



ORAL MODIFICATIONS OF THE CONTRACT CISG AND CROATIA –

A COMPARATIVE PERSPECTIVE

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TABLE OF CONTENTS

ABSTRACT.....	ii
1. INTRODUCTION.....	1
2. INTRODUCTORY REMARKS ON THE CISG.....	3
2.1 World wide acceptance	3
2.2 Common reasons for non acceptance.....	4
3. CONTRACT MODIFICATION IN THE CISG	6
3.1 Parol evidence rule.....	6
3.1.1 Parol evidence rule in common law doctrine	6
3.1.2 Parol evidence rule within the CISG article 29(1)	10
3.2 Merger clauses – article 29(2)	12
3.3. Interpretation of statements made by the parties – article 8	13
4. CIVIL OBLIGATIONS ACT – MAIN SOURCE OF CONTRACT LAW IN CROATIA.....	19
4.1 Substance of contract modifications	19
4.2 Form of contract modifications.....	20
4.2.1 Formality freedom – articles 286 and 289	21
4.3 Completeness of a legal document – article 291.....	24
4.4 Written confirmation of an oral agreement – article 287	25
5. CONCLUSION	27
6. BIBLIOGRAPHY	29

ABSTRACT

This thesis deals with the common issue of oral modifications made to the written contract. It recognized that the UN Convention on Contracts for the International Sale of Goods is widely recognized but still largely circumvented by practitioners. The same situation occurs in Croatia. Thesis compares the articles on oral modification of the Convention with the according articles of the Civil Obligations Act of the Republic of Croatia. Parol evidence rule, merger clauses and formality freedom concepts are explained in their usual meaning and in the meaning within the Convention. No significant differences exist, moreover the Convention seems to be more appropriate to suit the needs of fast-paced globalized business-doing as its rules are more liberal.

1. INTRODUCTION

In this thesis the solutions offered on the oral modifications of the contract of the United Nations Convention on Contracts for the International Sale of Goods (further on: the CISG, the Convention) and The Civil Obligations Act of the Republic of Croatia (further on: the Act) are compared.

The CISG is a very important international instrument that regulates international sale of goods and Croatia is its signatory party. However, it is often ignored by Croatian legal practitioners for various reasons. One reason is lack of familiarity with the CISG solutions. To answer the question if the solutions provided in the Convention are that much different from the solutions provided in the Act, I will compare them in a small segment of oral modification. This segment is particularly interesting to me because it is essential to merchants who do business in a fast-pace environment and have no time write down every single alteration of their business agreements. The law they apply needs to be flexible, a helping hand not a burden that slows them down. Why do Croatian lawyers see the CISG as a burden rather than as a helping hand? What are the major differences in this segment?

As an introduction to the topic, thesis first addresses world-wide state acceptance of the Convention, then lists major general reasons for non-acceptance by practitioners. Croatian reasons for non-acceptance are subsequently analyzed. Further on, applicable CISG provisions on oral modifications are analyzed, mainly article 29 and article 8 and then they are compared with articles 286-289 of the Civil Obligations Act. Articles of the Convention are analyzed through the doctrine of the parol evidence rule and merger clauses. Their common law origins are compared with CISG solutions. The findings of the comparison

between the CISG and the Act will demonstrate that the differences are small and not significant.

Topic of oral modifications of the contract is not relevant only to the Croatian lawyers but to all practitioners, especially those coming from common law countries, who deal with the CISG as the issue of the parol evidence rule is the most litigated issue of contract law¹ in common law countries and its conflict with formality freedom of the Convention is extremely interesting.

¹ Alberto Luis Zuppi, The Parol Evidence Rule; A Comparative Study of the Common Law, the Civil Law Tradition, and Lex Mercatoria, 35 Ga. J. Int'l & Comp. L. 233, 235-237 (2007).

2. INTRODUCTORY REMARKS ON THE CISG

2.1 World wide acceptance

The United Nations Convention on Contracts for the International Sale of Goods (CISG, the Convention) is today considered to be one of the biggest success stories in the field of unification of international sales law. The idea about the need of unification was born quite early, in the 1920s with the work of Professor Ernst Rabel.² But nobody could have foreseen then that in 2013, 33 years after the CISG has been signed that the number of signatory states would climb up to the impressive 79. Brazil is the latest country that entered the CISG club and that happened very recently - 04.03.2013. Before this last accession, year 2008 was also very important for the international commercial law community because alongside Lebanon and Armenia, Japan as an important economic force signed the Convention.³ United Kingdom remains as one of very few important trading nations still not to sign the Convention.⁴

Does this world wide success reflect in application of the CISG in Croatia? Croatia is a Contracting State without any reservations declared since 8 October 1991 when it assumed the responsibility for its international relations from Yugoslavia.⁵ Even though it has been 21 years since then already and the Convention has been very much analyzed among Croatian legal theorists⁶ it is still hard to say that the CISG is fully accepted in practice. There are only nine recorded CISG cases in the biggest CISG case database online - Pace Law School Institute of International Commercial Law. In this unique place one can find over 2, 800

² Schwenzer, Ingeborg / Hachem, Pascal, The CISG - A Story of Worldwide Success, in: Kleinemann (ed.), CISG Part II Conference, Stockholm (2009) pp. 119-140 available online at

<https://ius.unibas.ch/uploads/publics/9587/20110913164502_4e6f6c6e5b746.pdf> (March 2013)

³ http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG_status.html (March 2013)

⁴ Butler, *infra* note 30 at 54

⁵ <http://cisgw3.law.pace.edu/cisg/countries/cntries-Croatia.html> (March 2013)

⁶ Tepeš, Nina; *Pravo u gospodarstvu: časopis za gospodarsko-pravnu teoriju i praksu*, 50(2011),3; pages 758-793, at 759

cases and 1, 500 scholarly writings on the CISG.⁷ Croatian neighboring country- Serbia has an evidence of 71 cases in this database and judging by this parameter only, a better acceptance of CISG in practice.⁸ Case Law on UNCITRAL Texts (CLOUT) database shows a bit different figures – 16 Croatian cases and just 7 Serbian.⁹ Nevertheless, even if we disregard the comparative approach, still just nine to 16 cases in 21 years seems much too little.

2.2 Common reasons for non-acceptance

The question arises – what are the main reasons of the Convention’s ongoing unpopularity in Croatia? Even though more and more countries join the Convention every year somehow practitioners worldwide are reluctant to use its benefits. Authors Ingeborg Shhwenzer and Pascal Hachem are suggesting three main reasons for this:

- 1) Lawyers are generally familiar with the Convention but they are uncertain about its application and functioning so they rather use their national law.
- 2) Parties to the contract prefer their national law if they are in the position to impose it on a contract.
- 3) Parties do not see the benefits of CISG compared to national laws.¹⁰

Croatian professors claim that lawyers in Croatia hesitate from the application of the CISG for the same reason as all other lawyers – lack of familiarity. Adding to that it is not insignificant to mention that Croatian business community is a small one and not that important in international trade terms.¹¹

⁷ <http://www.cisg.law.pace.edu/> (March 2013)

⁸ <http://www.cisg.law.pace.edu/cisg/text/casecit.html#serbia> (March 2013)

⁹ <http://www.uncitral.org/clout/searchDocument.do> (March 2013)

¹⁰ Schwenzer, supra note 2, at 126

¹¹ Baretić/Nikšić/Croatia, in: Ferrari (ed.) The CISG and Its Impact on National Legal Systems, at 94-97

Addressing the first issue - lack of familiarity it is safe to say that it will become lesser in time since CISG is part of the obligatory law school curriculum¹² and Faculty of Law Zagreb has participated in Annual Willem C. Vis International Commercial Arbitration Moot court competition for some years now. New generations of lawyers are becoming acquainted with the Convention during their formal education. One extra reason that does not provide excuse to Croatian practitioners for excluding the CISG is the fact that Civil Obligations Act¹³ of the Republic of Croatia is in fact in accordance or at least very similar to the solutions Convention offers.¹⁴

Concerning the latter excuse, it is enough to mention that five countries that Croatia exports to the most are all CISG signatory states. In the first half of 2012 Croatia exported most to Italy, Bosnia and Herzegovina, Germany, Slovenia and Austria¹⁵. So even though the total amount of Croatia's international trade may not be that big or relevant in the world wide sense there may well be situations where CISG will be automatically applicable. Croatian lawyers will not always be in the position to represent the stronger party of the contract and impose national law because it suits them most. Sometimes the buyer will be the stronger party and the buyer will insist on the CISG. Even if the buyer does not insist explicitly, CISG will still be applicable as part of the national law system if not properly excluded. Croatian

¹² Baretić/Nikšić supra note 11, at 100

¹³ Civil Obligations act is available in Croatian at <http://narodne-novine.nn.hr/clanci/sluzbeni/288230.html>, unofficial English translation available at <http://www.vsrh.hr/EasyWeb.asp?pcpid=286>

¹⁴ Tepeš, supra note 4, at 761, note 3

¹⁵ This is according to the information available at the Croatian chamber of commerce website: http://www.hgk.hr/wp-content/blogs.dir/1/files_mf/06%202012%20%20%20izvoz%20uvoz%20RH%20svijet%20%20public%20.pdf (March 2013)

lawyers should at least inform themselves how to properly exclude the application of the CISG.¹⁶

3. CONTRACT MODIFICATION IN THE CISG

Contract modification in the CISG is analyzed through the doctrine of parol evidence rule and merger clauses that are contained in article 29 of the Convention and through the rules on interpretation of the statements made by the parties contained in article 8 of the Convention.

3.1 Parol evidence rule

In following two sections this rule concerned with contract formation and modification is analyzed from the common law perspective and from the perspective of the CISG. An answer is given whether there is room for the parol evidence rule in the CISG.

3.1.1 Parol evidence rule in common law doctrine

Most simply put parol evidence rule forbids modification of a written agreement by extrinsic evidence.¹⁷ Extrinsic evidence is defined in Black's Law Dictionary as: evidence relating to a contract but not appearing on the face of the contract because it comes from other sources, such as statements between the parties or the circumstances surrounding the agreement.¹⁸ When there are some terms of the contract that are in writing and some that are not preference is given to the ones that are. There are two main reasons for this: (1) it is considered that it is easier to lie about the contract terms on the witness stand than to commit

¹⁶ Tepeš, supra note 6, at 791

¹⁷ Olson, AJ 1976, 'Parol Evidence in Washington: The Use of Extrinsic Evidence to Address the Integration and Interpretation of Documents', *Washington Law Review*, 4, p. 923, HeinOnline, EBSCOhost, viewed 5 March 2013.

¹⁸ Black's Law Dictionary (9th ed. 2009), available at Westlaw BLACKS.

forgery by tampering the document and (2) memories of a witness fade.¹⁹ American Uniform Commercial Code defines the rule in section 2-202 as follows:

(1) Terms with respect to which the confirmatory records of the parties agree or which are otherwise set forth in a record intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be supplemented by evidence of:

(a) course of performance, course of dealing, or usage of trade (Section 1-303); and

(b) consistent additional terms unless the court finds the record to have been intended also as a complete and exclusive statement of the terms of the agreement .

(2) Terms in a record may be explained by evidence of course of performance, course of dealing, or usage of trade without a preliminary determination by the court that the language used is ambiguous.²⁰

The rule was first established in an English case, known as the Countess of Rutland's Case of 1604.²¹ It was a case concerning real property dispute in which the Countess wished to rely on oral testimony to prove her right in a piece of land. This was not allowed because oral testimony could not beat a written deed. Sir Edward Coke reported on that case and he defined the rule : "[A]written deed will bar parol evidence." It was considered that written testimony is much more relevant than an oral one since oral ones are uncertain due to

¹⁹ White, J 2010, *Uniform Commercial Code*, n.p.: St. Paul, MN : West, 2010, Bibliotheksverbund Bayern, EBSCOhost, at 118

²⁰ UCC is available at: <http://www.law.cornell.edu/ucc/ucc.table.html> (March 2013)

²¹ Daniel, J 2007, 'K.I.S.S. THE PAROL EVIDENCE RULE GOODBYE: SIMPLIFYING THE CONCEPT OF PROTECTING THE PARTIES' WRITTEN AGREEMENT', *Syracuse Law Review*, 57, p. 227, LexisNexis Academic: Law Reviews, EBSCOhost, viewed 5 March 2013.

„slippery memory“.²² Soon the rule outgrew real property law and became a part of contract law forbidding generally oral variations of written agreements.²³ Today, parol evidence doctrine is considered to be one of the reasons why the UK still did not join the CISG and why parties in common law countries generally may opt out of the entire convention or at least part on contract formation and modification.²⁴ Author Juanda Lowder Daniel suggests that the name of this rule should be changed. Parol means oral, unwritten as defined in Black's law dictionary²⁵ or literally „by word of mouth“ according to Merriam-Webster's²⁶ and there is no issues with this part of the name. However, “evidence” part of the name suggests that this is a procedural rule, however it is not. This is a substantive law doctrine. Therefore the author suggests that the rule should be addressed as what it substantially is: „the rule designed to protect the parties' written agreement from impeachment by allegations of prior or contemporaneous matters not found in the writing“.²⁷ Also, some authors dispute the fact that parol evidence rule can even be called a “rule” considering the vast number of exceptions to the rule and considering it is not one simple rule but rather a complex concept.²⁸

Linguistic issues aside, there are some more important, substantial ones that need to be addressed- for instance ones concerning interpretation of the rule. It is often forgotten that extrinsic evidence is allowed to prove subsequent modifications of the contract terms. In a 1979 US case *Gold Kist, Inc. v Pillow* (582 S.W.2d 77; 1979 Tenn. App. LEXIS 307) there were two agreements between the parties: first one was written and the second one was oral. Court allowed admission of evidence proving the subsequent, oral agreement even though

²² Countess of Rutland's Case, The' 1826, Reports Of Sir Edward Coke, Knt. In Thirteen Parts, p. 50, HeinOnline, EBSCOhost, viewed 5 March 2013.

²³ Daniel, supra note 21, at 234

²⁴ Hunter, Howard; Comparative Sales Law, CEU Legal Studies Department readingmaterial, 2012/2013 at 20

²⁵ Black's Law Dictionary (9th ed. 2009), available at Westlaw BLACKS.

²⁶ Merriam-Webster's Collegiate Dictionary 846 (10th ed. 1993).

²⁷ Daniel, supra note 21, at 237

²⁸ Burnham, SJ 1994, 'Parol Evidence Rule: Don't Be Afraid of the Dark, The', Montana Law Review, 1, p. 93, HeinOnline, EBSCOhost, viewed 5 March 2013.

appellant argued that this would be contrary to parol evidence rule.²⁹ So in essence it is not allowed to use witness statements to prove the original, written agreement but if subsequent oral modifications have been made then witnesses can be called to testify about them. Further on, it is allowed to use extrinsic evidence to prove that there was no intention to start with that the written agreement between the parties should be binding. This rule was set out in a landmark case *Pendleton Grain Growers v. Pedro* (271 Ore. 24; 530 P.2d 85; 1975 Ore. LEXIS 478).

As mentioned above exceptions to the rule today are numerous. Some authors even go so far to say that because of the huge number of exceptions, the very rule has lost its meaning. It is true that from the first, original and strict meaning of the rule until today there have been many changes. The rule has become more flexible and courts do use the help of extrinsic evidence in order to discover the commercial purpose that the parties intended. Just two examples of numerous exceptions are one relating to businessman when courts can investigate the commercial purpose of the agreement to supplement the written terms and the other one relating to contracts that are in part written and in part oral-in those situations it is allowed to use extrinsic evidence for the oral part of the agreement.³⁰ Courts will also take into account extrinsic evidence to resolve ambiguity in the language, explain a technical term or see if performance of the parties caused modification of the agreement.³¹

One example of exception which American authors suggest, after analyzing the wording of UCC 2-202, is that courts can apply extrinsic evidence to prove modifications of a written

²⁹ White, supra note 19, at 118

³⁰ Petra Butler, *The Doctrines of Parol Evidence Rule and Consideration -- A Deterrence to the Common Law Lawyer?*, Singapore International Arbitration Centre, *Celebrating Success: 25 Years United Nations Convention on Contracts for the International Sale of Goods*" (Collation of Papers at UNCITRAL -- SIAC Conference 22-23 September 2005, Singapore), pages 54-66, at 60

³¹ Hunter, supra note 24 at 19

contract if that what is written is not in fact “a final written expression”.³² Extrinsic evidence is not allowed for agreements that are final and written, but if the court finds that the agreement was not final it can accept the extrinsic evidence.

3.1.2 Parol evidence rule within the CISG article 29(1)

Parol evidence rule is relevant in analyzing the CISG articles on formation of the contract and modification of the contract, more specifically articles 11 and 29³³ that prescribe formality freedom. For the purposes of this thesis we will concentrate only on the latter. Can extrinsic evidence be used to prove modification of the contract? The general principle of the CISG is formality freedom which means that a written form is not a prerequisite for contract formation, modification or termination. Parties can use every possible mean to prove the existence of the contract, even witnesses.³⁴ This formality freedom is often very difficult to perceive by legal laymen – parties to the contract often believe that their contract is valid only if written down.³⁵ Same goes for modifications. Absolute freedom of form stems from article 29(1) of the CISG.

„A contract may be modified or terminated by the mere agreement of the parties.“³⁶

Even though such vast formality freedom exists it does not impose any duty on the national judge to value the evidence in a certain way. Evidence rules are procedural rules and as such are not governed by the CISG. Procedural rules of common law states could bar extrinsic evidence to prove modifications and could give more value to written evidence.³⁷

³² White, supra note 19 at 130

³³ Ibid. at 56

³⁴ Ibid.

³⁵ Slakoper, Zvonimir; Gorenc, Vilim; Obvezno pravo, opći dio, Novi informator, Zagreb 2009, at 269

³⁶ Infra note 62

³⁷ Butler, supra note 30, at 57

As mentioned in the sections above, common law courts have come up with many exceptions to the parol evidence rule. When faced with a CISG case the US courts do not apply the parol evidence rule contained in section 2-202 of the UCC but instead give priority to the Convention.³⁸

This wasn't always the case. Before relevant court practice of the CISG was developed courts were hesitant to apply it. They excluded parol evidence just the same as hear-say evidence and applied local rules on procedure and evidence.³⁹ In the *Beijing Metals & Minerals v American Business Centre Inc.* case the court decided that parol evidence rule is a procedural rule of evidence and refused to apply the liberal rules on contract modification and formation of the CISG.⁴⁰ However, later on this practice of US courts has been changed and today they are more inclined to apply the CISG in cases that are governed by the CISG and circumvent the national rule on parol evidence.⁴¹ Today's practice of US courts is followed from the *MCC-Marble* case. In this case second instance court stated that parol evidence rule is not a procedural rule, rule of evidence, but a substantive rule and therefore does not necessarily need to be applied. It also found that the CISG does not contain a parol evidence rule or statute of frauds so the drafters obviously wanted to encourage parties to rely on their oral agreements. Further on, the Court analyzed article 8 of the Convention and correctly stated that negotiations prior to the agreement shall be taken into account when deciding about the terms of the contract.⁴² This is a rule followed in all CISG countries.

Even though under CISG written agreements are completely equal to oral ones, authorities confirm that special consideration will always be given to what the parties have written down and that is what parol evidence essentially is about – respecting what the parties have agreed

³⁸ Ibid. at 58

³⁹ Hunter, *supra* note 24 at 19

⁴⁰ Ibid.

⁴¹ Ibid. at 59

⁴² Ibid.

about and have put it in writing.⁴³ It seems from this that parol evidence and formality freedom can even work together when in hands of a witty and reasonable judge – because as stated previously it is up to every particular judge to decide how much significance will he/she give to a particular oral or written evidence.

3.2 Merger clauses – article 29(2)

Even though parol evidence rule means that the entire agreement of the parties is within the “four corners” of the contract and everything they have negotiated and agreed upon is written down, still the parties can and often do add an extra layer of protection against oral modifications by inserting a merger clause in their contract.⁴⁴ This way they will avoid any doubts on what kind of evidence is allowed to prove terms of the contract. Example of such a clause:

“This agreement signed by both parties and so initialed by both parties in the margin opposite this paragraph constitutes a final written expression of all the terms of this agreement and is a complete and exclusive statement of those terms.”⁴⁵

With this kind of a statement it is clear what the parties want. They specifically and exclusively rely on what has been written down in the contract and they are not allowing prior negotiations, intention or any evidence to be analyzed to prove the content of the terms. This kind of clause can be very much simplify and speed up the court process. Merger clauses (integration clauses, entire agreement clauses, four corner clauses⁴⁶) have been developed and used first just in the American common law but recently they have been

⁴³ Ibid. at 61

⁴⁴ Hunter, *supra* note 24 at 19

⁴⁵ White, *supra* note 19, at 131

⁴⁶ Shwenzer, Ingeborg; *Commentary on the UN Convention on the International Sale of Goods (CISG)*, third edition, Oxford University Press, 2010, article 29

widely used in international commercial contracts. Merger clauses help and fortify the parol evidence rule because they additionally protect the written agreement.⁴⁷

These kinds of clauses are covered in the first sentence of article 29(2) of the CISG:

„A contract in writing which contains a provision requiring any modification or termination by agreement to be in writing may not be otherwise modified or terminated by agreement.“⁴⁸

Schwenzer explains that these clauses exclude subsequent oral agreements and additions. Prior negotiations and terms negotiated orally and simultaneously with the written ones are also excluded if this is not forbidden by national laws on unfair contract terms or standard business terms. Merger clauses are to be interpreted like any other agreement between the parties – in accordance with article 8 of the CISG.⁴⁹ Merger clauses are equally important for individual contracts as well as for framework agreements for future sales contracts that may also impose form requirements.⁵⁰

3.3. Interpretation of statements made by the parties – article 8

As stated in previous chapters contract is modified according to article 29(1) when the parties have reached an agreement about the modification. The existing contract is modified by a new contract – no issues here.⁵¹

Problem arises here: when can it be said with certainty that the parties have reached this agreement? What is an agreement according to the CISG? To determine this we have to take a look at rules governing the formation of the contract. The Convention does not provide the

⁴⁷ 'Demystifying the Parol Evidence Rule - An Analysis of the Parol Evidence Rule in American Contract Jurisprudence and the lack thereof under the CISG' 2009, OAlster, EBSCOhost (March 2013)

⁴⁸ Infra note 73

⁴⁹ Schwenzer, supra note 46

⁵⁰ Ibid.

⁵¹ Camilla B. Andersen & Ulrich G. Schroeter eds., *Sharing International Commercial Law across National Boundaries: Festschrift for Albert H. Kritzer on the Occasion of his Eightieth Birthday*, Wildy, Simmonds & Hill Publishing (2008) 48-61, at 49

definition of the contract explicitly, but rather implies it in articles 14-24. According to these provisions contract is formed when offer and acceptance are exchanged, or more precisely when acceptance becomes effective.⁵² Definition of the contract is not as relevant here as contract formation is not the topic of this thesis and it is too wide and separate to be included. What is more interesting for this topic is the way oral statements made by the parties are interpreted and whether they amount to an agreement or not. To address this issue article 8 of the CISG needs to be looked at. Article 8 will provide an answer to the question what needs to be taken into account when analyzing individual statements made by the parties. Only CISG can give the answer to this question and domestic rules must not be called for because this matter is a matter of sale of goods as set out in article 7(2).⁵³

Article 8 reads:

(1) For the purposes of this Convention statements made by and other conduct of a party are to be interpreted according to his intent where the other party knew or could not have been unaware what that intent was.

(2) If the preceding paragraph is not applicable, statements made by and other conduct of a party are to be interpreted according to the understanding that a reasonable person of the same kind as the other party would have had in the same circumstances.

(3) In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties.⁵⁴

⁵² UNCITRAL publication of the CISG with explanatory note, pdf available at: <http://www.uncitral.org/pdf/english/texts/sales/cisg/V1056997-CISG-e-book.pdf>, at 37

⁵³ Schwenger, Supra note 46, Article 29; 2,3

⁵⁴ Supra note 81

How does the CISG approach interpretation of the parties' statements? As visible from the wording of the first paragraph subjective meeting of the minds is the most important criterion in the article. However, common intention of the parties is limited with a standard well known and common in commerce – „could not have been unaware“. This limitation will come of use when intent of only one party can be determined and the other could not have been unaware of it. Second criterion set out in paragraph two is the objective interpretation criterion where a reasonable person is taken as a standard to which a party in question is compared to. Finally, court can supplement the contract. Although, many legal experts object this kind of interpretation, it will be necessary when determining the intent of the parties would give no result.⁵⁵

Reasonable person of the same kind that is referred in paragraph two is the person who is engaged in the same type of business the contracting party is.⁵⁶ This reasonable person test will come into play when the subjective test fails and it is impossible to determine the subjective intent of the parties. It is sufficiently difficult to determine the intent of a single party let alone the common intent of both parties. Because of this article 8(2) will have more practical significance than article 8(1). Because this is an objective test it is irrelevant how the actual party to the contract understood a certain oral statement, only thing relevant is how a reasonable person would understand it.⁵⁷ Some legal experts suggest a following description of the reasonable person: “The relevant person is a professional who knows the practice of his trade sector, the different modes of sale of the relevant goods and the corresponding jargon, but also the technical procedure of transaction and the technical properties of the

⁵⁵ Schwenger, Article 8, at 145-181

⁵⁶ Ibid.

⁵⁷ Huber, *Peter, Mainz*, Some introductory remarks on the CISG, *Internationales Handelsrecht* (6/2006) 228-238, published by Sellier, European Law Publishers

goods and their utilization.”⁵⁸ For example if one party states that it will deliver goods in eight days and in its dialect this means a week but the other party understands this as a week having only seven days – a reasonable person standard will be implemented and week will be interpreted as a seven day period. Another example is a case when one party says the price is 50 dollars and the other party confirms but it is never specified which dollars American or Canadian. Since a reasonable party in the offerees shoes would assume that the American offeror is offering the price in American, not Canadian, dollars this currency will be applicable to the offer.⁵⁹

Irrespective the fact if subjective or objective standard was used in interpreting the statement, court should give consideration to additional elements cited in article 8(3). First thing explicitly mentioned in the article are negotiations. This means that a common law court will not take into consideration the parol evidence rule. As discussed previously parol evidence excludes extrinsic evidence that appeared during negotiations but 8(3) goes directly against this common law doctrine.⁶⁰ Besides negotiations the court will take a look at practices between the parties, usages and their subsequent conduct. The list provided in the article is not a final and closed one. This follows from the wording of the article when “all relevant circumstances” are mentioned. It is much better that the list is kept open because then the court has a bigger discretion as to what material it will consider when interpreting the statements. Even though court shall take into consideration negotiations between the parties when it will find it necessary, it may be precluded to do so if the contract contains a

⁵⁸ Felix Lautenschlager, Current Problems Regarding the Interpretation of Statements and Party Conduct under the CISG - The Reasonable Third Person, Language Problems and Standard Terms and Conditions, *Vindobona Journal of International Commercial Law & Arbitration* (2/2007) 259-290

⁵⁹ *Ibid.*

⁶⁰ Huber, *supra* note 84

merger clause. Since article 8(3) is a dispositive article, the agreement of the parties to exclude extrinsic evidence will prevail over this provision.⁶¹

Besides negotiations importance is given to practices between the parties. Practices are commonly used by courts and tribunals for interpretation of statements and conduct. For example: if parties have always made business in a way that after an order made by the buyer, seller delivers what was ordered then silence of the seller can be interpreted as acceptance, if parties have always dealt in a way that amount of goods delivered varies +/- 10% then this kind of delivery has to be accepted even though the contract term provides that the variations may be “up to” ten percent.⁶²

Usages and conduct are two last specific factors to be looked at. Problem with usages is that they are also mentioned in article 9 and there is a specific criterion for usages that needs to be met in order for the parties to be bound by them. However, most legal experts consider these usages in article 8(3) to be different from those in article 9. Usages mentioned in article 8(3) can be even local or national as opposed to ones in article 9 that need to be international. When speaking of conduct most widely used example is acceptance of late delivery. If party accepts late delivery without making any objections it is precluded from asserting that time was essential for the contract and that contract was breached fundamentally.⁶³

When interpreting a single statement general rules on interpretation will also be taken into account. Purpose of the contract will be taken into account, the contract will be looked at as a whole – a single statement will be looked at in the context of other provisions, more specific terms and individually agreed upon terms will prevail over standard and general ones, usual meaning of the word will prevail over specific one. Interestingly, good faith is not a principle

⁶¹ Schwenger, Supra note 46

⁶² Ibid.

⁶³ Ibid.

to be called for when interpreting oral statements – it is strictly limited to article 7(1) of the Convention. Finally, one additional interpretation principle is especially important for interpretation of oral statements – *favor negotii*. This principle assumes that parties wished to conclude a contract that has a meaning and serves the purpose they intended. Statements will be interpreted in such a way to keep the validity of the contract and to avoid absurd and contradicting terms.⁶⁴

⁶⁴ Ibid.

4. CIVIL OBLIGATIONS ACT – MAIN SOURCE OF CONTRACT LAW IN CROATIA

Most important source of contract law in Croatia is the Civil Obligations Act of 2005.⁶⁵ This act was passed in 1978 and after the breakup of the Socialist Federal Republic of Yugoslavia in 1991 Croatia as a new and independent state accepted this basic piece of legislature. In 2005 the Act has been heavily modernized and adjusted to European contract law.⁶⁶ There have been some changes in 2008 and 2011 but none concerning contract modification.

It is interesting to notice that the basic provision declaring complete freedom of form of contracts is basically the same in the oldest version of the Act of 1978 and the newest one of 2011.⁶⁷ There have been slight and formalistic changes language wise in a sense that some Serbian words have been replaced with more appropriate, Croatian ones, but the provision is essentially the same. In the 1978 version this is article 67 and in the 2011 version we are speaking of article 286. In conclusion, the principle of formality freedom is present in Croatian legal theory even before and independently of the CISG. More on this topic will be discussed later in this chapter.

4.1 Substance of contract modifications

When Croatian legal experts write on contract modifications they start with explanation what a contract is, or more generally what constitutes every civil obligations relationship. They say that every relationship of such kind is defined by its subjects and its object. Subjects have to be individualized and object needs to be determined or at least determinable.⁶⁸ This means

⁶⁵ Klaric, *infra* note 68

⁶⁶ Foreword to the first edition of the book Klarić, Petar; *Zakon o obveznim odnosima*, Narodne Novine d.d., 2012, foreword available online at: <http://www.nn.hr/PetarKlaricObvezniOdnosi12>

⁶⁷ Compare the wording of the 1978 version :

<http://www.ius.bg.ac.rs/prof/Materijali/karmar/Zakon%20o%20obligacionim%20odnosima.pdf> and the 2011 version available at *supra* note 14.

⁶⁸ Klarić, Petar and Vedriš, Martin; *Građansko pravo*; Narodne Novine d.d., Zagreb, 2008, at 443

that we at least have to know the names of the parties to the contract and if for example the contract is a sale, we have to know what is the thing being sold. When parts of such a relationship are modified are we speaking of a new relationship or is it still the same but altered one? All modern legislators have accepted the solution that a change of subjects does not change the identity of the legal relationship, but the change in its object, its content does change its identity.⁶⁹ In this thesis content of the modification won't be analyzed but the form the modifications are being carried out. It is irrelevant here whether the parties wish to substitute the debtor, the creditor, if a third party is assigned to perform the contract, if they agreed to change the main obligation or just one small aspect of it.

4.2 Form of contract modifications

Oral contracts are contracts concluded without the written evidence of the agreement – either by words, signs or some action that implies assent. The biggest advantage of such contracts is that they can be concluded extremely fast enabling fast movement of goods and services. However, it is very hard to supervise such contracts. It is mostly used in such circumstances where a written form would make business doing unreasonably difficult, for example on farmers markets.⁷⁰ Advantages and disadvantages are the same when we are speaking of oral modifications of a written contract. In today's fast moving society and economy business decisions are being made every minute. Sometimes the parties make a written trace about their subsequent agreement, sometimes they just do not have the time to document their negotiations and modifications.⁷¹ Sometimes it seems like the party insisting on every little modification to be in written is an unfriendly one, one that lacks trust, one that is suspicious. Parties wish to show good faith and friendship while they do business. Sometimes this very

⁶⁹ Ibid.

⁷⁰ Ibid. at 132

⁷¹ Butler, *supra* note 28 at 61

positive intention can result in dangerous legal consequences. Similarly, in arbitration parties often try to be overly friendly and then fall in the trap of drafting arbitration agreements that refer parties to the arbitration only after no amicable solutions can be found. Professor Varady suggests that if parties wish to create a friendly atmosphere they should rather drink a glass of wine together instead of implementing a condition in an arbitration clause that is highly questionable because we can never tell with certainty when the parties actually failed in such an attempt.⁷² Same advice could be given to parties orally modifying the written agreement – whenever possible ask for the written confirmation, it just might become crucial piece of evidence in a potential future dispute. Form requirements are often required not just for evidence purposes, but also for the purposes of entering land registries and enforceability.⁷³ It seems that Croatian legislator was bearing similar thoughts on its mind as articles 286 and 287 of the Civil Obligations Act were written.

4.2.1 Formality freedom – articles 286 and 289

According to Croatian Civil Obligations Act a contract can be concluded in any form whatsoever unless it is otherwise prescribed by law.⁷⁴ Contracts that have a written form requirement are for example: sale of real estate, documentary credits, lease of real estate, license agreement and sale on installments.⁷⁵ Contract additionally can't be in any form, naturally, if parties themselves have agreed that the contract in order to come into existence and become effective needs to be in a specific form. This is prescribed in article 289 of the Act.⁷⁶

To illustrate the differences between the two solutions let us take two sample contracts:

⁷² Tibor Varady, 'The Courtesy Trap – Arbitration "if no amicable settlement can be reached"' (1997) 14 *Journal of International Arbitration*, Issue 4, at 5–12

⁷³ Klarić supra note 34 at 135

⁷⁴ Tepes, Supra note 14

⁷⁵ Crnić, Ivica; *Zakon o obveznim odnosima, Napomene, komentari, sudska praksa i abecedno kazalo pojmova*; Organizator, Zagreb, 2012, at 450

⁷⁶ Ibid.

(1) There is a form requirement prescribed by law – article 286

X and Y have concluded the contract on the sale of Y's real estate – a farm house and the surrounding ranch. Since according to the article 377 of the Civil Obligations Act such contracts need to be concluded in writing they have done so.

(2) There is a form requirement because the parties have agreed so - article 289

X and Y have concluded a contract on the sale of a movable – Y's motor vehicle. Even though there is no form requirement prescribed X and Y have never the less agreed between themselves that if the contract is not in the written form and signatures solemnized by notary public that it would not be effective.

The biggest consequence of these differences is in contract modifications. If the contract form is requested and prescribed by law, every subsequent modification needs to be in that very form.⁷⁷ In our first example this would mean that if the parties agreed in fact not to sell the farm house and the whole surrounding ranch but just the farm house, they would have to modify their agreement in the written form for it to be effective. However, if the parties have decided themselves to insist on a certain form of the contract that is not requested by law, every subsequent modification of that contract can be made in any form.⁷⁸ This means that in the second case scenario even though X and Y have agreed on a written contract with solemnized signatures, if they wish to modify part of the contract such as date of delivery they can do so orally. Moreover, in the second case scenario it is completely irrelevant if the modification alters essential or non essential terms, if the obligation of the party after the modification will be diminished or greater than before.⁷⁹ X and Y could have

⁷⁷ Klarić, supra note 34 at 134

⁷⁸ Ibid at 135

⁷⁹ Ibid

agreed to orally modify the delivery date just as well as the price of the car, price being the essential part of the sale agreement.

First two paragraphs of article 286 form a rule and subsequent two form exceptions. First exception contained in paragraph 3 addresses the issue of non-essential terms agreed upon orally. The exception to the rule is: even though the contract and its modifications need to be in writing, subsequently agreed upon terms that are not essential and that are not mentioned in the contract will be valid even if made orally.⁸⁰ In our first example this would mean: X and Y have not discussed if the empty barrels in the cellar of the farm house would come with the house or not and after they signed the contract they have agreed over the phone to include the barrels in the sale – this kind of modification and agreement would be effective.

Second exception addresses the modifications that are in favor of a party and the rule on the duty of special form of the contract exists only to protect the parties. If parties subsequently and orally modify the contract in a way that after the modification the duties of one party are diminished or less onerous – this modifications will be effective even if there is a special form requirement for the main contract under the condition that this special form request exist solely because it is in the favor of contract parties⁸¹, not the state and public.

Prescribed form article 286 talks about is not only the written form. It can also mean agreement made before witnesses (today extremely rare except in inheritance law – will before witnesses) and with the participation of public bodies (court record, legal act of a notary public, solemnization by notary public).⁸² The Act also recognizes the contracts made

⁸⁰ Ibid

⁸¹ Ibid

⁸² Ibid at 131-134

in an electronic form. Such contracts are effective when parties have agreed upon essential elements, as prescribed in article 293.⁸³

Third and final paragraph of article 289 addresses the issue of contract formation, not modification, but it is worthy to mention that if the parties agree on a certain form as a requirement for the validity of their contract, only in order to have evidence of the contract, then the contract is concluded when the parties have agreed on its terms⁸⁴, not when it is written down and signed. But the obligation of the parties to put the contract in the form they agreed upon is created simultaneously as the main obligations of the contract.

If the contract is not in the form that is either prescribed by the law or decided upon by the parties it will not have any legal effect. There is an exception to this rule if the purpose of the provision in the act that requires form indicates something else but the lack of legal effect as a consequence. This exception does not apply to the situation where the parties themselves have agreed upon a special form requirement.⁸⁵

4.3 Completeness of a legal document – article 291

When parties negotiate the terms of the contract that has a special form requirement and end up entering one term in the written contract but agree on a different term orally - for example for tax purposes they enter one price in the contract but agree on a much higher price – just the terms contained in the written agreement will be effective.⁸⁶ It is important to distinguish this situation from the one in articles 286 and 289 where we are dealing with subsequent modifications. Here, in 291 the original, written contract and the modification both occur in the same time. Oral agreements happen simultaneously with the written terms. It is irrelevant

⁸³ Supra note 14

⁸⁴ Ibid.

⁸⁵ Ibid

⁸⁶ Klarić, supra note 34 at 135

for this rule if the special form requirement is prescribed by law or decided upon by the parties.

However, this rule has met several different interpretations in the practice of Croatian courts. First group of judges interpret the rule in a way that the buyer owes the price from the written contract because the orally agreed upon term is not binding due to lack of form. Second group suggest that the orally agreed price is valid because it reflect true will of the parties and the third group is the most rigorous one because they see the whole agreement as non effective. The third group hold that the orally agreed price is not valid due to lack of form and the price in the written contract is not valid because it does not reflect the true will of the parties. The most authoritative opinion is that “oral agreement about the price is effective even though the written agreement on the sale of real estate contains a different price” and that the buyer who refuses to pay the orally agreed price is dishonest when he insists on paying an illusory price stated in the written agreement.⁸⁷

There are two exceptions to the basic rule of article 291, paragraph one. They are identical to the exceptions of the rule contained in article 286 with only one minor difference. Article 291 paragraph 2 states that besides being non essential, simultaneous and not mentioned in the written contract – oral modifications will be valid under the condition that they are not contradicting to the written terms.⁸⁸

4.4 Written confirmation of an oral agreement – article 287

A new rule has been introduced in the Civil Obligations Act in 2005 regarding oral agreements. According to this new rule in article 287 every party in an oral agreement has a right to request from the counter party to provide a written confirmation of an oral agreement.

⁸⁷ Ibid.

⁸⁸ Ibid.

The obvious purpose of this provision is to keep an evidence of a permanent value about the agreement made and to avoid potential disputes on the terms of the contract. Orally concluded contract will be valid even without this kind of confirmation. Additionally, if the party who is requested to return the signed contract as a confirmation of the oral agreement does not do so the decision of the court can replace it.⁸⁹ Since written confirmation is not necessary for the contract to be effective, we can assume that the only practical advantage of this is having solid evidence in case of a dispute. However, it won't have much use if the party refuses to give such a confirmation and then the court has to determine the content of the agreement. In such a case the party is in the exact same place as this provision did not exist at all.

⁸⁹ Klarić, *supra* note 34 at 132

5. CONCLUSION

After a thorough analysis of both the CISG and the Croatian Civil Obligations Act it is safe to say that there are no significant reasons for Croatian practitioners to opt out of the Convention because of the rules on modification of the contract. Fear the lawyers have because of the lack of familiarity with the provisions of the CISG is not rational or well-based on real differences between the two.

As shown, both instruments rely on the principle of formality freedom. Even though the parol evidence rule is a very important legal doctrine in common law countries in the process of negotiations and compromise it was not included in the CISG. Many common law lawyers have had a fear of this formality freedom and preferred their own national laws that contain parol evidence rule instead. Legal experts have shown that this fear is outdated and irrational because CISG acknowledges the special place of written agreements and modifications, the Convention itself allows parties to include in their contract a clause that can substitute the parol evidence rule – a merger clause. Additionally, parol evidence rule itself is losing sense since case law and practice have established numerous exceptions to it. As the application of the Convention rises in common law contracts and disputes, and these countries have had to make more serious adjustments to the principles the Convention contains, it is unclear why do Croatian lawyers still refrain from applying the CISG. Croatia is very familiar with formality freedom as it is present in its main act on contracts from the very beginning.

Lawyers in Croatia should start applying the CISG as it best serves the needs of their clients as it is flexible, liberal and in accordance with the needs of the fast-paced business environment where there is not always enough time to put the oral agreements on paper. Croatian Act has more detailed rules and more possibilities that could slow down the trade. For example - requirement that the sale of goods that is paid in installments needs to be

evidenced in writing, there are complicated rules on oral modifications to the written agreement if the modifications are less onerous, depending if they are material or immaterial, there is a special provision on written confirmation of the oral agreement. All of these provisions seem to over regulate part of law that suffers significantly when it is over regulated. Detailed provisions make sense and they maybe even should be there to protect the regular buyers, non-businessmen. However, when lawyers are drafting the contracts they have to bear in mind that their clients are professional businessmen and it is in their best interest to have a set of rules that supports business doing, not one that imposes more duties.

In conclusion, CISG is a crucial and widely used instrument in the international sale of goods and it should not be ignored by Croatian lawyers. Rules on oral modifications of the contract are more in accordance with business needs of the modern traders than the rules in the Civil Obligations Act.

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