

# Application of the CISG to International Government Procurement of Goods

Cesar Pereira\*

**Keywords:** CISG; international sale of goods; public procurement; international government purchases

## **Abstract:**

*Harmonization is one of the most sought goals in international transactions and one of the main purposes of international treaties and agreements dealing with international commerce. Alongside the Government Procurement Agreement under the World Trade Organization (GPA/WTO), the United Nations Convention on Contracts for the International Sale of Goods of 1980 (CISG) can offer benefits to government procuring agencies in their international purchases. Conversely, some of its characteristics require the attention of state parties. International government purchases and sales are under the scope of the CISG, and procuring agencies must beware of the CISG's potential benefits and special requirements. In international government purchases or sales in which the provisions of the CISG are not excluded or derogated, the parties will be subject to the effects of the CISG. This paper is based on existing case law, current practice of certain national governments and international agencies, and on a joint interpretation of the CISG and international public procurement model. It aims to discuss the interaction between the CISG and public procurement regulations. Additionally, it delves into the potential gains for government procuring entities in adopting the uniform contract regulation of the CISG to govern their international transaction with goods. Finally, it examines potential difficulties in public procurement proceedings when the CISG is combined with domestic public procurement legislation.*

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\* Cesar Pereira is a Brazilian attorney, partner at Justen, Pereira, Oliveira & Talamini (São Paulo). He holds an LLM (1998) and a JSD (2005) in Public Law from Pontifícia Universidade Católica (PUC-SP), and he was a visiting scholar at Columbia University Law School in 2013-2014. He has published and edited numerous books, articles and book chapters on subjects related to infrastructure, public law, and arbitration. He is a Fellow of the Chartered Institute of Arbitrators (FCI Arb) and serves as an arbitrator in matters involving PPPs and commercial law. He is the president of the Arbitration Center of the Federation of Industries of the State of Paraná (CAMFIEP) and vice-president of Brazil Infrastructure Institute, an industry think tank. Postal address: Rua Joaquim Floriano, 413, cj 111 – São Paulo, SP – 04.534-011. Brazil. Email: cesar@justen.com.br, cesar.pereira@camfiep.org.br or cesar.pereira@brazilinfra.com. The author thanks Ana Julia Aragão for her research work and Karina Carvalho, Cassiano Zimmermann (CAMFIEP), Jacqueline Henry-Lucio and Luísa Quintão for their assistance in the revision of this paper.

## 1. Introduction<sup>1</sup>

The United Nations Convention on the International Sale of Goods (CISG) originates from efforts of UNCITRAL – United Nations Commission for the International Trade Law. This UN commission is generally charged with recording information and disseminating knowledge regarding the CISG.

It is interesting to realize that the same commission develops an entirely separate body of rules and recommendations concerning government procurement. This takes the form of a model law, not a convention for a uniform law such as the CISG. The obvious difference is that, while the CISG becomes national uniform law when it is signed and ratified, the UNCITRAL Model Law on Public Procurement is only a reference for national legislators. Nonetheless, such model law is widely acknowledged as an important tool in shaping many countries' regulation of government purchases.<sup>2</sup>

Some states have gone beyond the mere adoption of the model law as guidance and have joined the Government Procurement Agreement (GPA) under the World Trade Organization (WTO) framework. This is an international convention that creates harmonized rules based on common principles of fairness and probity. It also ensures national treatment to foreign bidders from contracting states. The original GPA was revised in 2011 and the revision entered into force in April 2014. Prior to its future accession, each prospective new member will be required to negotiate with all the others to define coverage and legislative harmonization.

Many governments also rely on funding from international financial agencies such as the IRDB – International Reconstruction and Development Bank (World Bank) or any of the other various similar institutions. While they make funding available, such institutions also ensure that the expenditure of such funds by the recipient government does not discriminate against nationals of other member states. This is achieved through the mandatory application in many cases of certain guidelines issued by the financial agencies themselves.

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<sup>1</sup> An earlier version of this article was published in I. Schwenzer. *35 Years CISG and Beyond* (The Hague: Eleven, 2015), which is the conference book for the Basel international conference held in January 2015 where this paper was first given. The current version is being published with the authorization of the book editor.

<sup>2</sup> For several aspects of international public procurement, including the UNCITRAL Model Law and the GPA/WTO, see S. Arrowsmith, J. Linarelli Jr., D. Wallace, *Regulating Public Procurement. National and International Perspectives* (Kluwer Law International, 2000). Arrowsmith, M. Troybus (Eds.), *Public Procurement. The Continuing Revolution*, (Kluwer Law International, 2003). P. Trepte. *Regulating Procurement*. (Oxford University Press, 2004).

International government procurement has therefore been the subject of attention by governments, international organizations, and potential suppliers in a variety of forms and angles. The most attention is directed to the harmonization of rules and the avoidance of nationality-based discrimination. The purposes are to ensure access to a global marketplace and give international suppliers a minimum level of foreseeability in the applicable rules.

The CISG has similar purposes from a contractual standpoint. It aims to provide legal uniformity as an instrument to facilitate and foster international commercial transactions. It is somewhat surprising that such international instruments or institutions do not explicitly adopt more often (or rather hardly ever adopt) the CISG as a tool for international harmonization.<sup>3</sup> Some of the reasons for this omission are discussed below.

This paper aims at examining certain effects of the CISG on government contracts. It also intends to shed light on the potential benefits of the CISG and to discuss the rights of individual suppliers when the CISG is affirmatively adopted or not effectively excluded or derogated in international government purchases.

## **2. Sphere of Application**

Articles 1-3 CISG generally define the Convention's sphere of application. Article 1(1) provides that "[t]his Convention applies to contracts of sale between parties whose places of business are in different States" when both states are CISG contracting states or when the conflict of law rules lead to the application of the laws of a contracting state. International treaty law determines whether a certain country is a contracting state under the CISG. In accordance with Article 99(2) CISG, the Convention enters into force with regard to any state "on the first day of the month following the expiration of twelve months after the date of the deposit of its instrument of ratification, acceptance, approval or accession". Therefore, all of the discussion in this paper relates to the possible application of the CISG only when a given contract falls under the sphere of application arising from Article 1-3 CISG. If, for instance, one of the countries involved in the relevant contract is not a CISG contracting state and the CISG is not applicable

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<sup>3</sup> See UNCITRAL, Guide to Enactment of the UNCITRAL Model Law on Public Procurement, available at <http://www.uncitral.org/pdf/english/texts/procurem/ml-procurement-2011/Guide-Enactment-Model-Law-Public-Procurement-e.pdf>, p. 61/62, access June 20, 2015. The commentary to art.3 of the Model Law does not yet address the CISG as a possible international commitment with impact on public procurement.

under its Article 1 (b), either because the applicable law is that of the non-contracting state or the other country is also not a contracting state, domestic law or other international instruments will apply, and the discussion in this paper will be irrelevant.

Article 1(3) complements the provisions regarding the sphere of application and commands that “[...] nor the civil or commercial character of the parties or of the contract is to be taken into consideration in determining the application of this Convention”. The exclusions in art.2 and the clarifications in art.3 further define the scope of application of the CISG.

The provision concerning the irrelevance of the civil or commercial character of the parties or the contract is especially interpreted to mean that the CISG governs any international sales – or, conversely, purchases – of goods, regardless of the nature of the parties or the contract. Government entities are active in international sales, mostly as buyers but potentially also as sellers.<sup>4</sup> Therefore, the CISG sphere of application comprises contracts entered into by national governments at central or sub-central levels. It also comprises contracts subject to private or public law in states that acknowledge such distinction.

### **3. Sphere of Application in Government Purchases**

The international interpretation of the CISG assumes generally that the CISG is fully applicable to contracts to which states are parties. This encompasses government departments or agencies, such as those responsible for defense purchases, and any type of government-owned or government-controlled corporations found in many jurisdictions. The state entity can be a purchaser or a seller; oil and gas contracts can easily involve government entities as sellers, for instance.

Some of the main international commentators of the CISG have examined this topic and are in favor of the potential application of the Convention to government contracts.<sup>5</sup>

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<sup>4</sup> In many countries, government entities may be involved in the international supply of goods, especially commodities such as metals or oil and gas. The commercial or administrative nature of such transactions is a matter governed by domestic law. However, they all fall under the general scope of application of the CISG.

<sup>5</sup> P. Schlechtriem, “Unification of the Law for the International Sale of Goods” in *German National Reports (Private Law and Civil Procedure) XIIth International Congress of Comparative Law* (Baden-Baden: Nomos, 1987), pp. 126-127, available at [www.cisg.law.pace.edu/cisg/text/e-text-11.html#N\\_2](http://www.cisg.law.pace.edu/cisg/text/e-text-11.html#N_2). Schwenger, “Introduction”, in: Schwenger. *Commentary on the UN Convention on the International Sale of Goods (CISG)*, 3<sup>rd</sup> edn. (Oxford University Press, 2010), p. 8 (“Classifying a public body’s procurement contracts as ‘matters subject to public law’ could curtail or exclude the application of the CISG or its individual rules almost at will”). J. Honnold, H. M. Flechtner, *Uniform Law for International Sales under the 1980 United Nations Convention*, 4<sup>th</sup> edn. (Wolters Kluwer, 2009), pp. 180-183.

U. Schroeter advances a persuasive explanation about the context of international purchases in which a supplier is selected through a tender process:

“The CISG furthermore also applies to international sales contracts concluded with a seller which has been selected by way of a call for tender (invitation to tender, call for bids). This form of contract initiation is frequently employed for purchases by private companies, but occurs particularly often in cases in which the buyer is either a government authority (public procurement) or a private company acting in order to fulfill a contract with a government. Domestic laws which govern call for tender often impose certain rules designed to guarantee the fair selection of the successful tenderer (e.g. principle of non-discrimination, preference for the tender which offers the lowest price or is the ‘economically most advantageous’). Within the EU, such rules are often based on EU Procurement Directives, which in particular seek to protect foreign tenders (sellers).

Since domestic laws in this field primarily aim at regulating the phase leading up to the selection of the successful tenderer, the contract can subsequently be concluded in accordance with Articles 14-24 without resulting in any conflict between the two sets of rules. The tenders accordingly constitute offers under Article 14(1), among which the successful tender is accepted by way of the award decision which at the same time constitutes the acceptance under Article 18(1). Domestic provisions declaring null and void such contracts which have been concluded in violation of public procurement information duties or time periods can be applied to CISG contracts by virtue of Article 4, sentence 2(a). If, on the contrary, the domestic law on (public or private) calls for tender provides for remedies which are incompatible with the Convention’s rules – as e.g. claims for damages for failure to enter into a contract in situations in which the offer was freely revocable under the CISG – such remedies are pre-empted by the Convention.<sup>6</sup>”

These remarks explain in part why one cannot find internationally a large number of cases applying or discussing the CISG in matters involving government entities.<sup>7</sup> In

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<sup>6</sup> U. Schroeter, “Introduction to Arts. 14-24” in Schwenzer, *Commentary* (2010), pp. 244-245.

<sup>7</sup> Regarding this topic under Brazilian law, see M. Kurcgant. “Os contratos administrativos e a Convenção de Viena sobre venda e compra internacional de mercadorias” in *Fórum de Contratação e Gestão Pública*, (Belo Horizonte, 2014) ano 13, n. 152, pp. 54-64 and Pereira. “Aplicação da CISG a licitações e

many national laws, unlike in most Latin American countries<sup>8</sup> and in the United States, the specific regulation of government procurement focuses only on the selection of the contractor, not on the formation of the contract or the subsequent contract administration (rights and obligations of the parties). This restriction is also true in multinational systems such as the EU Directives, the UNCITRAL Model Law and the GPA/WTO. In addition, larger or more complex purchases are often made through local vendors or with suppliers with places of business in the country of the purchasing government. In Brazil, to use this country as an example, in order to supply goods under a contract that requires substantial activities in Brazil – such as assembly, commissioning and post-sale support – a foreign company must be previously “authorized to operate in Brazil” (art.1134 of the Brazilian Civil Code). This may eliminate the international character of the sale and make the CISG inapplicable unless (a) the vendor is able to obtain such authorization regardless of not having a local basis (place of business) in Brazil or (b) the seller’s relevant place of business, as defined by art.10(a) CISG, is outside Brazil.

The acknowledgment that government contracts are in the sphere of application of the CISG is just a starting point for understanding the problems regarding international government purchases. The CISG is primarily a body of dispositive rules, which can be excluded or derogated by the will of the parties and applied only in the absence of contrary agreement, with only a few exceptions. Nonetheless, this acknowledgment is an essential element to ensure clarity regarding the rules governing such transactions, especially in view of the CISG rules of which the parties cannot voluntarily contract out of or around.

There are significantly fewer reported court and arbitral decisions dealing with government contracts and the CISG than the economic significance of such marketplaces would suggest. International experts estimate a country’s government procurement market at around 10-15% of the country’s GNP (Gross National Product).

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contratos administrativos de compra internacional de mercadorias”, in Schwenger, Pereira and Tripodi (Eds.). *A CISG e o Brasil* (Marcial Pons, 2015), pp. 161-176.

<sup>8</sup> For Brazil as a reference for similar regulations in Latin America, see M. Justen Filho and Pereira. (Eds), *Infrastructure Law of Brazil*, 3<sup>rd</sup> ed., (Belo Horizonte: Forum, 2012). For the US government procurement regulation concerning contract formation and administration, see J. Cibinic, Jr. R.C. Nash, Jr. Nagle, J.F. *Administration of Government Contracts*, 4<sup>th</sup> edn. (Wolters Kluwer, 2006); Cibinic, Jr., Nash and C.R. Jr. Yukins. *Formation of Government Contracts*, 4<sup>th</sup> edn., (Wolters Kluwer, 2011); S.W. Feldman, *Government Contract Guidebook*, 4<sup>th</sup> edn., (Thomson Reuters Westlaw, 2013); and W.N. Keyes, *Government Contracts under the Federal Acquisition Regulation*, 3<sup>rd</sup> ed., (Thomson West, 2003), with 2014/2015 supplement issued in October 2014.

Many of the world's largest economies take part in the GPA/WTO, which among other things ensures access to a substantial portion of each country's government procurement marketplace. In addition, in many large economies such as China and certain countries in Latin America and the Middle East a significant part of the economy's transactions involves government-controlled companies subject to government procurement regulations. There is a constant interplay between government procurement rules and the law governing international transactions, namely the CISG.

The existing international case law often upholds the premise that government contracts are generally within the CISG's sphere of application. An outstanding precedent is the US case, *Hilaturas*, which was resolved in 2008.<sup>9</sup> It dealt with the supply of goods to the Iraqi government by a Spanish supplier under the Oil for Food program. The case was ruled in favor of the Iraqi government with grounds on the CISG. Another similar case is *ETECSA* (Empresas de Telecomunicaciones de Cuba S.A.), involving the purchase by a Cuban mixed-capital company – controlled and partly owned by the government – of cell phones supplied by a South-African vendor. The case was heard by Sala de lo Económico del Tribunal Supremo Popular in Havana, Cuba, on 16 June 2008.<sup>10</sup> A third case discussing the CISG involving government entities is *Agropodderzhka Trade House LLC v. Sozh State Farm Complex*, heard by the Economic Court of the Gomel Region of Belarus on 6 March 2003.<sup>11</sup>

Other cases often mentioned by scholars illustrate ordinary situations involving international government transactions and their relation with the CISG. In the Russian submarine case, the Russian government sold a decommissioned submarine to a foreign party as scrap material. The decision applied the exclusion of art.2(e) CISG to conclude that the sale of a ship or vessel was not covered by the CISG, and that the good at issue was still a ship even if considered inactive by the seller.<sup>12</sup> In a case in which the state of Slovenia purchased weapons from an Austrian supplier, a private local Slovenian company intermediated the transaction, but the negotiations were conducted by the then

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<sup>9</sup> *Hilaturas Miel, S.L. v. Republic of Iraq*, 573 F. Supp. 2d 781 (S.D.N.Y. 2008), CISG Online 1777. CISG Online is available on [www.globalsaleslaw/index.cfm?pageID=28](http://www.globalsaleslaw/index.cfm?pageID=28). The case is also reported by U. Schroeter, *supra*, p. 244, n. 192.

<sup>10</sup> Available at <http://www.cisgspanish.com/seccion/jurisprudencia/cuba/>, last access on 21 June 2014.

<sup>11</sup> CLOUT (Case Law on UNCITRAL Texts) case 496.

<sup>12</sup> Russia 18 December 1998 Maritime Commission Arbitration proceeding 1/1998, available at <http://cisgw3.law.pace.edu/cases/981218r1.html>, last access on 21 June 2014.

recently formed government (in 1993).<sup>13</sup> The *Diversitel* case dealt with a subcontract for the purpose of finally supplying certain pieces of equipment to the Canada Department of Defense. The delay in performance by a vendor located in California was considered a fundamental breach because it prevented the Canadian buyer Diversitel from timely performing its supply contract with the Canadian government.<sup>14</sup>

Lastly, many governments and procuring agencies already acknowledge the application and relevance of the CISG with regard to government purchases. In a classic work on the US Federal Acquisitions Regulation (FAR), W.N. Keyes discusses the CISG as part of the rules applicable to international purchases (“international acquisitions” in the book’s terminology).<sup>15</sup> In 2005, G. Bell reported that the Singapore government had started to define the CISG as applicable law in its international contracts.<sup>16</sup> In an unpublished paper dated 2013, D. Hanson mentions the New Zealand practice, which takes into consideration the manual prepared for the New Zealand government as guidance for foreign bidders. This material expressly mentions the CISG as part of the system of rules governing such purchases,<sup>17</sup> and the New Zealand government includes this reference in its explanation of rules relating to international tender procedures.<sup>18</sup> In their March 2013 revision, the World Bank standard tender rules for the purchase of goods recommended the adoption, as applicable law, of the purchasing country’s law, without making reference to any exclusion of the CISG.<sup>19</sup> Therefore, if the purchasing country is a CISG contracting state or if the applicable

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<sup>13</sup> Austria 24 February 1999 Appellate Court Graz (*Military weapons case*), available at <http://cisgw3.law.pace.edu/cases/990224a3.html>, access on 21 June 2014.

<sup>14</sup> Ontario Supreme Court of Justice, *Diversitel Communications Inc. v. Glacier Bay Inc.*, available at <http://www.unilex.info/case.cfm?id=1189>, last access on 21 June 2014. This case is reported by U. Schroeter, *supra*, p. 244, n. 193.

<sup>15</sup> Keyes, *Government Contracts under the Federal Acquisition Regulation* (2003), pp. 566-569.

<sup>16</sup> G. Bell, *Why Singapore should withdraw its reservation to the United Nations Convention on Contracts for the International Sale of Goods (CISG)*. (2005) 9 SYBIL 55–73. Nota 36 (“A happy exception is now found in the standard procurement contract terms of the Government of Singapore which, in most cases, no longer excludes the CISG. The standard choice of law clause now reads: “This Contract shall be deemed to be made in Singapore and shall be subject to, governed by and interpreted in accordance with the Laws of the Republic of Singapore for every purpose”. See *Contract and Purchasing Procedures*, issued by the Government of Singapore, available online at [http://www.gebiz.gov.sg/scripts/doc/contract\\_purchasing.pdf](http://www.gebiz.gov.sg/scripts/doc/contract_purchasing.pdf)”).

<sup>17</sup> Available at <http://www.business.govt.nz/procurement/for-agencies/key-guidance-for-agencies/principles-rules-and-the-law>, last access on 21 June 2014.

<sup>18</sup> Available at <http://www.business.govt.nz/procurement/pdf-library/agencies/rules-of-sourcing/government-rules-of-sourcing-April-2013.pdf>, last access on 21 June 2014. It should be acknowledged that in spite of such clear reference to the CISG, I was unable to find any instance from New Zealand in which the CISG has been used to resolve disputes regarding government purchases.

<sup>19</sup> Available at <http://siteresources.worldbank.org/EXTEOS/Resources/575134-1316086157992/8148378-1358160892181/9006015-1361557869334/Goods-EN-02April13-v1.pdf>, last access on 21 June 2014.



private international law leads to the application of the law of a contracting state (CISG, Article 1(a) and 1(b), respectively), the World Bank rules will lead to the application of the CISG unless the parties have agreed otherwise under Article 6 CISG.

This brief review of scholarly writings and case law leads to the conclusion that international purchases made by government entities are comprised in the CISG abstract sphere of application. This conclusion is a starting point for a detailed discussion of the many problems arising from the interplay between the CISG and the domestic and international regulation of government procurement.

The CISG is generally applicable to international sales regardless of whether government entities are involved. A *lex specialis* argument to favor domestic government procurement law over the CISG is not persuasive. If the government procurement law may be considered special because it deals with *public* sales whether domestic or international, the CISG is equally special because it deals with *international* sales whether public or private. The CISG prevails with regard to international sales because it is chronologically more recent and mainly because it is the outcome of an international treaty. The full application of the CISG, excluded or derogated only in accordance with its own art.6, corresponds to a commitment made by each contracting state toward each and all the others.

Government contracts are also not excluded by art.2 CISG. Article 2(b) CISG excludes sales made through “auctions”. In many countries, such as in Brazil, reverse auctions or procurement auctions are one of the most commonly used procurement methods. In addition, government agencies often sell goods in auctions that are no longer in use or that have been apprehended in criminal actions. One could object to the applicability of the CISG by assuming that no sale or purchase made through an auction of any kind would be covered by the Convention. However, this argument has been examined and rejected by commentators given the limited purpose of the art.2(b) CISG exclusion.<sup>20</sup> The same goes for framework agreements or IQID (indefinite quantity, indefinite delivery) contracts: they are covered by the CISG when governments are involved in the same way and with the same restrictions as when the parties are private.

Finally, the art.2(a) CISG exclusion does not extend to international purchases made by governments. Although a government entity will not ordinarily purchase the goods

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<sup>20</sup> Schwenzer and P. Hachem comment Art. 2(b) CISG and explain that “[...] a contract ‘awarded’ to the highest bidder in a public (international) procurement bid can very well be governed by the CISG”, in Schwenzer. *Commentary* (2010), p. 56.

for resale or as inputs for industrial activities, it does not generally meet the requirements for treatment as a consumer (purchaser for personal, family or household use) under the CISG.<sup>21</sup> In addition, the exclusion of art.2(a) CISG is not dependent on the concept of consumer transactions given by each country's own domestic consumer law.<sup>22</sup> Even if a government entity can be protected as a consumer under its own law and for certain specific purposes,<sup>23</sup> it does not follow that its international purchases or sales will be excluded as consumer transactions under art.2(a) CISG.<sup>24</sup>

#### **4. Application of the CISG to govern its own exclusion or derogation**

Government contracts for the international purchase or sale of goods are within the CISG's sphere of application. In strict legal terms, the main and most immediate consequence of this conclusion is that the CISG's secondary rules<sup>25</sup> (rules of structure or competence -- the ones dealing with interpretation of contracts and construction of the parties' conduct) will always apply. These are the CISG rules that govern the Convention's own exclusion or derogation.

In most situations, the CISG allows the parties to agree on the exclusion or derogation of its provisions. Therefore, the CISG will only govern a certain transaction between a seller and a buyer if the parties have not effectively excluded its application. The CISG is the legal source of the validity and effectiveness of the parties' actions that exclude or derogate the CISG's own provisions. Such actions are interpreted within the framework of the CISG, including the principle of uniform international application (art.7 CISG). This guideline will require attention to international commentary and case law from the parties and the domestic decision-maker. Otherwise, domestic views

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<sup>21</sup> See Schwenger and Hachem in Schwenger. *Commentary* (2010) pp. 49-55.

<sup>22</sup> For the relationship between the CISG and domestic consumer law, see A. C. Beneti. "A Convenção de Viena sobre Compra e Venda Internacional de Mercadorias (CISG) e a questão do Direito do Consumidor" in Schwenger, Pereira and Tripodi (Eds.), *A CISG e o Brasil* (2015), pp. 93-107.

<sup>23</sup> Justen Filho shows that government contracts are not covered by consumer protection law, only by government procurement law and the provisions of the solicitation and the contract. Consumer law could only apply in exceptional circumstances of a purchase of goods or services directly in the marketplace (*Comentários à Lei de Licitações e Contratos Administrativos*, 16<sup>th</sup> ed. (RT Thomson Reuters, 2014), p. 1081). The Brazilian Superior Court of Justice ruled in 2010 that consumer law is not generally applicable to government contracts. It will only apply in exceptional circumstances when the government entity is the weaker party in the contract due to specific circumstances of the contract at hand (STJ, 2a. T, RMS 31.073, Rel. Min. Eliana Calmon, j. 26.8.2010).

<sup>24</sup> For the CISG prevalence over domestic consumer protection law, see Schwenger and Hachem in Schwenger. *Commentary* (2010), p. 55.

<sup>25</sup> The reference is to H.L.A. Hart's classification of rules in its *Concept of Law*: primary rules govern conduct; secondary rules govern the enactment, modification, interpretation, application and enforcement of primary rules.

concerning the power to exclude or derogate may undermine the application of uniform law and the CISG's international character. This concern is especially true in jurisdictions where government entities are considered to have certain *extraordinary prerogatives* in government contracts, in affiliation with the French notion of administrative contract (*marché public* and *contrat administratif*). The introduction of the CISG in a certain national context creates normative restrictions to the exercise of government prerogatives. The structural provisions contained in Arts. 6-9 will generally govern the extent to which the parties – typically a government entity and a private supplier – will have excluded or derogated from the CISG.

The main structural provisions (secondary rules) of the CISG are those dealing with exclusion or derogation (art.6), interpretation and related principles such as uniformity and internationality (art.7), broad admissibility of evidence and guidelines for the qualification of a party's conduct (art.8) and uses and practices as source of duties (art.9). Even if the government entity deliberately opts to exclude or derogate certain provisions of the CISG, as allowed by art.6 CISG, this option will be recognized, construed and given legal significance in accordance with the CISG provisions. As I. SCHWENZER and P. HACHEM put it, "The formation and interpretation of the exclusion of the CISG is subject to the rules of the Convention, as the CISG determines its sphere of application autonomously".<sup>26</sup> In a later work, P. HACHEM further explains this issue as follows:

"Where the CISG is objectively applicable, its rules on the formation of contracts must also govern the question of whether an agreement on the exclusion of the Convention has been formed. This notion appears to be undisputed. However, the exclusion of the CISG is typically part of a choice of law clause which at the same time designates the law the parties intend to apply instead of the Convention. The prevalent rule in private international law is that it is the law designated by the parties which governs the formation of the positive choice of law, that is the choice of the law that is intended to apply to the contract. It seems to me that while clearly it is the role of the CISG to decide whether the parties managed to opt out of it, it is just as clearly not the

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<sup>26</sup> Schwenzer and Hachem in Schwenzer. *Commentary* (2010), p. 104.

role of the CISG to decide whether the parties also successfully opted into the chosen law”.<sup>27</sup>

## **5. Relationship between the CISG and domestic government procurement law**

Governments in general usually adopt in their government contracts a reference to their domestic public procurement laws and regulations. They also tend to use detailed contracts to describe in great detail the rights and obligations of each party. Article 6 CISG governs the relationship between such choices and the CISG general provisions. The reference to domestic law and detailed contractual provisions amount to an exclusion or derogation as the case may be. We will return to this topic later in this paper.

International commentary points out that the two main points of contact between the CISG and any domestic government procurement law are the issues of validity (art.4 CISG) and freedom of form (art.11, 12 and 13 CISG). Validity is generally excluded from the scope of the CISG, and it is closely related to issues of agency – or, in administrative law terminology, competence and mandate of the procuring agency or official. Freedom of form could, in theory, lead to oral agreements between a government agency and its suppliers.

Article 4 excludes validity from the CISG’s sphere of application. Therefore, the selection method for determining the contractor or supplier is normally considered to be outside the scope of the CISG. In countries where domestic procurement law does not govern the content of the contract, only the selection of the contractor, the application of the CISG to international government purchases should be commonplace.

The same reasoning explains the situation of agent-principal relationship – or competence of the procuring agency and respective officials. Domestic administrative law will define who is the competent official to act on behalf of the government. This definition is outside the CISG and has no bearing in the application of the CISG. This is why commentators strongly stress that the identification of true agency or competence

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<sup>27</sup> Hachem. “Applicability of the CISG – Articles 1 and 6” in Schwenger, Y. Atamer and P. Butler, *Current Issues in the CISG and Arbitration* (Eleven, 2014), p. 37. Hachem concludes that “one may interpret an exclusion of the CISG to have been made under the caveat that the choice of law option must, at the same time, be successful”, p. 38. In systems such as Brazilian conflict of laws rules, according to which parties are arguably not allowed to freely choose the applicable law (except in arbitration, as per Law 9.307, of 1996), the chosen law may be incorporated into the contract as a contractual derogation of the CISG under art.6 CISG, not as the applicable law resulting from the exclusion of the CISG.

issues must be strict. An undue confusion between issues of *competence* and *form* can lead to an improper expansion of the field that is excluded from the CISG's sphere of application.

On the other hand, the *freedom of form* enshrined in art.11 is generally seen as a point of potential conflict with domestic government procurement regulation. Domestic procurement laws generally require government contracts to be done in writing.

J. HONNOLD points out scholars adopt one of two possible interpretations about the interplay between art.4 and 11 CISG with regard to government contracts required to be done in writing by domestic law.<sup>28</sup>

One line of thinking considers that the freedom of form (art.11 CISG) is overridden by the domestic law requirement since this is an issue of validity, and Art. 4 CISG excludes validity from the sphere of application of the CISG. However, this will take place only if the written form requirements under domestic law are justifiable and not merely a formality.

The other view considers that art.11 CISG is an exception admitted by art.4 CISG. This latter provision defines that “[...] *except as otherwise expressly provided in this Convention, [the CISG] is not concerned with: (a) the validity [...]*”. By providing that “[a] *contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirement as to form*”, art.11 CISG is an exception to art.4 CISG. Therefore, it provides for freedom of form even when domestic law requires written form for government contracts. In this view, the domestic form requirement is superseded by the CISG freedom of form. It is not a matter of validity under art.4 because art.11 is an exception to art.4 and places this issue under the coverage of the CISG.

## **6. Domestic government procurement law as derogation of the CISG (Art. 6)**

In general, a government contract will be done in writing and contain reference to the applicable domestic law. It will also contain as contractual clauses many or most of the applicable legal provisions regarding each party's obligations and the consequences of their breach.

Such references and clauses should be construed as contractual exclusions or derogations of the CISG in accordance with art.6 CISG.

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<sup>28</sup> Honnold and Flechtner, *Uniform Law under the 1980 Convention* (2009), p. 181-183.

It follows that the criteria laid out by the CISG for the interpretation of the exclusion or derogation will apply to determine the effectiveness and the extent of the derogation of the CISG by the domestic government procurement law or by the contractual provisions. International scholarship and case law set forth requirements for such interpretation, such as (i) the need of clear intent to exclude or derogate, so that the CISG will remain applicable in the absence of an unambiguous choice to avoid such application<sup>29</sup> and (ii) the application of the CISG rules on the formation and interpretation of contracts for the construction of the agreement to exclude or derogate, including art.8 and 9 CISG. As pointed out below in this paper, the standards of proof for the exclusion of the CISG in unilaterally drafted government contracts may be higher due to the constitutional protection of the counterparty's trust and legitimate expectations or, when such protection is not available, due to the *contra proferentem* doctrine.

The incorporation of government procurement law into the contract may cause the contract to be governed by the CISG with most of its substantive provisions derogated by domestic public procurement law. This solution may be undesirable but is acceptable under art.6 CISG. There is only a difference in degree between the derogation of only one provision of the CISG and the derogation of most of its provisions. If the incorporation by reference of the contrary conditions of the domestic public procurement law renders inapplicable all but one provision of the CISG (e.g. art.11 about freedom of form), this will still be important and useful for the party invoking the CISG for its protection.

One point that is particularly relevant is again the freedom of form under art.11 CISG. Even if the original contract is generally done in writing, as this is the international practice in government contracts, there can arguably be *amendments* made with freedom of form. If the parties have not either expressly or by incorporation excluded oral amendments, these will be valid in accordance with art.11 CISG.

In the US government procurement practice, scholars and case law adopt the idea of *constructive changes* as opposed to *formal changes* to the contract. The former are

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<sup>29</sup> For the need for a clear and unambiguous exclusion, see *Forestal Guarani, SA v Daros International, Inc.* (CISG-online 1779), *Easom Automation Systems, Inc v Thyssenkrupp Fabco, Corp* (CISG- online 1601), *Cedar Petrochemicals, Inc v Dongbu Hannong Chemichal Co, Ltd* (CISG-online 1509), *Property Casualty Company of America et al v Saint-Gobain Technical Fabrics Canada Limited* (CISG-online 1435), *TeeVee Toons, Inc et al v Gerhard Schubert GmbH* (CISG-online 1272) and *Ajax Tool Works, Inc v Can-Eng Manufacturing Ltd* (CISG-online 772).

inferred from conduct rather than from formal agreements.<sup>30</sup> Equivalent concepts exist in other jurisdictions. It is generally common for contractors in disputes with procuring agencies to use letters exchanged between the parties or other actions attributable to the government entity as grounds to establish *constructive changes*. Article 11 CISG will apply in such situations to give the nature of a binding agreement to such actions intended to modify the original contract even if they do not take the form of written agreements.

## **7. Possible violation of the bidders' right to equal treatment**

In accordance with art.1 CISG, the Convention will only apply to contracts between parties with places of business in different states. Internationality is one of the requirements for the CISG to apply. In a certain tender process initiated by a national procuring agency of a contracting state, and assuming that the conflict of laws rules lead to the application of such state's law (art.1(1)(b) CISG), the CISG will apply if the contract is awarded to an international supplier. However, there may be international and domestic bidders. This will lead to a situation in which each bidder may be subject to a different set of substantive rules depending on whether it is domestic or international.

A principle that is internationally accepted in government procurement is the equal treatment of the bidders. All national systems that follow international standards avoid discriminatory provisions that submit bidders to different treatments without reasonable justifications. Many countries adopt benefits for small and medium enterprises (SME), create preferences for locally made goods or services ("buy national") or use public procurement as a public policy tool (green procurement, for instance). However, these benefits must follow certain requirements and above all must not merely result from arbitrary discrimination against certain bidders, products, or services.

A question that must be addressed is whether equal treatment is violated when a procuring agency tenders out a contract that may be subject to the CISG or to domestic law depending on who the winning bidder is. Putting it in another way, is the government entity required to have tenders only with international suppliers (subject to the CISG) or only with domestic suppliers to avoid this possible breach to equal treatment?

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<sup>30</sup> See S.W. Feldman, *Government Contract Guidebook*, 4<sup>th</sup> edn. (Thomson Reuters Westlaw, 2013), especially pp. 532-535 (formal changes) and pp. 535-545 (constructive changes).

In the situation described above, there is no breach to equal treatment and no requirement for a separate tender process for each category of supplier. The difference in applicable law (CISG or domestic law) simply reflects a factual difference between the suppliers. Being located in different countries, they are subject to a variety of different burdens and are benefitted by a variety of different advantages. The bidder will be allowed to choose whether to take part in the tender as an international company or to set up a place of business in the procuring country. This organization is not different from any other tax or corporate arrangements. The bidder is responsible for the consequences of its choice.

This leads to the application of art.10(a) CISG, which deals with parties that have more than one place of business. The rule provides for the criteria to determine which place of business is material and decisive to the contract.<sup>31</sup>

The application of different rules for the contract depending on the relevant place of business of the winning bidder is possible and lawful. It leads to no invalidity or defect of the tender process. However, it is convenient that the rules are substantially the same to allow for a better comparison between the various bids. In the international practice, it is widely acknowledged that the CISG has been serving as inspiration for the reform of the domestic law on the purchase and sale of goods.<sup>32</sup> This effect has started to take place in Brazil as well. At the time of writing of this paper, a bill pending discussion in Congress for the enactment of a new Commercial Code has formally received amendment requests to include rules similar to the CISG to apply to domestic sales.<sup>33</sup> If this bill passes, the rules for international and domestic sales will be substantially similar. International scholarship mentions a variety of other examples of national law being influenced by the CISG.

Rules such as the Brazilian Commercial Code are not directly applicable to government contracts, only as principles of contract law that are incorporated by domestic law. Nonetheless, a government entity should draft the contract in a way that

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<sup>31</sup> See Schwenger and Hachem in Schwenger. *Commentary* (2010), pp. 199-202. P. Hachem in a later work mentions that the preferable view “operates on a case-by-case basis and relies on the domicile of the place of business which has the strongest influence on the contractual relationship. The strongest influence will typically be exerted by the place of business where customer complaints are ultimately handled, not merely filed, and in particular where the decisions on the next steps to take in handling disputes, including legal measures, are made”, “Applicability of the CISG – Articles 1 and 6” in Schwenger, Y. Atamer and P. Butler, *Current Issues in the CISG and Arbitration* (Eleven, 2014), p. 34.

<sup>32</sup> Schwenger. “Introduction” in Schwenger. *Commentary* (2010), p. 10.

<sup>33</sup> The bill is styled PL 1.572. Amendment 59 creates a domestic system that reproduces many of the CISG provisions.



will reduce the difference between parties that are subject to the CISG and others that may be subject to domestic law. Uniformity may lead to important gains for the procuring agency. The government can create uniformity by adopting contractually agreed-upon rules that are substantially the same for domestic and international suppliers. This will reduce the possible and otherwise lawful discrepancy between the different sets of rules to which each potential party may be subject.

## **8. Need for clarity in government contracts**

The CISG as default applicable law will combine with domestic procurement law and specific contractual provisions, since the latter will be incorporated as Art. 6 derogations of the CISG. This combination will establish the rules ultimately applicable to a certain government contract. This arrangement is valid but highly inconvenient. The procuring government agency should have a clear definition in its contracts of the points in which the CISG provisions will be replaced with domestic law or contractual provisions. The ambiguities or uncertainties must be resolved in favor of the application of the CISG due to the international commitments the Convention is designed to carry out.

In addition to being required by the CISG as a condition for the effectiveness of any exclusion or derogation, clarity in the adoption of the CISG is part of any contracting state's commitment upon joining the CISG system. In the international context, the accession of any country to the CISG community creates in the international counterparties the legitimate expectation that their contracts with the other country's nationals will be governed by the CISG. This expectation must not be frustrated, especially by the government agencies themselves. Therefore, they should avoid using ambiguous contractual language and (or) creating an uncertainty in the international suppliers as to what law and other conditions will apply.

The consequence of these premises is that the general criteria for recognition of an effective exclusion or derogation will apply. Scholars and case law have extensively developed such criteria. In general, both explicit and implied agreements are admitted to exclude or derogate. For instance, whilst case law does not consider a choice of "Brazilian law" as an exclusion of the CISG (since the Convention is part of that law), a choice of "Brazilian Civil Code" may amount to an exclusion under art.6 CISG if it reflects the intent of the parties to adopt an entirely different system of rules rather than

the CISG.<sup>34</sup>

Such reasoning may not be immediately applicable to government contracts, in which a higher standard of clarity is required for an exclusion to take place. International suppliers to a state entity may expect their contracts to be in principle governed by the uniform law adopted by the state. This amounts to a legitimate expectation covered by the protection of trust. By adopting the CISG, a state makes a promise to its potential international suppliers – or buyers, when the state is a seller – that the uniform law will be applicable. This promise does not make it impossible for the state to exclude or derogate from the CISG under art.6. However, it sets a higher standard of proof for the intent to exclude. Protection of trust is generally acknowledged as a derivation of widely accepted public law principles.<sup>35</sup> Such protected trust entitles the counterparties in a government contract for the international sale of goods to expect the CISG to apply unless clearly and expressly excluded. This is a matter of validity of the exclusion based on domestic public law standards, which are incorporated by art.4 CISG.

The same conclusion can be reached from a *contra proferentem* perspective, provided that the relevant government entity in a given transaction unilaterally defines the terms of its contract under public law. This goes beyond the notion that in doubt the application of the CISG should be favored. It requires the contract to be interpreted in any case in favor of the application of the CISG unless the opposite clearly arises from the language of the contract.

In a legal system in which no protection of trust is available and in which government contracts are negotiated without any prevalence of the government position, -- i.e., in which the fundamental terms are not unilaterally set by the procuring agency -- a higher standard of proof for exclusion or derogation will not exist. Conversely, in systems that recognize such higher standard of transparency applicable to government action, an exclusion of the CISG in a government contract must be express and explicit, and the usual standards for exclusion by implication will not apply. The CISG will then

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<sup>34</sup> See Hachem and Schwenzer in Schwenzer. *Commentary* (2010), pp. 114-116, esp. p. 115: “It seems common ground that the reference to a set of non-unified domestic sales provisions sufficiently indicates an intention to derogate from the entire Convention — e.g. ‘this contract is governed by the provisions of the German Civil Code (BGB)’. Such reference may, however, fail to effect a derogation from the entire CISG where the set of rules designated is only applicable to ‘merchants’ as defined by the domestic set of rules envisaged and this requirement is not fulfilled by both parties.”

<sup>35</sup> P. Reynolds. *Legitimate Expectations and the Protection of Trust in Public Officials* (October 8, 2010). Public Law, Vol. 2011, p. 330, 2011. Available at SSRN: <http://ssrn.com/abstract=1689518>

apply given that the contract will be in its sphere of application.

## **9. Role of bid protests and challenges**

Most domestic procurement regulations provide for mechanisms for bidders to interfere in the drafting of the solicitation or the contractual documents. Although this varies from country to country, the potential bidders are generally allowed to object to conditions in the solicitation documents or to challenge specific decisions by the procuring agency. Depending on each domestic system, such challenges may be escalated to higher ranks within the government or ultimately be taken to courts.

The phase after the advertisement of the tender and the actual bidding session is the adequate period for this form of participation. This is the appropriate drafting stage in which the procuring agency will finalize the solicitation and make all necessary decisions that will guide the entire process. If a bidder considers that the provisions concerning the application law are not sufficient, it should exercise its right to protest in order to request the application of the CISG or of part of its rules to the contract at issue.

## **10. Advantages for the procuring agency in applying the CISG**

Another angle to explore is how convenient it may be for the procuring agency to opt to keep the CISG as applicable law on the formation and content of the international sale contract, refraining from excluding or derogating its rules.

Any country that joins the CISG is in a way affirming the virtues of the Convention. This does not entail a duty to apply the CISG provisions. However, it does require the decision to exclude or derogate to be reasonable and grounded on sound legal reasons. Otherwise, a country's own government will be denying the conditions to fulfill the international expectations with regard to such country's disposition in adopting the uniform legislation.

There are important advantages in the total or partial adoption of the CISG to govern the international purchases made by government entities.<sup>36</sup> As pointed out above, countries such as Singapore and New Zealand expressly ensure in their public procurement guidelines the application of the CISG in these cases. The World Bank standard contract form also does not exclude the CISG.

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<sup>36</sup> For a comprehensive overview of why parties should apply or exclude the CISG, albeit not specifically focused on government contracts, see L. Spagnolo, *CISG Exclusion and Legal Efficiency* (Wolters Kluwer, 2014), especially pp. 78-100 (substantive advantages and disadvantages of the CISG) and 101-148 (non-substantive advantages and disadvantages).

First of all, there are CISG provisions that give reassurance to the international supplier and facilitate transactions. Its rules result from extensive discussion and the reconciliation of different legal systems. Three important examples are (i) the duty to inspect the goods and to give notice of non-conformity within a reasonable period (arts.38 and 39 CISG), (ii) the provision that a party is liable only for damages that the party “*foresaw or ought to have foreseen at the time of the conclusion of the contract*” (art.74 CISG) and (iii) the duty to mitigate one’s losses as a requisite for full recovery (art.77 CISG). The derogation of these or other rules will cause contractual insecurity and may discourage responsible suppliers from bidding on a certain procuring agency’s tender processes.

In addition, there is the issue of subcontracting. In many situations, a party supplying international goods to a government agency will have subcontracts that are subject to the CISG. When the government agency can foresee that this is the case, it is especially important that the CISG applies also to the contract between the government agency (ultimate buyer) and the immediate supplier. This will make it easier for the supplier to manage its contractual relationships with its own subcontractors. One of the cases mentioned above relating to the CISG in government transactions is *Diversitel*. The case involved an international sale in the defense sector for the ulterior purpose of supplying the item to Canada’s Ministry of Defense. Even if the CISG does not directly apply to the supply contract, its provisions can inspire a contractual arrangement that is similar to the subcontract. In *Diversitel*, for instance, the immediate contractor was Canadian and, therefore, not subject to the CISG; the Convention applied primarily to the subcontract.

These advantages reflect mainly on the price to be paid. Although there are no specific statistics about this issue, one may infer that an increase in the assurances given to the international bidder will result in reduction of price.

International banks or development agencies also play a role in this matter by analyzing and approving contracts for the use of funds that are donated or loaned. Another of the most well-known cases involving the CISG in government contracts involves a Spanish supplier and the Iraq government within the program *Oil for Food*, with international funding.

A government procuring agency must not take the easy road of simply excluding directly or indirectly the application of the CISG. Either because of the international commitment the CISG represents or of the many advantages of the uniform law, the

government agency is obligated to examine specifically the CISG and decide in a rational manner, with reasons, about its full application or possible derogation.

## **11. Conclusion**

The CISG sphere of application under art.1-3 CISG generally encompasses contracts entered into by government agencies or entities. When a government agency or entity from a CISG contracting state makes an international purchase (or, more rarely, a sale), the CISG will apply unless the relevant contract excludes or derogates the CISG in accordance with art.6 CISG or one of the exclusions of art.2 or 3 CISG is in place. The effectiveness and scope of any exclusion or derogation will be assessed and construed according to arts.7-9 CISG. The constitutional protection of the private counterparty's trust or legitimate expectations may lead to a higher standard of proof for the exclusion of the CISG. A contractual reference to a state's domestic government procurement law will primarily not be interpreted as an agreed-upon exclusion of the CISG, but rather only as a derogation of the contrary CISG provisions based on art.6 CISG.

In most national systems, the main areas of potential conflict between the CISG and international government procurement regulation are the issues of agency (art.4 CISG) and freedom of form (art.11 CISG). However, contract administration issues may be relevant in states in which government procurement legislation comprises not only the selection of the contractor, but also the formation and content of the contract, such as in most Latin American countries and the United States. In the latter states, the role assigned to domestic procurement law is greater, and there will naturally be less space for possible application of the CISG. Government transparency and effectiveness require clarity in the exclusion of the CISG. The lack of clear exclusion will allow a private contractor to rely on the CISG provisions that have not been derogated by contractual provisions or by incorporation of the domestic government procurement regulation into the contract.

Government agencies and entities must weigh the benefits of adopting the CISG. Bidders and interested third parties, such as citizens in systems that recognize the citizen's standing to challenge bidding procedures, have a role under national legislations to participate in the effective adoption of the CISG by submitting protests and challenges. These tools give the bidders the means to influence the final language of the contract with regard to the application or derogation of the CISG.

The CISG interferes directly with any government's international purchases. No government entity in a CISG contracting state may ignore the uniform law. Governments and international bidders must be aware of this legislation and its impact on their international transactions. The application or possible derogation of the CISG in each specific case must be clearly discussed and decided in a rational manner.

Domestic laws generally provide the tools for each government's agencies to make informed decisions and for bidders to directly interfere in the process of creating the solicitation for tenders. These tools comprise the ability to cause the procuring agency to reflect and decide on the application of the CISG based on rational reasons. In countries in which the accession to the CISG is relatively recent, the foreseeable inertia of government agencies to adjust to the CISG may be generally overcome by the active, careful, and attentive conduct of the suppliers that potentially take part in the government's procurement proceedings.