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COMPARING FORESEEABILITY IN CONTRACTUAL DAMAGES UNDER THE CISG, UNIDROIT PRINCIPLES AND PRINCIPLES OF EUROPEAN CONTRACT LAW

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Abstract

In contract law, when one party breaches its contractual obligations, the aggrieved party may claim to recover damages; however, they are not always entitled to the full amount of loss or damages caused. To limit damages in contract disputes, national legal systems and international instruments have introduced foreseeability into the contract language. The aim of this research is to investigate foreseeability as it has been applied under the Vienna Sales Convention (CISG), the UNIDROIT Principles (UPICC) and the Principles of European Contract Law (PECL). In the study, the principle of foreseeability is examined as regulated in these three instruments with a comparison of their similarities and differences. While textual differences between the instruments are minor, challenges remain in interpreting foreseeability rule including its ambiguity and uncertainty. Nonetheless, the broad and flexible approach of foreseeability continues to be effective in the global commercial context.

Keywords: foreseeability; contractual damages; United Nations Convention on Contracts for the International Sale of Goods; Principles of European Contract Law; UNIDROIT Principles of International Commercial Contracts.

1. Introduction

In contract law, incorporating foreseeability has become a popular method of limiting damage and has been entrenched in various national laws in numerous variations. The principle of foreseeability aims to limit the scope of damages that a breaching

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party is liable for; it ensures that the damages the breaching party pays are connected to and within the sphere of the contract. The effectiveness of foreseeability during its long history has driven its appearance in international trade relationships. At the international level, this principle can be found in the United Nations Convention on Contracts for the International Sale of Goods (CISG),[1] the UNIDROIT Principles of International Commercial Contracts (UPICC),[2] and the Principles of European Contract Law (PECL).[3] This study seeks to investigate how foreseeability was approached in the CISG, PECL and UPICC, performing a comparative analysis of the similarities and differences in their foreseeability rules.

2. Comparing the instruments

2.1. Foreseeability in general

Generally, foreseeability is used in the three instruments as a method of limiting damage awards. In the UPICC, it is addressed in Art. 7.4.4: '[t]he non-performing party is liable only for harm which it foresaw or could reasonably have foreseen at the time of the conclusion of the contract as being likely to result from its non-performance'. The non-performing party (and its servants or agents) is not liable for harm that the party could not have reasonably foreseen, at the time of concluding the contract, as the consequences of non-performance in the ordinary course of events and the particular

[1] The United Nations Convention on Contracts for the International Sale of Goods (CISG) is a multilateral treaty providing a uniform framework for international sales of goods between two parties whose places of business are in different countries. The Convention was prepared by the United Nations Commission on International Trade Law. It was adopted by a diplomatic conference in Vienna on April 11, 1980, and came into force on January 1, 1988. The CISG has been accepted and recognized worldwide, with 97 member states representing two thirds of world trade.

[2] The UNIDROIT Principles of International Commercial Contracts (UPICC) was written under the auspices of the International Institute for the Unification of Private Law's (UNIDROIT), and it comprises a set of general rules conceived for 'international commercial contracts.' It was first published in 1994 and was revised in 2004, 2010 and, most recently, in 2016. The main purpose of the UPICC is to 'provide a uniform framework for international commercial contracts, expressly refers to the need to promote uniformity in their application, i.e. to ensure that in practice they are to the greatest possible extent interpreted and applied in the same way in different countries'. The UPICC is considered the soft law of international commercial contracts, a guide for harmonizing international commercial contract law by interpreting and supplementing national law and international uniform law instruments.

[3] The Principles of European Contract Law (PECL) is a set of model rules drafted and promulgated by the Commission on European Contract Law. Part I of the PECL was published in 1995; part II has been available since 1999, and part III was completed in 2002. The Principles attempt to provide a set of neutral, basic rules for contract law in Europe, that include not only international commercial contracts, but also domestic and consumer contracts. They also aim to form a common core of European contract law toward the future unification of the laws. The PECL are inspired by the United Nations Convention on Contracts for the International Sale of Goods and is analogous to model laws in the United States. The PECL are very similar to the UPICC; the two pursue similar aims and were drafted in a similar style and structure. The PECL are also soft law and are not legally enforceable. However, they have gained a significant informal influence on law reform in a number of European countries.

contract circumstances. Because all harm suffered could be deemed unforeseeable, claims for damages could be limited or even denied altogether.[4]

According to Art. 9:503 of the PECL, '[t]he non-performing party is liable only for loss which it foresaw or could reasonably have foreseen at the time of conclusion of the contract as a like result of its non-performance, unless the non-performance was intentional or grossly negligent'. Under the PECL, the non-performing party is only liable for loss that at the time the contract concluded he actually foresaw or could reasonably have foreseen unless the non-performance was committed intentionally or was caused by gross negligence.

Article 74 CISG holds that:

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 contract.

Accordingly, the party in breach is only liable for losses they could foresee or ought to have foreseen at the time of the conclusion of the contract and is precluded from liability for any damage beyond the party's foreseeability. Art. 74 strongly affirms the idea that 'having regard to all circumstances of the given case, the party in breach is not liable for a loss he could not foresee'.[5]

2.2. Who must foresee the loss?

Who is required to foresee the harm or loss? Should it be contemplated by both parties? Both the UPICC and PECL stipulate that it is the non-performing party that is required to foresee the harm or loss. The Official Comments on UPICC Article 7.4.4 further clearly state that the non-performing party includes its servants or agents. Instead of differentiating types of breach as some legal systems do,[6] the two principles use the term 'non-performance' which includes every circumstance where a given party's failure to perform its contractual obligations. All possible damages caused by non-performance can be measured by foreseeability.

The CISG differs in requiring the party in breach to foresee the loss. The requirement to the non-performing party or party in breach to foresee of the three instruments is because only he has knowledge and could be aware of the facts and matters that will

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4 Ewan McKendrick: Damages. In: Stefan Vogenauer – Jan Kleinheisterkamp (ed.): *Commentary on the UNIDROIT Principles of International Commercial Contracts (PICC)*. Oxford, University Press, 2015. 995.

5 Victor Knapp: Comments on Article 74. In C. Massimo BIANCA: *Bianca-Bonell Commentary on the International Sales Law*. Milan, Giuffrè, 1987. 538–548. Art 74, para 2.8.

6 See Ingeborg Schwenzer: Rechtsbehelfe und Rückabwicklungsmodelle im CISG, in den European und UNIDROIT Principles, im Gandolfi-Entwurf sowie im Schuldrechtsmoderniesierungsgesezt. In: Peter Schlechtriem (ed.): *Wandlungen des Schuldrechts*, 1. Aufl. Schriften der Ernst-von-Caemmerer-Gedächtnisstiftung 5. Baden-Baden, Nomos Verlagsgesellschaf, 2002. 49.

constitute a breach or non-performance.[7] This limited reference to the non-performing party or party in breach corresponds with the risk allocation rationale.[8] According to Murphey, affirming the party in breach under Article 74 surely does not envision delivering a windfall to the plaintiff, because the plaintiff recovers something not foreseen. Rather, this language reflects the view that the focus should be on the party who will have to answer for the amount of the loss.[9]

However, differences between the characteristics of the non-performing party/or party in breach and a 'reasonable person' could raise the question of who ought to have foreseen or could reasonably have foreseen the loss: a reasonable person in the same circumstances or the party in breach/non-performance. Even though there are slight differences in wordings, these instruments preclude the consideration of a reasonable person and indicate clearly that who 'ought to have foreseen' or 'could reasonably have foreseen' the loss is the party in breach/non-performing party itself.

2.3. Foreseeability of what?

Next, whereas both the CISG and PECL require foreseeability of loss, the UPICC refers to foreseeability of harm. Although there is only a slight difference in meaning, the use of 'harm' in the UPICC seems to expand the liability of the non-performing party.

2.4. The burden of proving foreseeability

The burden of proof of foreseeability of harm implied in the three instruments is on the aggrieved party. The injured party is required to provide that harm or loss that is certain or likely to result from such a breach must have been foreseeable.[10]

2.5. Test for foreseeability

All three instruments apply both subjective and objective tests to determine what is reasonably foreseeable. Under both the UPICC and PECL, the non-performing party is responsible not only for harm that it actually foresaw in a particular situation (subjective) but also for harm it 'could reasonably have foreseen' (objective). The word 'reasonably' used in this context does not imply a reasonable person in the philosophical consideration

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7 Chengwei Liu: Remedies for Non-Performance, Perspective from CISG, UNIDROIT Principles & PECL. Law School of Renmin University of China, 2003. https://tinyurl.com/4b3ucc5t (Accessed on 18 February 2024).

8 Djakhongir Saidov: *The Law of Damages in International Sales – The CISG and other International Instruments.* Oxford, Hart Publishing, 2nd ed., 2021. 114.

9 Arthur G. Murphey Jr.: Consequential Damages in Contracts for the International Sale of Goods and the Legacy of Hadley. *The George Washington Journal of International Law and Economics* 23, (1989–1990), 415.

10 Sieg Eiselen: Remarks on the Manner in which the UNIDROIT Principles of International Commercial Contracts May Be Used to Interpret or Supplement Article 74 of the CISG. *Pace International Law Review* 14, (2002), 379.

discussed above; rather, it refers to reasonable foreseeability[11] and a 'higher probability than a mere possibility'.[12] It is important to evaluate a party's capacity to anticipate the harm and its consequences. The reasonableness element is added to the text to emphasise that only a party's subjective determination of foreseeability is not enough to award full compensation. Objective standards need to be applicable that account for market fluctuations or changes to the nature of the contract.

Although the CISG uses a slightly different expression, 'foresaw or ought to have foreseen', it contains the same subjective and objective standard: The breaching party is liable if there is evidence the party actually foresaw or was in a position to foresee the loss in circumstances. The objective test may be restricted by a reasonable distribution of risks in the contract. In cases when any reasonable person would have foreseen the loss and the breaching party actually did foresee the loss, the subjective foreseeability criterion is met.[13] There is no particular reason why the instruments express differently in this regard. This author considers that 'ought to have foreseen' is stricter than the UPICC's and PECL's 'could reasonably have foreseen' because it seems to impose a duty on the party to foresee harm or loss.

2.6. Time of Foreseeability

The time required to determine foreseeability in the three instruments is the time at the conclusion of the contract, similar to the Hadley rule or English law: the time parties made the contract.[14] The non-performing party or the party in breach is excluded from liability for harm or losses they objectively could not foresee at the moment the contract concluded even if they became aware of the harms while performing the contract.[15] Following this criterion requires establishing the precise time the contract concluded. Regarding that issue, the phrase 'at the time' in Art. 74 CISG as well as in the UPICC and PECL appears to be unambiguous and does not appear to need to be amended.[16] It is impossible to validate any legal consequences if harm or loss is foreseen after the contract comes into force[17] because the parties can only assume the risks and have the chance for self-protection (to consider price, insurance, liability and benefit, etc.,) at the time of the conclusion of the contract. At this stage, the parties have opportunity to consider any special circumstances outside the ordinary course of events that they ought to foresee when concluding the contract.

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11 Saidov op. cit. 116.

12 McKendrick op. cit. 996.

13 Liu op. cit. section 14.2.2.

14 See *Hadley v Baxendale* [1854] 9 Ex 341 para 354. Liu op. cit. section 14.2.3.

15 Knapp op. cit. para 2.13.

16 Guenter Heinz Treitel: Remedies for Breach of Contract: A Comparative Account. *Oxford University Press,* (1988), 160.

17 See Peter David Victor Marsh: Comparative Contract Law: England, France, Germany. *Gower Publishing*, (1994), 314.

The PECL sets the exception that in case of intentional or grossly negligent non-performance, the foreseeable reference point of time at the time of concluding the contract might not be applied. By expressing 'unless the non-performance was intentional or grossly negligent', it may infer that the time of foreseeability may be extended to a later time after the contract was made. This different expression of the PECL may come from its wider application to also national and consumer contract and therefore, it is reasonable to refer time of foreseeability to the point of time after the contract concluded.

Although the clause 'at the conclusion of the contract' is widely used and supported by the legal systems, international instruments and scholars, there are other views on the time to measure foreseeability. It is criticised that in practice foreseeability of consequences is not possible to affect the terms of the transaction because 'it is normally impracticable to fix a separate rate for every contract'.[18] Murphey comments that 'a sounder decision can be made nearer the time of performance or breach'.[19] Samek argues that the time of breach should be applied in case of wilful breach because such wilful action is undoubtedly less deserving of protection than accidental or negligent one.[20] Robin Cooke considers both at the date of contracting and immediately before the breach as the point of time to measure foreseeability of loss.[21] In *Chilean Sea Bass Inc. v. Kendell Seafood Imports, Inc.,* the seller ('CSB') and the buyer ('Kendell') concluded a contract in January 2020, when the COVID-19 pandemic started, for supplying more than 350 tons of Antarctic toothfish. Soon after, COVID-19 disrupted both domestic and international fishing markets, causing significant losses to both parties. CSB then claimed that Kendell violated the terms of the agreement and owed $2,549,749.70. Kendell contends that Pedro Grimaldi, an affiliate of CSB, legitimately altered the contract by lowering the price in order to mitigate the pandemic's impact on the market and preserve the commercial partnership. The US District Court notes that Kendell and CSB entered a valid modification in March 2020 to reduce the price by $6 per kilo and Kendell did not pay the amount owed under this modification, the Court finds Kendell breached its modified contract. Damages must be foreseeable based on what Kendell knew, or ought to have known, at the time of the modification. Id., art. 74. It was foreseeable, when Kendell agreed to a $6 per kilo modification, that failure to pay would result in substantial and calculable losses to CSB.[22]

The time of concluding contract is the appropriate time to evaluate foreseeability so that the parties have opportunity to protect themself. However, the author argues that

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[18] Patrick Selim Atiyah: The Rise and Fall of Freedom of Contract. *Clarendon Press*, (1979), 432–433; also A. L. Corbin: Corbin on Contracts: A Comprehensive Treatise on the Working Rules of Contract Law. *West Publishing Co* 5, (2002), 64–65.

[19] Murphey op. cit. 415.

[20] Robert Samek: The Relevant Time of Foreseeability of Damages in Contract. *The Australian Law Journal* 38, (1964), 125.

[21] Robin Cooke: Remoteness of Damages and Judicial Discretion. *The Cambridge Law Journal* 37, 2. (1978). 288–300.

[22] Chilean Sea Bass Inc. v. Kendell Seafood Imports, Inc., C.A no. 21-cv-337-JJM-LDA (2024) https://tinyurl.com/59hn255k (22 June 2024)

there are circumstances of wilful or negligent breach where measuring foreseeability at a later date may be justifiable.

2.7. Causality requirement and probability of loss

A party cannot foresee any result without awareness of the possible consequences to others. Therefore, causality plays a role in foreseeability loss determinations: not every harm or loss that could be foreseen should necessarily be included in a damage award. Each of the three instruments under discussion here incorporates a causality requirement: 'as being likely to result from its non-performance' (UPICC), 'as a likely result of its non-performance' (PECL) and 'as a possible consequence of the breach of contract' (CISG).

The UPICC and PECL only allow the harm/or loss to be recoverable once it is foreseeable as '(being) likely to result' from non-performance. In contrast, the CISG stipulates that the foreseeable loss must be 'a possible consequence of the breach of contract'. Ziegel distinguishes 'likely to result' or 'a likely result' from 'a possible consequence' with this example: 'If one takes a well-shuffled pack of cards it is quite possible, though not likely, that the top card will prove to be the nine of diamonds even though the odds are 51 to 1 against' (1994).[23] CISG's 'a possible consequence' seems broader than the requirement of 'likely (to) result' set out in the UPICC and PECL,[24] but this wider implication is limited by the previous phrase of 'in the light of the facts and matters of which he then knew or ought to have known',[25] the ability to foresee only works if the party can be aware of the relevant facts and matters. It is noted that the UPICC and the PECL contain no similar phrase; they appear to set more restrictive standards for foreseeability than the CISG.

Stoll states that 'there is only a need for factual causation inquiry as the foreseeability rule is employed in the place of the legal causation requirement'.[26] This requirement creates the causal relationship between the breach and the loss that Liu points out 'strongly overlaps the foreseeability rule'. He further states that there exists an interconnection between foreseeability and causation that cannot easily be separated. However, some scholars criticise this understanding on the ground that it leaves no room for the two concepts to be considered mutually exclusive.[27] A foreseeability rule can work consistently and flexibly with a causality rule.

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[23] Jacob Ziegel: Parker School Text as quoted. In: Albert H. Kritzer: Guide to Practical Applications of the United Nations Convention on Contracts for the International Sale of Goods. *Kluwer*, (1994), 587–588.

[24] Eiselen op. cit. 415

[25] Edward Allan Farnsworth: Damages and Specific Relief. *The American Journal of Comparative Law* 27, 2–3. (1979), 253. https://doi.org/10.2307/840031

[26] Hans Stoll: Comment Art 74. In: Peter Schlechtriem (ed.): *Commentary on the UN Convention on the International Sale of Goods (CISG)*. Oxford, Oxford University Press, 2nd ed., 1998.

[27] Liu op. cit. section 14.2.5.

2.8. What precisely needs to be foreseen?

The question of what precisely must be foreseen is not expressed clearly in the three instruments and therefore becomes a controversial topic in their formal comments. There are different interpretations of the international instruments regarding this issue without particular reason.[28] One of the Comments to the UPICC states that foreseeability pertains to the nature or type of harm rather than its extent unless the extent is significant enough to 'transform the harm into one of a different kind',[29] and the Comments to the PECL imply that both the type and the extent of the loss must be foreseen.[30] Commentators to the CISG interpret differently by arguing that what must be foreseen is not only the type and the extent of the loss but also the 'chain of events leading up to the loss'.[31] The type or nature of the loss is linked to a defining and integral feature of the notion of loss and it should be distinguished from the extent of the loss which relates to translating the limits of loss into money terms. Foreseeability to the extent of the loss is suggested by commentators in both PECL and CISG, whereas the Comments to the UPICC consider it is only possible if the extent is sufficient to alter the nature of harm. In *Zhejiang Xinlong Construction Co Ltd v Shaoxing Zhengxin Metal Trading Co Ltd*[32], the appellate court ruled that the failure to supply steel of the seller which resulted in the buyer's loss that ensued a 40% increase of the market price of steel, was foreseeable. Judge Yuan referred foreseeability to a universal consensus found in international treaties such as Article 7.4.4 of the UPICC and Article 74 of the CISG as the mirror because it is supported by Chinese law.[33] Notably, in dealing with the issue of whether the type or extent of a loss must be foreseen which was not solved by Chinese law, Judge Yuan considered only the type (not to extent) of a loss is subjected to the foreseeability test.[34] His view is similar to the approach advocated for Article 7.4.4 of the UPICC. In this case, the 40% rise of the market price was insufficient to

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28 Saidov op. cit. 126.

29 Official Comment to Art 7.4.4 UNIDROIT Principles 2016, 276.

30 Illustration 1, Comment A on art 9:503 PECL. In: Ole Lando – Hugh Beale (ed.): *Principles of European Contract Law: Parts I and II prepared by the Commission on European Contract Law*. The Hague, Kluwer Law International, 2000.

31 Hans Stoll – Georg Gruber: Arts 74–77 CISG. In: Peter Schlechtriem – Ingeborg Schwenzer (ed.): *Commentary on the UN Convention on the International Sale of Goods*. Oxford, OUP, 2nd edn, 2005. 766.

32 [浙江信龙建设有限公司与绍兴正欣金属物贸有限公司产品购销合同纠纷上诉案], Shaoxing IPC, (2018) Zhe 06 Min Zhong No 1634, rev'g Shaoxing Yuecheng District People's Court, (2018) Zhe 0602 Min Chu No 565.

33 Yuan Xiaoliang: The People's Judicature, 35/2019, 83 at 85. Also, Chinese Contract Law art 113.; Chinese Civil Code art 584.; also, Guiding Opinions of the Supreme People's Court on Several Issues Concerning the Adjudication of Cases Involving Civil or Commercial Contract Disputes under the Current Situation [最高人民法院关于当前形势下审理民商事合同纠纷案件若干问题 的指导意见], Fa Fa [2009] 40 (issued and effective as of 7 July 2009) art 10.

34 Qiao Liu: The PICC in Chinese Courts. *Uniform Law Review* 27, 3. (2022), 472. https://doi.org/10.1093/ulr/unac027; City University of Hong Kong School of Law Legal Studies Research Paper No. 2022 (2) – 005, 24–25.

translate the harm into one of a different kind as described in the Comments to Article 7.4.4 of the UPICC. One case where foreseeability of the extent of the loss is implied. In this case, the Appellate Court refused the expert's calculations of the "foreseeable damage" should be 120% of the base market price as the correct determination of the foreseeable damage. Instead, the Court set the limit of foreseeable damage at 20% of the agreed price, based on the calculations presented by the expert. It is further explained by the Supreme Court that because the market price increased significantly beyond the reasonably acceptable limit of contractual risk after the contract was concluded, the seller was released from obligation for 80% of the harm claimed by the buyer.[35]

If only the type of loss is required to foresee, the parties may find it challenging to establish reasonable expectations about the potential financial liabilities in case of breaching contract. This brings uncertainty, especially in the international context, and therefore businessman tends to escape the international instruments and this may challenge the uniform application of the rules and rights around compensation to aggrieved parties.

2.9. Foreseeability in case the breach was deliberate or negligent

The question of whether a breach was deliberate or negligent also influences the determination of foreseeability. Some national legal systems award damages even for unforeseeable harm when the breach is caused by a party's intentional actions or gross negligence, but there is no such exception expressed in the UNIDROIT Principles and the CISG. Neither of the latter instrument awards full compensation for harm or loss, even it is impossible to foresee, in case of a deliberate breach. In contrast, the PECL addresses the issue of intentional or grossly negligent breach. The non-performing party is not exempted from liability for losses from intentional or grossly negligent non-performance if such losses were unforeseeable; instead, the PECL awards full compensation.[36] This distinguishes it from the other two instruments, which take fault as a basis.

3. Conclusion

Generally, foreseeability under the three regulatory frameworks requires the parties, at the time a contract concludes, to be able to anticipate and assess the potential risks and liabilities they could incur during the performance of the contract. Even though the three sets of rules seem very reminiscent of one other, the wording of foreseeability in the PECL is broader than in the other instruments. This is because of the wide application of PECL to the contract law which includes international commercial contracts, domestic as well as consumer contracts. A comparison of the texts of foreseeability rule under the three instruments reveals that the variations in wording among the three instruments are insignificant and do create not a huge practical impact.

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[35] Case no. V CSK 254/14, available at https://cisg-online.org/search-for-cases?caseId=12977 (28 June 2024)

[36] Liu op. cit. section 14.2.6.

The three international instruments have tried to standardise the rule, but confusion remains regarding interpreting the different foreseeability clauses. All the three instruments face the same issues: ambiguity surrounding the term and scope of foreseeability, and the burden of proof of foreseeability. There are also debates on the issue of fixing the time when harm or loss should be foreseen to the time of conclusion of the contract. The lack of clarity on what precisely must be foreseen as well as the differing interpretations by commentators to the three instruments will lead to inconsistent application of the instruments and create uncertainty about the injured party's right to be compensated and its amount. However, there is no need to follow a more specific but precise approach because a broad and flexible method remains balanced and effective for various circumstances, especially in the global commercial environment. The widespread application of the foreseeability rule by international instruments demonstrates its effectiveness in limiting damages in a modern and global context.

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