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NEW CHALLENGES IN INTERNATIONAL
DISTRIBUTION
Distribution contracts with Department Stores and
Sales through Internet

Which law should govern the contract of sale between suppliers and distributors?

Introductory remarks

The UN Convention on Contracts for the International Sale of Goods (CISG) is one of the most important international uniform law instruments, as evidenced both by number of Contracting States (77) and number of cases dealing worldwide with its uniform rules. The CISG has been the centre of a tremendous interest in legal writing and has drawn the attention of domestic and international legislators. Thus, the understanding of the main rules regarding the sphere of application of the CISG is of great importance for the parties in international commerce and for the courts all over the world.

The sphere of application of the CISG is defined by Articles 1 - 6. The CISG governs the contract of sale of goods (application *ratione materiae*) between the parties whose places of business are in different States (application *ratione personae*) when the states are Contracting States (direct application) or when the rules of private international law lead to the application of the law of a Contracting state (indirect application). These basic requirements for application of the CISG are defined by Article 1. On the other hand, Article 2 excludes certain types of sales from the scope of the CISG and Article 3 establishes additional requirements for the application of the CISG to contracts for goods to be manufactured and mixed contracts. Furthermore, the extent to which sales transactions are

¹ This presentation is a part of the article of J.Perovic, *Selected Critical Issues Regarding the Sphere of Application of the CISG*, published in Annals of the Faculty of Law in Belgrade, Belgrade Law Review, Journal of Legal and Social Sciences University of Belgrade, Year LIX.2011.No.3, p.181-196;

governed by the CISG is determined by Articles 4 and 5. Finally, Article 6 precises that the CISG applies subject to contrary agreement by the parties („opting-out“ approach).

This presentation will focus on the practical problems which usually arise with respect to the application of the CISG to a distribution agreement.

Contract of sale

For the application of the CISG, first of all, the requirements concerning contract of sale must be satisfied. The CISG does not expressly define the contract of sale. However, this definition can be established indirectly from the provisions regulating the obligations of the seller (Article 30) and of the buyer (Article 53). According to those provisions, the contract of sale is a contract in which the seller is obliged to deliver the goods, to hand over the documents relating to them and to transfer the property in the goods, and the buyer is obliged to pay the price for the goods and to take delivery of them as required by the contract. In that respect, it can be noted that the meaning of the contract of sale in the CISG does not differ from the relevant definitions of the national codes² and that the CISG governs most kinds of sales³ in international commerce.

Applicability of the CISG to international distribution contract

With regard to distribution contract, one has to distinguish between the framework distribution contract on the one side, and the individual contracts of sale concluded between the supplier and the distributor on the basis of the framework contract on the other side. The framework distribution contract which regulates the longterm relationship between the parties,

² This is a classic definition of sale. See B.AUDIT, *La vente internationale de marchandises – Convention des Nations-Unies du 11 avril 1980*, Paris, L.G.D.J, 1990, p.25; C.WITZ, *Les premières applications jurisprudentielles du droit uniforme de la vente internationale – Convention des Nations Unies du 11 avril 1980*, Paris, L.G.D.J, 1995, p.32; K.H. NEUMAYER, C. MING, *Convention de Vienne sur les contrats de vente internationale de marchandises Commentaire*, Lausanne, Cedidac, 1993, p.38. See also V.HEUZÉ, *La vente internationale de marchandises, Droit uniforme, Traité des contrats sous la direction de Jacques Ghestin*, Paris, L.G.D.J, 2000, p.75. For the comparison with the relevant definition of the Serbian Code of Obligations, J.PEROVIC, *Bitna povreda ugovora*, Belgrade, 2004.

³ See the view expressed by I. SCHWENZER, P.HACHEM, „Art.1 “ in P.SHCLECHTRIEM, I.SCHWENZER, Third Edition, Oxford University Press, 2010, p.32, according to which “*Not expressly mentioned but regularly encompassed by the Convention are furthermore sales under conditions including the retention of title or time limits as well as contracts providing for the direct delivery of the goods to the customer or the buyer. The same hold true for contracts containing pre-emptive options or rights to re-purchase, buy-back-sales, counter-purchases and offsets*”.

which is mainly related to the rights and obligations of the parties arising from the *distribution* relation, by prevailing opinion is not governed by the CISG.⁴ Contrary to that, the *individual sales contracts* which parties conclude each time when the goods suppose to be supplied to the distributor, may fall under the CISG, if the other requirements for application are met.⁵ Consequently, the international distribution contract is generally submitted to the different legal regimes.

For instance, in the case of the District Court's Gravenhage⁶, a Dutch company and a Swiss company concluded a framework agreement for the non exclusive distribution of certain products. The agreement contained no choice of law clause. On the same day, the parties concluded a sales contract of the same products. That contract was to be governed by Swiss law. The sales contract contained elements of distribution as for instance the clause on non-exclusivity. The buyer claimed that the seller did not fulfil its obligations deriving from the distribution agreement and therefore refused to make payment for the sale. The seller sued for payment. In counterclaim, the buyer asked for the setting aside of the distribution agreement. The court stated that the CISG does not apply to distributionship agreements. The framework contract could not be regarded as a sale because the most important elements of the sale contract were in fact laid down in the sale contract itself. The seller's claim was rejected under the applicable domestic law.

Similar was the ICC case where a German seller and a Spanish buyer concluded an agreement pursuant to which the buyer was to be the exclusive distributor in Spain of industrial equipment produced in Germany.⁷ Several individual sales contracts were then concluded between the parties. Four years later the German company informed the Spanish buyer that, due to the insufficiency of the buyer's sales, it would sell its products in Spain through another company. Thereafter, upon the buyer's refusal to pay for some of deliveries, the seller started arbitral proceedings. The buyer counterclaimed damages arising from breach of the exclusive distributionship agreement as well as from lack of conformity of certain products. The sole arbitrator held that the CISG was not applicable to the distribution

⁴ V.HEUZÉ, op.cit, p.75; C.WITZ, op. cit. p.32. See the view expressed in F.FERRARI, *La compraventa internacional Aplicabilidad y aplicaciones de la Convención de Vienna de 1980*, Valencia, 1999, p.129

⁵ P.SCHLECHTRIEM, „Art.1“ in P.SCHLECHTRIEM, I.SCHWENZER, *Commentary on the UN Convention on the International Sale of Goods (CISG)*, Second Edition, Oxford, Oxford University Press, 2005, p.27.

⁶ Decision of 02.07.1997, CISG-online.

⁷ 23.01.1997. 8611/HV/JK

agreement as such but to the individual sales contracts concluded pursuant to the distribution agreement.⁸

However, the problem could arise from the fact that the borderline between the framework distribution contract and the sales contracts may be uncertain if the framework contract already contains most of the typical obligations of a seller and a buyer (precisely formulated), so it is only up to the distributor to require delivery at a certain date, in a specified quantity, and just to confirm the seller's obligations which are already provided by the framework contract.⁹ It for this reason that some authors does not exclude possibility of application of the CISG rules relevant to the entire framework agreement, if such rules arise from the general rules of the law of obligations (i.e., if they are not specially adapted to the contract of sale).¹⁰ In that regard, Professor Schlechtriem noted that the parties can also choose to make the CISG applicable to all obligations created by the distribution contract, such as service obligation of the supplier to provide advertising and merchandising, to abstain from direct sales in the distributor's country or region, and the distributor's obligations to stock spare parts, to promote the goods and the seller's brand name, etc.¹¹

Application of the CISG to the framework distribution contract can be found in the case law.

For instance, in the case of the Italian *Corte di Cassazione* (14 December 1999),¹² a Italian company and a British company entered into an agreement providing for sale and the distribution of goods. The Italian company sued the British company claiming contract avoidance. The decision of the Italian Supreme Court relied on the assumption that the CISG is applicable not only to sales, but also to distribution agreements, provided that these can be construed as accessory clauses to a sale contract. Similar was the case of the Arbitral Tribunal Hamburg (21 June 1996).

⁸ The same views concerning this question were expressed in the decision of District Appeal Court of Amsterdam (16 July 1992) concerning exclusive distribution contract for the resale of shower cabinets, decision of the United States District Court in the case *Viva Vino Import Corporation v. Farnese Vini* (29 August 2000), decision of the Metropolitan Court of Budapest regarding the exclusive distribution of Swiss instruments in Hungary (19 March 1996), decision of the Appellate Court of Düsseldorf relating to an exclusive distribution of German engines for lawn mowers in Italy (11 July 1996), etc., CISG-online.

⁹ P .SCHLECHTRIEM, *ibidem*.

¹⁰ See for example F.VISHER, L.HUBER,D.OSER, *Internationales Vertragsrecht*, 2nd ed., Berne 2000, § 356.

¹¹ P .SCHLECHTRIEM, „*Art.1*“, *op.cit*, p.28.

¹² *Imperial Bathroom Company v. Sanitari Possi S.p.A.*, source: CISG-online 895.

The similar view was expressed in the case of the Arbitral Tribunal Hamburg where the seller, a Hong Kong company, and the buyer, a German company, had concluded a general agreement for the exclusive delivery and distribution of Chinese goods.¹³ Under this agreement, the seller was responsible for the business relations with Chinese producers while the buyer was responsible for the distribution of the goods in Europe. On this basis, the parties concluded separate sale contracts. Due to financial difficulties, a Chinese producer could not deliver the ordered goods to the seller, who consequently could not perform its contractual obligation to the buyer. The seller demanded payment of the sum due resulting from previously delivered goods. The buyer set off against the claim a damage claim for lost profit and refused to pay. The arbitral tribunal in this case applied the CISG as the relevant German law under article 1.1.b. CISG and upheld the seller's demand for payment.¹⁴

Conclusion

In the light of the mentioned problems, one can note that the CISG is applicable to the individual sales contracts concluded between the supplier and the distributor on the basis of the framework distribution contract if the general conditions for the application of the CISG are met. On the other hand, regarding the applicability of the CISG to the *framework* distribution contract, certain reserve can be expressed. The CISG is created for the needs of international sale. It means that: a. it does not contain the rules adequate for the rights and obligations of the parties arising strictly from the distributionship (e.g. the distributor's obligation to promote the goods and the seller's brand name or the obligation of the supplier to provide advertising and merchandising); b. regarding the rights and obligations of the supplier and distributor arising from sale, the CISG rules could be inadequate in particular case since they do not take into consideration the specific characteristics of the distribution relation, like for instance the *intuitu personae* nature and the economic objectives to be achieved. On the other hand, the CISG rules which are of "more general nature" like the one related to interpretation of the contract usages, formation of the contract, etc. could perfectly fit the distribution contract. In sum, one may conclude that problems of applicability of the

¹³ 21.06.1996, CISG-online

¹⁴ The same view as about the applicability of the CISG to distribution agreement was expressed in the decision of the US District Court (17 May 1999) in case *Medical Marketing International v. Internazionale Medico Scientifica*, note P. SCHLECHTRIEM, ibidem, as well as in the decision of the OLG Koblenz (17 September 1993), CISG-online 2 U 1230/91.

CISG to the international distribution contract are to be solved on the basis of the facts of each particular transaction and not under a general rule specifying *a priori* whether it is possible to apply the CISG or not. In case the dispute arises from the rights and obligations of *sale*, the judge/arbitrator may apply CISG, taking into consideration all relevant circumstances of the case. Contrary to that, if the dispute is related strictly to the *distributionship*, the application of the CISG could be inappropriate. Thus, in order to avoid uncertain situations, the parties should, by choice of law clause, precisely solve the question of applicable law to the framework contract as well as to the individual sale contracts.