound by domestic choice of law restrictions, often adopt legal rules, such as the Principles, because of the presumed neutrality of these rules.[29] This has certainly been the case in the United States. Finally, soft law instruments, unlike treaties and conventions, are not subject to the lengthy process of ratification that can delay enforcement for years. This is a significant advantage to the SME and start-up sectors as they can adopt the current framework, rather than having to wait for the long and sometimes frustrating process of getting a treaty or convention changed, agreed and approved by countries.

The Principles not only assist in the trading of goods, but also extend to services, unlike the CISG. However, these Principles have demonstrated that they are offering concrete and worthwhile solutions and arguably are a move forward in harmonizing and unifying contract laws. Even though the Principles are not a rigid and are a limitative legal source. The Principles provide flexibility to accommodate specific provisions to further individual parties' interest in their private dealings, or to promote national trade and economic policies. This makes the Principles a unique tool to be adapted into any contract and arguably protect the parties' just expectations arising from their contract. This includes those SMEs and start-ups that are currently or will be providing services across international borders.

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[25] Henry Gabriel, 'UNIDROIT Principles as a Source for Global Sales Law' (2013) 58 Villanova Law Review 664.
[26] Ibid 664.
[27] Ibid.
[28] Ibid.
[29] Ibid.

A basic principle in international trade, is the ability for an individual or entity to contract. The freedom to undertake international trade and contract is a cornerstone of an open, market-oriented and competitive international economic order. Arguably, the preamble to the Principles provides the basis for international and commercial contracts. However, the Principles do not provide any express definition, but the assumption is that the concept of "commercial" contracts should be understood in the broadest possible sense. That is, not defining what is in and what is out, allows the inclusion of not only trade transactions for the supply or exchange of goods or services, but also other transactions. This includes investments, concession agreements, and contracts for professional services. Therefore, combined with the CISG, the Principles will fill any gaps in the contract of services. Article 6 of the CISG allows the parties to exclude the Convention wholly or in part. The parties are free (by agreement) to vary the effect of any provision of the Convention. A merger clause that explicitly barred evidence of negotiations would be effective. The Principles recognize the validity of a merger clause that indicates that the writing is totally integrated.[30] The use of such a clause is likely to be effective in contracts that involve services.

Individual's party to the contract may choose to replace individual Articles of CISG with the Principles, however it is unlikely that they will totally exclude the CISG.[31] Even so, in circumstances where the international sales contract is governed by CISG, the Principles could be of importance, particularly in relation to those contracts that will be formed in the new economy for services. For instance, Article 7(1) CISG, "in the interpretation of this convention regard is to be had to its international character and to the need to promote uniformity in its application". Article 7(2) states that "questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based".

As highlighted by Professor Bonell the historical interpretation of the CSIG have had to be found by the judges and arbitrators on an ad hoc basis. The Principles can be used to interpret or supplement provisions of the CISG. On the other hand, in order for individual provisions to be used to fill gaps in CISG, they must be the expression of general principles underlying also the CISG. The Principles have been effective in clarifying ambiguous provisions of the CISG. Article 7.1.4(2), which states that the right to cure is not precluded by notice of termination, in connection with Article 48 of the CISG. Article 7.1.7(4) expressly indicates that the remedies not affected by the occurrence of an impediment preventing a party from performing the contract in accordance with Article 79(5). Furthermore, Article 7.3.1(2) specifies the factors to be taken into account for the determination of whether or not there has been a fundamental breach of contract, in connection with Article 25 CISG.[32] However, Articles 2.1.15 and 2.1.16[33] on negotiation in bad faith and breach of a duty of confidentiality of the Principles can fill this gap. In summary, the Principles apply to any commercial contract, and as such, there is sufficient adequacy when coupling the two instruments together and utilizing the Model Clauses to establish effective contracts for the SME and start-up sectors. Furthermore, Article 7(1) of the CISG states that "[i]n the interpretation of this Convention regard is to be had to its international character and to the need to promote uniformity in its application". The Principles are of international character, and therefore, they

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[30] A Guide to Article 8< https://www.cisg.law.pace.edu/cisg/principles/uni8.html> accessed 28 September 2017.

[31] Michael Bonell, 'The UNIDROIT Principles of International Commercial Contracts and the Harmonization of International Sales Law" (2002) R.J.T. 36.

[32] Ibid.

[33] UNIDROIT Principles, Annexure <http://www.unidroit.org/english/principles/contracts/principles2016/principles2016-e.pdf> accessed 28 September 2017.

may be used when interpreting the CISG, provided that the relevant provisions of the Principles serve the same purpose as their corresponding provisions in the CISG.[34]

The problem is the relationship between the CISG, the Principles and domestic law needs to be regulated.[35] How that is to be done is a critical point. There is nothing to stop contractual parties to contract that the CISG applies and all gaps are to be filled by recourse to the Principles. The CISG, although solely sales law, in general, relies on contract principles, hence gap-filling by the Principles is not a giant step. Even so, as Professor Bonell demonstrates that progress in this area has been made by the creation of Model Clauses for the Use of the Principles of International Commercial Contracts.[36] The UNIDROIT Governing Council unanimously adopted the Model Clauses at its ninety-second session in May 2013.[37]

Having model clauses is certainly a step forward because the Principles have not been noted extensively by courts, let alone applied. In the United States, Professor Gabriel notes that there are only two reported cases, where the courts addressed but did not apply the Principles.[38] Furthermore, there are only 255 reported cases and arbitral awards listed on the UNILEX, suggesting that the use of the Principles is not widespread.[39]

The Australian example, demonstrated by Professor Zeller, is where the Principles have been quoted seven times, once in the Australian High Court, three times in the Federal Court and three times in the state of New South Wales - Supreme Court. The Australian High Court had to look at the claim whether a breach of a "non-essential" term gives rise to a breach of contract. The Australian High Court comparatively addressed this issue with other laws and noted:

> "It finds no reflection in the relevant parts of the United States Restatement of the law. Nor is it adopted in the Uniform Commercial Code of the United States. There is nothing like it in the United Nations Convention on Contracts for the International Sale of Goods 1980. Nor does it appear in the Principles of International Commercial Contracts 2004."[40]

In *University of Western Australia v. Gray*, where the question revolved around the implication of terms at law, Principles Articles 4.8 and 5.1 were only mentioned in passing.[41] The

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[34] John Felemegas, 'The United Nations Convention on Contracts for the International Sale of Goods: Article 7 and Uniform Interpretation', in *Pace Review of the Convention on Contracts for the International Sale of Goods (CISG)* (Kluwer Law International 2000-2001) 115 - 265, at Chapter 4, 6(b) <http://cisgw3.law.pace.edu/cisg/biblio/felemegas.html#ch4> accessed 28 September 2017.

[35] Bruno Zeller, 'The Development of a Global Contract Law. Still a Dream?' in *The Age of Uniform Law - Essays in Honour of Michael Joachim Bonell to Celebrate his 70th Birthday* (UNIDROIT Rome, Italy 2016) Vol. 2, 1184.

[36] Michael Bonell, 'Model Clauses for the Use of the UNIDROIT Principles of International Commercial Contracts' (2013) 18 UNIF. L. REV.475.

[37] Summary of the Conclusions, Doc CD (92) Misc 2 (UNIDROIT 2013), online, 2.

[38] Henry Gabriel, 'The UNIDROIT Principles: an American Perspective on the Principles and Their Use' (2012) UNIF. L. REV. 509.

[39] Ibid 513.

[40] *Koompahtoo Council v Sanpina P/L/* (2007) 233 CLR 115. 157 referring to articles 7.3.1 and 7.3.3.

[41] (2009) 179 FCR 346.

Australian courts have considered the Principles in the context of good faith,[42] oral modification clauses[43] and construction and interpretation of contracts.[44]

As Professor Zeller notes that both the CISG and the Principles have a problem. The CISG is unfortunately routinely excluded and the Principles – being soft law – are rarely applied. Furthermore, the CISG has gaps and requires a supplementary law to resolve disputes, which are supplied by the otherwise governing domestic law. The Principles being part of a Model Clause would fill that gap-filling requirement. There would then be no need to resort to domestic law unless mandatory laws are at issue. Therefore, in terms of a step in the direction of harmonized contract law, only one of the Model Clauses is truly useful: "This contract shall be governed by the United Nations Convention on Contracts for the International Sale of Goods (CISG) interpreted and supplemented by the Principles of International Commercial Contracts (2010)."[45] This is despite or because of the fact that the CISG in general deals only with sales contracts, whereas the Principles govern commercial contracts. In effect, they may in many cases provide a solution for ambiguities or gaps in the CISG.[46] Even so, it is left to the parties to include the governing law into their contracts and hence a Model Clause will assist. For instance, where the above Model Clause would have resolved the issue is to be found in *Hideo Yoshimoto v. Canterbury Golf International Ltd*.[47] The court in essence grappled with the difficult question as to whether evidence relating to prior negotiations can be applied. The court noted:

> "A particular clause might be said to have a plain meaning and was held to have such a plain meaning by the Judge at first instance. The context, the commercial objective of the contract and its contractual matrix, however, point away from that meaning. In addition, reliable extrinsic evidence is available which confirms that this plain meaning is not what the parties actually intended."[48]

The court observed that "(T)his document, which is in the nature of a restatement of the commercial contract law of the world, refines and expands the principles contained in the United Nations Convention."[49] The next section briefly highlights the corresponding provisions within the CISG and Principles for a breach of contract.

V REMEDIAL PROVISIONS OF THE CSIG AND UNIDROIT PRINCIPLES

There are a number of remedial provisions that intersect between the CISG and UNIDROIT Principles. Remedial provisions are important for SMEs and start-ups because they do not necessarily have the financial or other resources to seek damages (recover any loss) when there has been a breach of a contract. Where there is a "fundamental" breach,[50] the rights available to the injured party are equal. This, there is no one remedy or remedies that is superior. The

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[42] *Hughes Aircraft Systems International v Airservices Australia*, (1997) 76 FCR. 161; *United Group Rail Services LTD v Rail Corporation New South Wales* (2009) 74 NSWCA 618.7, and *Alcatel Australia LTD v Scarcella and others* (1998) 44 NSWLR 349.
[43] *GEC Marconi Systems Pty Ltd v BHP Information Technology Pty Ltd*, (2003) 128 FCR, 1.
[44] *Franklins Pty Ltd v Metcash Trading Ltd*, (2009) 76 NSWLR 603.
[45] UNIDROIT Principles Model Clause No. 1.2(a), 3)
<http://www.unidroit.org/english/principles/modelclauses/modelclauses-2013.pdf> accessed 29 September 2017.
[46] Felemegas (n 21).
[47] (2000) NZCA 350.
[48] Ibid 1.
[49] Ibid 87-89.
[50] Convention International Sale of Goods 1980, Article 25.

concept of *fundamental breach* under determines the availability of the avoidance remedy in respect of any breach, except late performance.[51] Fundamental breach is also important for the transfer of risk.[52] Article 7.3.1 of the Principles provides the basis of '*fundamental non-performance'*. However, and unlike Article 25 of the CISG, its scope is limited to the termination of a contract. Article 25 of the CISG provides that a breach is fundamental, if it results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract, unless the party in breach did not foresee and a reasonable person of the same kind in the same circumstances would not have foreseen such result. Importantly, for the effective management of contracts, Article 25 CISG attempts to define fundamental breach in terms of a detriment; a substantial deprivation or foreseeability.[53] Allowing the avoidance or termination of a contract only when the breach - non-performance qualifies as "fundamental", Article 25 CISG and Article 7.3.1 of the Principles follow the same policy, namely to preserve the enforceability of the contract whenever feasible.[54]

Article 7.3.1(2)(b) and (d) of the Principles provides the reliance on one party's future performance in determining fundamental breach. However, no use can be made of the factor focusing on whether the breach was committed *intentionally* or *recklessly* in accordance with Article 7.3.1(2)(d) of the Principles. The wording of Article 25 of the CISG does not prevent the determination of the fundamental nature of a breach by taking into account the breaching party's intent or conduct. It should be noted that under the CISG, "fault" is not generally a prerequisite to a finding of contractual liability and that this principle is as true with respect to the right to avoid the contract as it is to the right to require substitute delivery or to claim damages. Neither remedy depends on "fault" in the sense of deliberate or negligent wrongdoing. In light of the CISG's remedial system, it therefore seems to be more plausible not to automatically qualify any intentional or reckless breach as fundamental in terms of Article 25 of the CISG.[55] The intention of the breach can be only taken into account where the willful or reckless conduct creates uncertainty as to the breaching party's future performance.[56] The approach of whether the breaching party will suffer disproportionate loss as a result of the preparation for performance if the contract is avoided[57] is not applicable under the CISG. The language of Article 25 CISG does not allow consideration of the consequences for the breaching party when the breach is treated as fundamental. Furthermore, it is not clear under which circumstances a breaching party's loss becomes significant. Any determination of fundamental breach would therefore be arbitrary and cause uncertainty. Moreover, the Principles are aimed at limiting the exercise of the right of avoidance, not at determining a fundamental breach. In summary, this is an excellent demonstration of the interaction of both instruments, as such, the first condition for making use of

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[51] Ibid Articles 49(1)(a), 64(1)(a), 72(1) and 73(1).
[52] Ibid Article 70.
[53] Graffi, 'Case Law on the Concept of "Fundamental Breach" in the Vienna Sales Convention' (2003) 3 International Business Law Journal 338 (stating that the CISG simply provides general interpretive guidelines); <http://cisgw3.law.pace.edu/cisg/biblio/graffi.html> accessed 29 September 2017.
[54] Robert Koch, 'Applying the United Nations Convention on Contracts for the International Sale of Goods: The Elusive Goal of Uniformity in Review of the CISG' in *Cornell Review of the Convention on Contracts for the International Sale of Goods* (1995) 21-49 C.1 (stating that the Convention's goal of saving deals promotes important international values pertinent to the contracting process) <http://cisgw3.law.pace.edu/cisg/biblio/hillman1.html> accessed 30 September 2017.
[55] Ibid 823.
[56] Ibid.
[57] UNIDROIT Principles, Article 7.3.1(2)(e).

the criteria established by the Principles is fulfilled. They assist in seeking damages for the loss as a result of a breach of contract.

Damages are the most important remedy because they provide relief, which is more easily enforced against local assets or against an issuer of a letter of credit than specific reliefs, such as performance, substitution, or repair.[58]. Article 74 provides damages that must "consist of a sum equal to the loss, including loss of profit, suffered as a consequence of the breach". What this achieves is to ensure that the party who has been affected is in a good a position as if the party in breach had properly performed the contract, and to ensure full compensation.[59] Furthermore, Article 75 provides for the calculation of damages where the contract has been avoided and a cover purchase has been undertaken. Traditionally, damages were calculated as to the economic loss of the individual or entity, however, there has been a shift towards ensuring damages are available for contract violations where no economic loss has been incurred.[60] Secondly, the right to interest exists "if a party fails to pay the price or any other sum that is in arrears, the other party is entitled to interest on it."[61]

VI CONCLUSION

The preparation or modification of international commercial law conventions and treaties tends to be a long process, and the long length of time is partially attributable to incessantly searching for common principles and reconciling established principles from different legal systems and traditions. Coming back to the central question of this chapter, the CISG coupled with the Principles which are included by a carefully drafted Model Clauses, as a framework, are sufficiently adequate to accommodate contracts for the service sector and services that currently are, and will, be provided by SMEs and start-ups. This chapter has highlighted that SMEs and start-ups make a significant contribution to a countries' economic activity and growth. With most countries transitioning their economies from traditional manufacturing to digital technology, there is likely to be the need for the use of international commercial contracts for service sector. The Principles are arguably the best known and have been taken note of by the legal profession. The Model Clause will negate the "downside" and highlight the "upside" of global contract law. Finally, more needs to be done to promote the CISG, the UNIDROIT Principles and Model Clauses, so as they are adopted by the SMEs and start-up sectors as part of the development and expansion of the new digital - technological economy.

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[58] Avery Katz, 'Remedies for breach of contract under the CISG' (2006) International Review Law Economics 378-396.

[59] Advisory Council, Opinion no 6: Calculation of Damages under CISG Article 74, Spring 2006, <http://www.cisgac.com> accessed 30 September 2017.

[60] Peter Schlechtriem and Ingeborg Schwenzer, *Commentary on the UN Convention on the International Sale of Goods* (3rd edn. Oxford University Press, Oxford 2010).

[61] Convention International Sale of Goods 1980, Article 78 and UNIDROIT Principles, Article 7.4.9.