CISG Advisory Council* Opinion No. 10
Agreed Sums Payable upon Breach of an Obligation in CISG Contracts

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INGEBORG SCHWENZER, Chair
MICHAEL BRIDGE, ERIC E. BERGSTEN JOACHIM BONELL, ALEJANDRO M. GARRO, HAN SHIYUAN, ROY M. GOODE, JOHN Y. GOTANDA, SERGEI N. LEBEDEV, PILAR PERALES VISCASILLAS, JAN RAMBERG, HIROO SONO, CLAUDE WITZ, Members
SIEG EISELEN, Secretary*

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OPINION

1. The Convention governs the incorporation in the contract and interpretation of clauses providing for the payment of agreed sums for failure to perform the contract (“agreed sums”).

2. According to the principle of freedom of contract laid down in Article 6 CISG the parties may derogate from Articles 74 – 79 CISG by including such clauses.

3. The CISG does not exclude provisions on the protection of the obligor of the otherwise applicable law or rules of law, except for form requirements.

4. (a) Provisions on the protection of the obligor of the otherwise applicable law or rules of law relying on notions such as reasonableness, excessiveness or proportionality must be applied in accordance with an international standard. This standard must be developed from the underlying principles of the CISG.

(b) In an international context, agreed sums do not fail such provisions on the sole grounds that they compel the obligor to perform.

5. Whether an impediment exempts the obligor from payment of the agreed sum is primarily a matter of interpretation of the contract under Articles 8 and 9 CISG.

Unless otherwise agreed, Article 79(1) CISG exempts the obligor from the obligation to pay an agreed sum.

6. Where the obligee has contributed to the failure of the obligor triggering the agreed sum, it is barred by Article 80 CISG from relying on agreed sums to the extent that it has caused the breach.

7. A failure to take reasonable measures to mitigate the loss (Article 77) does not affect the amount recoverable as an agreed sum.

8. The relationship of agreed sums to the default remedies of the CISG for breach of contract is primarily a matter of interpretation of the contract under Articles 8 and 9 CISG. Unless otherwise agreed the following rules apply:

(a) Specific performance may be claimed in addition to the agreed sum, only if the agreed sum is not meant to replace performance of the contract.

(b) Avoidance of the contract does not affect an agreed sum (Article 81(1) CISG).

(c) In addition to the agreed sum no further damages may be claimed.

COMMENTS

1. The Convention governs the incorporation in the contract and interpretation of clauses providing for the payment of agreed sums for failure to perform the contract (“agreed sums”).

Rule 1 repeats the undisputed view that Articles 14 – 24 CISG govern the incorporation of agreed sums.¹
2. According to the principle of freedom of contract laid down in Article 6 CISG the parties may derogate from Articles 74 – 79 CISG by including such clauses.

2.1 Comparative Overview

2.1.1 Agreed sums payable upon breach of an obligation are a frequent feature in sales contracts. Today, parties are free to include such clauses in Civil Law systems. Excessive sums are typically subject to reduction. The Nordic systems likewise recognise the concept of agreed sums, although there are no specific rules in the respective Contracts Acts. In terms of their validity, the Nordic systems treat them as every other clause in the contract. This means that a modification of excessive sums is possible under the provisions allowing for a modification of unconscionable terms in a contract.

2.1.2 In Common Law jurisdictions the distinction of penalty and liquidated damages clauses is of far greater importance than in Civil Law jurisdictions. Originating in the development of equitable relief against penal bonds, traditional Common Law denies enforceability to clauses that are found to act in terrorem and are thus classified as penalties; liquidated damages on the other hand are enforceable under Common Law. At its simplest, the courts require that the agreed sum be a genuine pre-estimate of the loss. This approach is today also followed in other legal systems of Common Law descent, although there are notable exceptions, even within Common Law systems.

2.1.3 Mixed Jurisdictions are divided on the subject of agreed sums. The Philippines and South Africa have established rules corresponding to those of Civil Law legal systems. Although somewhat ambiguous, the same approach can be inferred for Israel. Scotland has traditionally followed the English approach. However, under the anticipated Penalty Clauses (Scotland) Bill the court may modify sums that are manifestly excessive.

2.1.4 At the international level the first steps were taken by the 1973 Convention Benelux Relative à la Clause Pénal. In the aftermath of the drafting of the CISG UNCITRAL in 1983 finalised the Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance. Subsequent followers to the UNCITRAL Rules are Article 7.4.13 UNIDROIT Principles of International Commercial Contracts in 1994, 2004 and 2010, Article 9:509 Principles of European Contract Law in 1999 and Article III.–3:712 of the Draft Common Frame of Reference in 2009. The approach taken by the UNCITRAL Rules and its followers dispenses with the distinction of penalty and liquidated damages clauses. Rather, all agreed sums are upheld, subject to reduction in case of excessiveness. An essentially identical approach is also taken by Article 170 of the European Code of Contract published by the Gandolfi Initiative in 2001.

2.2 The Position of the CISG

Rule 2 of this opinion acknowledges the frequency of agreed sums in commerce and reemphasises the freedom of the parties to include such clauses into their contract. Courts and arbitral tribunals have based this principle either on Article 6 or on Article 45(2). Since penalty and liquidated damages clauses are inseparably intertwined with the law of damages, such clauses affect Articles 74 – 77, 79, 80 of the Convention.

3. The CISG does not exclude provisions on the protection of the obligor of the otherwise applicable law or rules of law, except for form requirements.

3.1 Rule 3 addresses the interplay of the Convention and domestic rules protecting the obligor.

3.2 Legal systems have developed different mechanisms to offer protection for the obligor. These can be summarised as follows: Legal systems may establish specific formal requirements for agreed sums; legal systems may fix the maximum amount of such sums; legal systems may deny enforceability to agreed sums classified as penalties; legal systems may provide for the reduction of excessive sums. Furthermore, the obligor may be protected by general provisions exempting it from liability.
3.3 From the perspective of the CISG, all of these protection mechanisms concern the validity of agreed sums. Where domestic laws establish fixed amounts for agreed sums,19 these provisions determine to what extent an agreed sum is valid. Where a legal system denies enforceability to agreed sums classified as penalties,20 the function of the clause determines the validity of the entire clause. Where a legal system provides for the reduction of excessive sums, such provisions determine the extent to which an agreed sum is valid. As the CISG is not concerned with questions of validity – Article 4 sentence 2(a) CISG – domestic protection mechanisms generally remain applicable to agreed sums in CISG contracts.

3.4 Courts and arbitral tribunals have therefore rightly applied domestic protection mechanisms against agreed sums also where such clauses were incorporated in CISG contracts.21 In particular, it has been denied that a reduction mechanism could be based on Articles 8 and 77.22 In one case, it was, however, held, that the reduction mechanism established in Article 7.4.13(2) PICC 1994 satisfied the requirements of an international trade usage under Article 9(2) and on that account was held applicable.23

3.5 Rule 3 contains an exception to the general rule for domestic form requirements. These are not applicable on account of Article 11 CISG. Some domestic legal systems, especially in Eastern Europe and Central Asia, have established specific formal requirements to be met by agreed sums.24 Article 4 sentence 2(a) CISG, however, defers questions of validity to domestic "except as otherwise expressly provided in this Convention". Article 11 CISG, which establishes the freedom of form, is unanimously perceived to be such an exception, that is, this provision governs a validity question.

3.6 One court decision has, however, held that despite Article 11 CISG domestic formal requirements specifically addressing agreed sums remain applicable as the Convention did not contain any provisions dealing with agreed sums.25 The better view, which is adopted in Rule 3, is to give Article 11 CISG a broad meaning so as to eliminate all domestic form requirements for the sales contract or any of its clauses, unless Articles 90, 96 CISG lead to a different result.

4. (a) Provisions on the protection of the obligor of the otherwise applicable law or rules of law relying on notions such as reasonableness, excessiveness or proportionality must be applied in accordance with an international standard. This standard must be developed from the underlying principles of the CISG.

(b) In an international context, agreed sums do not fail such provisions on the sole grounds that they compel the obligor to perform.

4.1 General

4.1.1 Rule 4 addresses the application of domestic validity tests as envisaged by Rule 3 to agreed sums contained in CISG contracts. Independent of the individual approach taken by a legal system the subject matter is always whether and to what extent a clause is upheld in a contract. From a functional perspective, some legal systems completely invalidate clauses while others partially invalidate them by reduction of the sum agreed upon; then again, some legal systems uphold clauses in their entirety and only subject to unconscionability and immorality, which is again a question of validity.

4.1.2 The most prominent protection mechanisms against agreed sums are the unenforceability of clauses classified as penalties and the reduction of excessive sums. As noted earlier,26 the first approach is primarily taken by Common Law legal systems, while the second is typical for Civil Law legal systems, Nordic systems, Mixed systems and also for international instruments.
4.1.3 As regards these mechanisms, independent of the individual approach taken by a legal system the subject matter is always whether and to what extent a clause is upheld in a contract. From a functional perspective, some legal systems completely invalidate clauses while others partially invalidate them by reduction of the sum agreed upon; then again, some legal systems uphold clauses in their entirety and only subject to unconscionability and immorality, which is again a question of validity.

4.2 Interpretation of Domestic Tests Under the CISG

4.2.1 The CISG is part of the law of every Contracting State. More specifically, it is that part of state law which governs international sales contracts. Thus, where purely domestic provisions are needed to supplement this part of the law it makes sense to interpret them in a way so as to reflect the international dimension of this area of the law. In other words, a clause that may be unreasonable in domestic sales is not necessarily unreasonable in an international setting.

4.2.2 From this finding it follows that when applying tests such reasonableness, proportionality or whether an agreed sum is a genuine pre-estimate of the loss, these must be assessed against an international standard to be derived from the CISG. To put it in traditional terms of legal systems prohibiting penalties: Whether a sum stipulated is a genuine pre-estimate of the loss – which in the end is always a test of reasonableness – must not be decided in accordance with domestic case law but in light of what is reasonable in international trade. To put it in traditional terms of legal systems employing a reduction mechanism: Whether a clause is excessive under the circumstances and thus to be reduced is not to be decided in light of what is held to be excessive in domestic contracts, but is to be determined by applying an international standard.

4.3 The Standard of the CISG

4.3.1 Determining the standard established by the CISG means interpreting the Convention under Article 7(1) CISG. It is necessary to determine, whether the possibility of inducing performance by making use of an agreed sum is also part of the international standard established by the CISG, ie whether party autonomy provides sufficient grounds in international trade to do so.

4.3.2 The possibility to induce performance by an agreed sum is recognised in most Civil Law legal systems, Mixed Jurisdictions, Nordic legal systems and in international instruments. The mandate of Article 7(1) CISG requires the standard also to be acceptable to those legal systems which take a different stance. This relates to those legal systems that protect the obligor by denying enforceability to clauses classified as penalties. Here, it is justifiable that the test of whether an agreed sum is a genuine pre-estimate of the loss in international sales contracts can also be passed by clauses inducing performance by the respective counter-party.

4.3.3 A closer analysis of the developments in Common Law jurisdictions reveals that the traditional rule has come to be seen as a rare departure from the general principle of freedom of contract and is perceived to be a relic from the age of English courts of equity protecting obligors in penal bonds.27 The traditional Common Law approach has been labelled an anomaly,28 with its underlying ratio being ‘mysterious’29 and remaining ‘one of the abiding mysteries of the common law’30 which in the end turns out to be an ‘anachronism, especially in cases in which commercial enterprises are on both sides of the contract’.31 In a similar vein Lord Diplock had stated in Robophone Facilities Ltd v Blank: ‘I will make no attempt, where so many others have failed, to rationalise this common law rule. It seems sui generis.’32 Others speak of an ‘accident of legal history’.33

4.3.4 Furthermore, there is increasing acceptance of the notion that the law of damages protects the interest in the performance of the contractual obligations owed and not merely the economic balance sheet. In comparative law discussion this development is typically described as a paradigm shift from the ‘economic benefits principle’ to the ‘performance principle’.34 Under this latter principle the law of damages is considered to function as an enforcement of contractual obligations.35
4.3.5 A vivid example is *Attorney-General v Blake*. The majority of the Law Lords reasoned that ‘the law recognises that damages are not always a sufficient remedy for breach of contract. [...] Even when awarding damages, the law does not adhere slavishly to the concept of compensation for financially measurable loss. When the circumstances require, damages are measured by reference to the benefit obtained by the wrongdoer.’ One commentator has noted that an agreed sum providing for the disgorgement of benefits derived from breach of contract under the traditional rule would clearly fail to be a liquidated damages clause but that ‘it would seem odd to knock out such a clause as a penalty at least in a situation where the courts would otherwise be willing to award an account of profits or restitutionary damages’.

4.3.6 Further evidence for a changing perception of the law of damages – although not directly related to international sales contracts – can be derived from an increasing tendency to either grant or advocate punitive damages also in breach of contract actions.

4.3.7 Putting together these developments, the exception made for agreed sums from the general principle that terms freely entered into have to be strictly enforced may see a change in the near future. It follows, that where the CISG provides the backdrop for the general test of reasonableness to be carried out under the genuine pre-estimate of loss test, agreed sums should not fail the genuine pre-estimate of the loss test simply because they seek to induce performance of the obligation owed. Rather, they should fail this test if they are excessive in relation to that goal, ie where they are disproportionate in the context of the individual contractual relationship.

4.3.8 Consequently, agreed sums in CISG contracts should generally be upheld independent of the function they assume. Domestic tests of validity employing a standard of reasonableness have to be applied against the background provided by the CISG. This background provides that the mere fact that a clause secures performance as owed under the contract is not sufficient for the agreed sum to fail the test of unreasonableness. However, the CISG does not provide any guidelines as to the legal consequences should the clause in question be held to be unreasonable, ie to not be a genuine pre-estimate of loss or an excessive sum. This issue is exclusively for the applicable domestic law to decide.

5. Whether an impediment exempts the obligor from payment of the agreed sum is primarily a matter of interpretation of the contract under Articles 8 and 9 CISG. Unless otherwise agreed, Article 79(1) CISG exempts the obligor from the obligation to pay an agreed sum.

5.1 Rule 5 addresses the constellation where the breach of the obligor triggering the agreed sum is caused by an impediment beyond control that it was neither able to foresee nor to overcome or at least its consequences. In such situations, absent any agreement to the contrary, Article 79 CISG exempts the obligor from the obligation to pay damages. Rule 5 provides the same result with regard to the agreed sum.

5.2 Attempts to expressly extend Article 79 CISG to agreed sums at the Vienna Conference were not successful. In court practice on the CISG, this problem has apparently only arisen in one case but was left open by the court as the results would not have differed in that case. Article 7(1) CISG dictates that its interpretation has to give due regard to the international character of the CISG. In light of the fact that Article 5 UNCITRAL Rules, the official Comment 2 on Article 7.4.13 PICC and the vast majority of domestic legal systems hold the obligor only liable for the agreed sum where it is liable for the non-performance, Article 79 CISG should be interpreted – absent any indications by the parties to the contrary – as relieving the obligor from an agreed sum where the requirements of that provision are met.

6. Where the obligee has contributed to the failure of the obligor triggering the agreed sum, it is barred by Article 80 CISG from relying on agreed sums to the extent that it has caused the breach.
6.1 Rule 6 addresses situations where the obligee of the agreed sum has contributed to the breach triggering the agreed sum. This may for instance occur where the FOB-buyer is late in naming the vessel or gives wrong instructions regarding loading points and schedules thus delaying delivery. In these instances Article 80 CISG prevents the aggrieved party from relying on the breach to the extent that it has contributed to it.

6.2 Rule 6 clarifies that Article 80 also applies to agreed sums. Hence, the contribution of the obligee made to the breach must be reflected in a proportional reduction of the agreed sum.

7. A failure to take reasonable measures to mitigate the loss (Article 77) does not affect the amount recoverable as an agreed sum.

7.1 Rule 7 deals with the interplay of the general duty to mitigate losses and the agreed sum payable by the breach of the obligor. The CISG clearly distinguishes contribution to breach by the obligee and mitigation of losses incurred. As a starting point – and in contrast to Article 80 – Article 77 does not have any impact on the fact that the agreed sum is triggered in its full amount. Under the CISG the failure to mitigate losses on the side of the obligee does not impact the amount that must be paid by the obligor. Agreed sums are payable upon breach independent of whether an actual loss has occurred. If it is generally irrelevant, whether a loss has occurred it cannot be of relevance, whether that loss is an unmitigated or a mitigated one. Articles 74 – 77 are rules for calculating damages. Where, however, an agreed sum is stipulated in the contract, the parties have taken care of this necessity in advance. In particular, Article 77 does not contain a reduction mechanism.

7.2 In addition, if Article 77 CISG were considered relevant to the amount of the agreed sum, would then be necessary to determine the actual loss and the amount that could have been avoided. These questions are prone to lead to disputes between the parties and prevent a quick and efficient resolution of the dispute. This, however, would defeat the exact purpose of the agreed sum. At the domestic level this issue has been raised in statements to the effect concepts of liquidated damages and mitigation are fundamentally different and do not influence each other.

7.3 Furthermore, it appears preferable to leave it to the obligee whether it decides to take mitigating measures. The economic incentive to take mitigating measures is to reduce the actual loss and recover the sum in full. The economic risk of not taking mitigating measures is that the actual loss may exceed the agreed sum and that the obligee then cannot recover the outstanding part.

8. The relationship of agreed sums to the default remedies of the CISG for breach of contract is primarily a matter of interpretation of the contract under Articles 8 and 9 CISG. Unless otherwise agreed the following rules apply:

(a) Specific performance may be claimed in addition to the agreed sum, only if the agreed sum is not meant to replace performance of the contract.

(b) Avoidance of the contract does not affect an agreed sum (Article 81(1) CISG).

(c) In addition to the agreed sum no further damages may be claimed.

8.1 General

8.1.1 Rule 8 addresses the relationship of the agreed sum triggered by the breach to the general remedies available in case of breach of contract.

8.1.2 This is not a question of validity and despite recurring statements to the contrary should therefore not be dealt
with under domestic law. The CISG is exclusively in charge of determining its sphere of application and thus of its remedies for breach of contract. Naturally, it is first and foremost up to the parties to make provision for the remedies available (Article 6 CISG) subject to the boundaries set by the applicable domestic law (Article 4 sentence 2(a) CISG). The first step is thus always the interpretation of the clause in dispute in accordance with Articles 8, 9 CISG. If this does not lead to a solution the following guidelines apply.

8.2 Specific Performance

8.2.1 Legal systems agree that the mere presence of an agreed sum does not in and of itself exclude the remedy of specific performance. The majority of legal systems provides by default that the obligee cannot cumulatively claim the agreed sum and specific performance where the agreed sum was incorporated into the contract precisely to remedy total non-performance, eg non-delivery, as this would lead to double recovery.

8.2.2 Where on the other hand the agreed sum is incorporated to remedy improper performance, the obligee can cumulatively request payment of the agreed sum and specific performance. This is particularly the case where the agreed sum is stipulated for situations of delay, which have been hat issue in the vast majority of cases dealing with agreed sums in CISG contracts.

8.2.3 An interpretation of the Convention under Article 7(1) CISG having regard to the international character of the CISG suggests that this approach to specific performance also has to be adopted as the default rule under the Convention.

8.3 Avoidance of the Contract

8.3.1 Under Rule 8 b. avoidance of the contract does not bar the obligee from recovering the agreed sum triggered by the breach of contract. This is consistent with the general concept of the CISG to allow for the combination of avoidance of contract and damages for breach of contract.

8.4 Damages

8.4.1 Rule 8 c. clarifies that unless the parties agree otherwise, the obligee may not recover any losses exceeding the agreed sum. The matter is therefore first of all of interpretation of the parties' agreement under Articles 8 and 9.

8.4.2 At the domestic level the position among legal systems is split with regard to the relationship of agreed sums to the remedy of damages for breach of contract. One view is that as a general rule the obligee should not be entitled to any additional losses. Exceptions are typically only made where the obligor has acted intentionally or fraudulently. In other legal systems, courts are granted the possibility to increase the sum. In some systems courts seem to enjoy broad discretion, as the right to adjust the agreed sum in question appears not to be subject to any qualifications. Other legal systems granting this possibility to courts, however, require that the agreed sum be disproportionately low (‘dérisoire’, ‘ínfimo’). In systems prohibiting penalties, the obligor may not be able to invoke an unreasonably low agreed sum on the grounds of unconscionability, thus leaving the obligee with its ordinary claim for damages.

8.4.3 The other view is that a claim for additional damages is generally admissible with the sum being set off against the claim by default.

8.4.4 At the international level the UNCITRAL Rules attempt to strike a balance between both positions on the availability of a claim for additional losses. First of all, Article 7 sentence 1 states that no damages may be claimed to the extent the loss is covered by the agreed sum. This is parallel to domestic rules setting off the agreed sum against the damage claim. *E contrario* – ‘to the extent’ – it follows that beyond the extent of the loss covered by the agreed sum damages may be claimed. The middle ground approach taken by the UNCITRAL Rules is then evidenced in Article 7 sentence 2. This provision restricts the availability of a claim for additional damages to cases where the loss ‘substantially exceeds the agreed sum’.
8.4.5 Also in this context it is up to the parties to make provision for this issue. It is highly advisable that phrases such as “to the exclusion of additional claims” or “without prejudice to other claims” be used. On account of Article 6 CISG, the Convention does not object to either of the two solutions. However, the applicable domestic law may take a different stance and strike down clauses which allow for cumulative requests for the agreed sum and damages for breach of contract.

8.4.6 It follows from this result that where under the CISG additional claims may not be recovered, because the agreed sum is exclusive in nature, domestic provisions allowing courts and arbitral tribunals to increase the amount payable are pre-empted. The results found by the Convention must not be circumvented by domestic law. If a sum is unreasonably low a legal system is not prevented from declaring these clauses invalid for reasons of unconscionability or equivalent concepts.

** The CISG-AC is a private initiative supported by the Institute of International Commercial Law at Pace University School of Law and the Centre for Commercial Law Studies, Queen Mary, University of London. The International Sales Convention Advisory Council (CISG-AC) is in place to support understanding of the United Nations Convention on Contracts for the International Sale of Goods (CISG) and the promotion and assistance in the uniform interpretation of the CISG.

At its formative meeting in Paris in June 2001, Prof. Peter Schlechtriem of Freiburg University, Germany, was elected Chair of the CISG-AC for a three-year term. Dr. Loukas A. Mistelis of the Centre for Commercial Law Studies, Queen Mary, University of London, was elected Secretary. The founding members of the CISG-AC were Prof. Emeritus Eric E. Bergsten, Pace University School of Law; Prof. Michael Joachim Bonelli, University of Rome La Sapienza; Prof. E. Allan Farnsworth, Columbia University School of Law; Prof. Alejandro M. Garro, Columbia University School of Law; Prof. Sir Roy M. Goode, Oxford, Prof. Sergei N. Lebedev, Maritime Arbitration Commission of the Chamber of Commerce and Industry of the Russian Federation; Prof. Jan Ramberg, University of Stockholm, Faculty of Law; Prof. Peter Schlechtriem, Freiburg University; Prof. Hiroo Sono, Faculty of Law, Hokkaido University; Prof. Claude Witz, Universität des Saarlandes and Strasbourg University. Members of the Council are elected by the Council. At subsequent meetings, the CISG-AC elected as additional members Prof. Pilar Perales Viscasillas, Universidad de La Rioja; Professor Ingeborg Schwenzer, University of Basel; Prof. John Y. Gotanda, Villanova University; and Prof. Michael G. Bridge, London School of Economics, Prof HAN Shiyuan, Tsinghua University, Beijing; Prof. Jan Ramberg served for a three-year term as the second Chair of the CISG-AC. At its 11th meeting in Wuhan, People’s Republic of China, Prof. Eric E. Bergsten of Pace University School of Law was elected Chair of the CISG-AC and Prof. Sieg Eiselen of the Department of Private Law of the University of South Africa was elected Secretary. At its 14th meeting in Belgrade, Serbia Profession Ingeborg Schwenzer, University of Basel was elected Chair of the CIG-AC.


2 See for Argentina Art 652 CC; Armenia Art 369 CC; Austria § 1336(1) CC; Belarus Art 311 CC; Belgium Art 1226 CC; Bolivia Art 532 CC; Brazil Art 408 CC; Bulgaria Section 92 OCA; Cambodia art 403 CC; Chile Art 1535 CC; China Art 114 Contract Law; Colombia Art 1592 CC; Costa Rica Art 708 CC; Croatia Art 350 Civil Obligations Act; Czech Republic § 544 CC; Ecuador Art 1578 CC; Egypt Art 223 CC; El Salvador Art 1406 CC; Georgia Art 417 CC; France Art 1226 CC; Germany § 339 CC; Greece Art 405 CC; Estonia § 158 Law of Obligations Act; France Art 1226 CC; Italy Art 1382 CC; Iraq Art 170 CC; Iran Art 230 CC; Japan Art 420 CC; Jordan Art 364 CC; Republic of Korea Art 398 CC; Latvia Art 1716 CC; Lebanon Art 266 Code of Obligations and Contracts; Lithuania Art 6.71 CC; Luxembourg Art 1226 CC; Macau Art 799 CC; Mexico Art 1841 CC; Moldova Art 624 CC; Mongolia Art 232 CC; the Netherlands Art 6.91 CC; Nicaragua Art 1985 CC; Panama Art 1039 CC; Paraguay Art 454 CC; Peru Art 1341 CC; Poland Art 481(1) CC; Portugal Art 812 CC; Romania Art 1066 CC; Russia Art 330 CC; Slovakia § 544 CC; South Korea Art 398 CC; Spain Art 1152 CC; Switzerland
Art 160 CO; Syria Art 224 CC; Taiwan Art 250 CC; Uruguay Art 1363 CC; Venezuela Art 325 CC; Vietnam Art 422 CC; Yemen Art 348 CC.

Some Civil Law legal systems do not establish express reduction mechanisms. This is eg the case in the Czech Republic, Costa Rica, Latvia and Slovakia. In Japan Art 420(1), sentence 2 CC expressly states that the court may not increase or decrease the amount of liquidated damages. Art 420(3) CC equates penalties and liquidated damages. The same applies under Iran Art 230 CC.

See for Argentina Art 656 CC; Armenia Art 372 CC; Austria § 1336(2) CC; Belarus Art 314 CC; Bulgaria Section 92 OCA; Chile Art 1539 CC; China Art 114 Contract Law; Colombia Art 1601 CC; Croatia Art 354 Civil Obligations Act; Ecuador Art 1587 CC; Egypt Art 224(2) CC; El Salvador Art 1415 CC; France Arts 1231, 1152 CC; Georgia Art 420 CC; Germany § 343 CC; Greece Art 409 CC; Estonia § 162 Law of Obligations Act; France Art 1152 CC; Italy Art 1384 CC; Iraq Art 171(2) CC; Iran Art 230 CC; Jordan Art 364(2) CC; Republic of Korea Art 398(2) CC; Lebanon Art 266(2) Code of Obligations and Contracts; Lithuania Art 6.73(2) CC; Luxembourg Arts 1231, 1152 CC; Macau Art 801 CC; Mexico Arts 1844, 1845 CC; Moldova Art 630(1) CC; Mongolia Art 232(8) CC; the Netherlands Art 6.94 CC; Panama Art 1041 CC; Paraguay Art 459 CC; Peru Art 1346 CC; Poland Art 484(2) CC; Portugal Art 812 CC; Romania Art 1070 CC; Russia Art 333 CC; South Korea Art 398(2) CC; Spain Art 1154 CC; Switzerland Art 163 CO; Syria Art 225(2) CC; Taiwan Art 252 CC; Uzbekistan Art 326 CC; Venezuela Art 1260 CC; Yemen Art 354 CC.


See for Denmark Art 36 Contracts Act; Finland Section 36 Contracts Act; Norway Art 36 Contracts Act; Sweden § 36 Contracts Act; Iceland Art 36 Contracts Act. Cf also Dimatteo, op cit (n. 5), at p 655.


See for India Section 74 Contracts Act (1872); Pakistan Section 74 Contracts Act (1872). In Malaysia Section 75 Contracts Act (1950) explicitly provides for the enforceability of agreed sums, even if classified as penalties. However, the Malayan Supreme Court has interpreted this provision to the contrary, see Selva Kumar A/L Murugiah v Thiagarajah A/L Rethinasamy [1995] 1 MJL 817; criticism from Mohd Danuri/Ch Munaim/Yen, Liquidated Damages in the Malaysian Standard Forms of Construction Contract: The Law and the Practice, (2009) 25 Constr L J 103 et sqq.


See for the Philippines Art 1229 CC; South Africa Arts 1, 3 Conventional Penalties Act (1962).

See for Israel Art 15 Contracts (Remedies for Breach of Contract) Law which speaks of ‘agreed compensation’ under the heading of ‘liquidated damages’.


At the time of writing the consultation process had finished but the bill has not been passed yet.

See Art 8 UNCITRAL Rules; Art 7.4.13(2) PICC; Art 9:509(2) PECL; Art III.-3:712(2) DCFR. See also Art 4(1) Convention Benelux.

Art 170(4) ECC.


See for Bolivia Art 534 CC; Brazil Art 412 CC; Mexico Art 1843 CC; Mongolia Art 232(4) CC; Portugal Art 811(3) CC; Vietnam Art 378 Contract Law.

See for this mechanism in traditional Common Law supra para 2.1.2.

With regard to the invalidity of an agreed sum RB Hasselt, 21 January 1997, CISG-online 360 (domestic Belgian law
applied, clause invalid). With regard to the reduction of excessive sums see Hof van Beroep Antwerp, 18 June 1996, CISG-online 758 (domestic French law applied); Gerechtshof Arnhem, 22 August 1995, CISG-online 317 (domestic German law applied under which a reduction was denied); CIETAC, 7 December 2005, CISG Pace (domestic Chinese law applied); CIETAC, 9 November 2005, CISG-online 1444 (domestic Chinese law applied); CIETAC, 6 February 1997, CISG Pace (domestic Chinese law applied); Tribunal of International Commercial Arbitration at the Russian Federation Chamber of Commerce and Industry, 27 April 2005, CISG-online 1500 (domestic Russian law applied); Tribunal of International Commercial Arbitration at the Russian Federation Chamber of Commerce and Industry, 19 March 2004, CISG-online 1186 (domestic Russian law applied); Tribunal of International Commercial Arbitration at the Russian Federation Chamber of Commerce and Industry, 19 February 2004, CISG-online 1182 (domestic Russian law applied); Tribunal of International Commercial Arbitration at the Russian Federation Chamber of Commerce and Industry, 4 April 2003, CISG-online 1547 (domestic Russian law applied); Tribunal of International Commercial Arbitration at the Russian Federation Chamber of Commerce and Industry, 10 January 1998 CISG-online 2122 (domestic Russian law applied).


24 See for Armenia Art 370 CC; Belarus Art 312(1) CC; Georgia Art 418(2); Kazakhstan Art 294 CC; Kirgizstan Art 321 CC; Lithuania Art 6.72 CC; Moldova Art 625(1) CC; Mongolia Art 232.3 CC; Russia Art 330 CC; Slovakia § 544(2) CC; Tajikistan Art 356 CC; Turkmenistan Art 428 CC; Uzbekistan Art 261 CC.


26 See supra para 2.1.1 et seq.

27 For details see Hachem, op cit (n. 7), p 34 et seq.

28 See XCO International, Inc v Pacific Scientific Company, US Ct App (7th Cir), 24 May 2004, 369 F3d 998 at 1001: ‘Courts don’t review the other provisions of contracts for reasonableness; why this one?’


36 [2001] 1 AC 268 (HL). The spy Blake - in the words of Lord Nicholls of Birkenhead a ‘notorious, self-confessed traitor’, Attorney-General v Blake [2001] 1 AC 268 (HL) at 275 – had been a member of the Secret Intelligence Service (SIS) between 1944 and 1961. In 1951 he switched sides to the Soviet Union. In 1989 he wrote his autobiography which was published in 1990. In so doing, Blake violated the clause in his contract with SIS obliging him not to divulge any official information gained as a result of his employment. The information revealed by Blake, however, had been no longer confidential and their publishing did not damage public interest. The Crown sued for the 90’000 £ which Blake so far had not been paid under his publishing contract and which had by injunction been frozen. With a majority of four to one the Law Lords awarded the claimed sum to the Crown.

37 See Attorney-General v Blake [2001] 1 AC 268 (HL) at 285 per Lord Nicholls of Birkenhead.


39 See for the USA § 355 Restatement (2nd) of Contracts. In Canada the landmark decision is Whiten v Pilot Insurance Co, Can Sup Ct 22 February 2002, [2002] 1 SCR 595, majority vote delivered by Binnie J. The dissenting vote by LeBel J related only to the amount awarded. There were several decisions leading up to this decision, see already Ribeiro v Canadian Imperial Bank of Commerce, Ont Sup Ct, 9 February 1989, 67 OR 2d 385 where punitive damages were awarded for wrongful dismissal by a bank. In Vorvis v Insurance Corporation of British Columbia, Can Sup Ct, 4 May 1989, [1989] 1 SCR 1085 the court explicitly departed from the formula of the US § 355 Restatement (2nd) of Contracts which expressly speaks of ‘also a tort’. In her dissenting vote Wilson J even rejected this requirement and stated that it was the nature of the defendant’s conduct which was decisive. It was again pointed out in Royal Bank v W Got & Associates Electric Ltd, Can Sup Ct, 15 October 1999, [1999] 3 SCR 408 that – although rare – there are cases in which the circumstances justified punitive damages also in the absence of a tort. In England such statements can be found in Burrows, op cit (n. 40), p 409: ‘recent developments suggest that the rule in Addis [...] may require reconsideration in the

40See Schwenzer, Commentary (n 1), Art 79 CISG, para 51.


45At the domestic level fears have been voiced that this would then lead to wasteful failures to mitigate or, if mitigation is successful, overcompensate the obligee, see Beale, Remedies, p 57.


48Mohs/Zeller, op cit (n 46), at p 2.


50For details see Hachem, op cit (n 7), p 155 et seq.

51See for Austria § 1336(1) sentence 3 CC; Bolivia Art 533(1) CC; Brazil Art 1537 CC; Colombia Art 1594 CC; Costa Rica Art 426 Com C; Ecuador Art 1580 CC; El Salvador Art 1408 CC; France Art 1229(2) CC; Georgia Art 419(1) CC; Germany § 340(1) CC; Italy Art 1383 CC; Latvia Art 1718(1) CC; Lebanon Art 266 Code of Obligations and Contracts; Lithuania Art 6.73.1(1) sentence 1 CC; Mexico Art 1846 CC, Art 88 Com C; Moldova Art 626(1); the Netherlands Art 6.92(1) CC; Paraguay Art 458 CC; Peru Art 1341 CC; Portugal Art 811(1) CC; Spain Art 1153(2) CC, Art 56 Com C; Switzerland Art 160(1) CO; Uruguay Art 288 para. 2 Com C; USA Perillo, Corbin on Contracts. A Comprehensive Treatise on the Rules of Contract Law, vol XI Damages, Newark/San Francisco: LexisNexis Mathew Bender (2005), p 513; Venezuela Art 1258 CC. In China this follows e contrario from Art 114(3) Contract Law.

52See for Argentina Art 659 CC; Austria § 1336(1) sentence 3 CC; Bolivia Art 533(1) CC; Brazil Art 411 CC; Chile Art 1537 CC; China Art 1143(3) Contract Law; Columbia Art 1594 CC; Ecuador Art 1580 CC; France Art 1229(2) CC; Georgia Art 419(1) CC; Germany § 341(1) CC; Italy Art 1383 CC; Latvia Art 1720 No 2 CC; Lebanon Art 266 Code of Obligations and Contracts; Lithuania Art 6.73(1) sentence 1 CC; Mexico Art 1846 CC; Moldova Art 626(1); Switzerland Art 160(2) CO; USA Perillo, op cit (n 51), p 513; Art 170(3) ECC.

53See for Algeria Art 185 CC; Argentina Art 655 CC; Bahrain Art 227 CC; Belarus Art 313(2) CC; Brazil Art 416 sentence 2 CC; Costa Rica Art 426 Com C; Egypt Art 225 CC; England Diestal v Stevenson [1906] 2 KB 345; Italy Art 1382 CC; Iraq Art 171 CC; Kuwait Art 304 CC; Libya Art 228 CC; New Zealand Burrows/Finn/Todd, op. cit. (n. 15), para 21.2.6(a); Paraguay Art 454(2) CC; Portugal Art 811(2) CC; Qatar Art 267; Syria Art 226 CC; USA Farnsworth, Contracts, p 304 et seq; Yemen Art 355 CC.

54See for Algeria Art 185 CC; Bahrain Art 227 CC; Costa Rica Art 427 Com C; Egypt Art 225 CC; France Stellmann, Die Vertragsstrafe in einem Europäischen Privatrecht, Berlin: Duncker & Humblot (2001), p 174 et seq with an overview of the
discussion; Iraq Art 171 CC; Kuwait Art 304 CC; Libya Art 228 CC; Qatar Art 267; Syria Art 226 CC; Yemen Art 355 CC.

55 See for China Art 114(2) Contract Law; Jordan Art 364(2) CC; Morocco Art 264 Code of Obligations and Contracts; the Netherlands Art 6.92(2) CC; United Arab Emirates Art 390(2) CC.

56 France Art 1152(2) sentence 1 CC; Argentina Alterini, Contratos Civiles – Comerciales – de Consumo – Teoría General, Buenos Aires: Abeldedo-Perrot (2005), p 602.

57 See for the USA Farnsworth, Contracts, p 301 et seq.

58 See for Austria § 1336(3) sentence 1 CC; Bulgaria Section 92 OCA; Estonia § 161(2) Law of Obligations Act; Georgia Art 419(2) CC; Germany § 340(2) sentence 2 CC; Lithuania Art 6.73(1) sentence 3 CC e contrario; Moldova Art 625(2) sentence 1 CC; Switzerland Art 161 CO; Schwener, Schweizerisches Obligationenrecht Allgemeiner Teil, 6th edn, Bern: Stämpfli (2012), para 71.12.


60 See for the USA See for the USA H & M Driver Leasing Service, Unlimited, Inc v Champion International Corporation, II Ct App, 17 March 1989, 536 NE2d 858 at 860: ‘Here, the contract expressly provided that the USD 10,000 ‘liquidated damages’ was recoverable in addition to ‘any and all actual damages’ resulting from breach. As such, that clause imposed a clear penalty which cannot be enforced.’ Hachem, op cit (n 7), p 163.

Referring Principles:

VI.4 - Promise to pay in case of non-performance