



Kalev Saare

Docent of Civil Law,  
University of Tartu



Karin Sein

Doctor iuris,  
Lecturer of Private International Law,  
University of Tartu



Mari Ann Simovart

LL.M., Lecturer of Civil Law,  
University of Tartu

# The Buyer's Free Choice Between Termination and Avoidance of a Sales Contract

## 1. Introduction

National private law systems of European Union member states have different approaches with respect to freely allowing or restricting the concurrence of avoidance for mistake and termination of contract. For instance in Germany<sup>1</sup>, upon sale of a defective thing, the priority of applying a contractual legal remedy applies, and termination is either excluded or significantly restricted, even though a case of mistake *per se* would actually exist. The Austrian and Swiss civil codes, however, allow free concurrence of such claims; in Spain and Italy, juridical practice has recognised the right of one party — the buyer — to choose the most suitable remedy.<sup>2</sup> There are no provisions in the Estonian Law of Obligations Act<sup>3</sup> (LOA) or the General Part of the Civil Code Act<sup>4</sup> (GPCCA) that would prevent the entitled party from using the most suitable remedy if both termination and avoidance are simultaneously available. Conflicting viewpoints have, however, been expressed on this matter in Estonian legal discourse.<sup>5</sup>

Differing positions with respect to this question have also been assumed in the uniform law instruments (UNIDROIT Principles of International Commercial Contracts<sup>6</sup> (PICC), Draft Common Frame of Refer-

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<sup>1</sup> F. Ranieri. *Europäisches Obligationenrecht*. 2. Aufl. Springer 2003 pp. 344–345.

<sup>2</sup> *Ibid.*, pp. 350, 364.

<sup>3</sup> *Võlaõigusseadus*. – RT I 2001, 81, 487; 2007, 56, 375 (in Estonian).

<sup>4</sup> *Tsiviilseadustiku üldosa seadus*. – RT I 2002, 35, 216; 2007, 24, 128 (in Estonian).

<sup>5</sup> I. Kull and I. Parrest believe that “in the light of the general principles of the law, the regulation included in the special part of the LOA as *lex specialis* should have primacy over the institution of mistake.” See I. Kull, I. Parrest. *Teatamiskohustus võlaõigusseaduse kontekstis* (Notification Obligation in the Context of the Law of Obligations Act). – *Juridica* 2003/4, p. 219 (in Estonian). M. Käerdi believes that in principle, a person has the right to choose. See M. Käerdi. *Eksimuse käsitus tsiviilõiguses* (Treatment of Mistake in Civil Law). Tallinn 2002, p. 68 (in Estonian). In the comments to the Law of Obligations Act it is expressed that “an obligee may have the [...] possibility to choose between a legal remedy and between avoidance of contract [...] for mistake. See P. Varul, I. Kull, V. Kõve, M. Käerdi. *Võlaõigusseadus I. Kommenteeritud väljaanne* (Law of Obligations Act I. Commented edition). Tallinn 2006, p. 322 (in Estonian). It is said in the comments to the Law of Obligations Act regarding sales contracts that in principle, the buyer has a choice, but the general assumption should be that avoidance is against good faith in the event of absence of substantive case of fundamental breach of contract required for termination. See P. Varul, I. Kull, V. Kõve, M. Käerdi. *Võlaõigusseadus II. Kommenteeritud väljaanne* (Law of Obligations Act II. Commented edition), Parts 2–7 (§§ 208–618). Tallinn 2007, p. 38 (in Estonian).

<sup>6</sup> Available at <http://www.unidroit.org/english/principles/contracts/main.htm> (1.05.2008).

ence<sup>7</sup> (DCFR), and Vienna Convention on Contracts for the International Sale of Goods<sup>8</sup> (CISG)). Pursuant to Article 3.7 of the PICC, for instance, a party is not entitled to avoid a contract on grounds of mistake if the circumstances on which that party relies afford, or could have afforded, a remedy for non-performance; i.e., the primacy of a contractual remedy applies. Pursuant to DCFR II.–7:216, however, a person is entitled to freely choose the most suitable remedy. With regard to the CISG, European Union member states have applied different interpretations regarding the relations and primacy of the right of termination of contract in relation to the right of avoidance of a contract governed by national law.<sup>9</sup> The above suggests that the prerequisites for and consequences of termination and avoidance of contracts require a comparative approach and clarification, as do situations of fact wherein the compositions of both termination and avoidance may be simultaneously fulfilled.

This article analyses the institutions of termination and avoidance of contract through the example of a sales contract, because, in practice, the choice between these two institutions causes the most problems in the context of a sales contract. Because of the limited scope of the article, it discusses only the legal remedies belonging to the buyer. The task of this research project does not include the specific types of sales contract, such as sale on approval, sale with right of repurchase, or the differences related to consumer sales — except by reference to a single characteristic example. As an example for grounds for avoidance, this article examines only mistake as one of the most commonplace grounds for avoidance of sales contract in practice, other possible grounds for avoidance are not looked at.

The article aims to determine whether in Estonian private law it would be necessary to set forth certain priorities or restrictions regarding the choice between these two legal remedies, or can justification be found for the DCFR rule that a person may choose freely between these legal remedies? The article therefore discusses the more significant problems concerning the possible priority between termination and avoidance, or the allowing of free choice between them. The study's hypothesis argues that establishing the priority of one institution over another with no exceptions is unjustified, and that in specific cases possible restrictions for preferring one over another can proceed only from general principles of civil law, primarily from the principle of good faith. With regard to the Estonian legal order, we proceed from the presumption that there cannot be an *a priori* right or wrong solution regarding the relationship between avoidance and termination. This does not, however, exclude the possibility that in other legal orders the same question could not be governed differently, depending on the peculiarity of the given order in question.<sup>10</sup>

## 2. Comparison of material grounds for termination and for avoidance

### 2.1. The possibility of simultaneous presence of grounds for termination and for avoidance

Concurrence of avoidance of sales contract and contractual claims (primarily termination, but in single cases also avoidance for mistake and the claim for amendment of contract pursuant to the *clausula rebus sic stantibus* doctrine<sup>11</sup>) emerges in the event that the circumstances of fact make up both legally relevant cases. This is primarily possible where a circumstance related to any characteristics of a sold thing that the buyer or the buyer and seller together assumed in error also becomes a condition of the sales contract and, in the event the given circumstance differs from reality, entails breach of contract by the seller and, thus, liability of the seller.<sup>12</sup> This constitutes a situation in which a flaw in the object sold, deemed to be fundamental breach, also constitutes a relevant mistake for the purposes of GPCCA § 92 and DCFR II.–7:201 — i.e., erroneous assumption of existing facts, whether caused by the other party, recognised by the other party, or commonly assumed if, the actual circumstances having been known, the transaction would not have been concluded in the first place or would have been concluded under materially different conditions, and the mistaken party does not bear the risk of mistake. An example could be employed from the official comments to the PICC<sup>13</sup> wherein A, a farmer, who

<sup>7</sup> C. von Bar, E. Clive, H. Schulte-Nölke (eds.), Principles, Definitions and Model Rules of European Private Law. Draft Common Frame of Reference (DCFR) Interim Outline Edition III. München: Sellier 2007. Available at [http://www.law-net.eu/en\\_index.htm](http://www.law-net.eu/en_index.htm) (28.04.2008).

<sup>8</sup> Ühinenud Rahvaste Organisatsioon konventsioon kaupade rahvusvahelise ostu-müügi lepingute kohta. – RT II 1993, 21/22, 52 (in Estonian).

<sup>9</sup> F. Ranieri (Note 1), pp. 363, 375.

<sup>10</sup> P. Huber. Die Konkurrenz von Irrtumsanfechtung und Sachmängelhaftung im neuen Schuldrecht. Festschrift für Walther Hadding. Walter de Gruyter Verlag 2004, p. 105.

<sup>11</sup> On the distinguishing between the institutions of *clausula rebus sic stantibus* and mutual mistake, see M. Käerdi (Note 5), pp. 71–73.

<sup>12</sup> P. Varul *et al.* Law of Obligations Act I (Note 5), p. 37.

<sup>13</sup> Available at <http://www.unilex.info/dynasite.cfm?dssid=2377&dsmid=13637&x=1> (13.05.2008).

finds a rusty cup on the land sells it to B, an art dealer, for 10,000 euros. The high price is based on the assumption of both parties that the cup is made of silver, as other silver objects had previously been found on A's land. It subsequently emerges that the object in question is an ordinary iron cup worth only 1000 euros. Accordingly, B refuses to accept the cup and to pay the agreed price, on grounds that it does not comply with the terms of the contract. B also avoids the contract on grounds of mistake as to the quality of the cup.

The following differences can be found between the elements of the compositions of termination of sales contract and avoidance of sales contract for mistake: 1) the right of termination emerges if the problem lies in the performance of a concluded, valid contract (LOA § 101 (1) 4), § 116 (1), DCFR III.–3:501) whereas the right of avoidance for mistake emerges if the problem is related to the conclusion of the contract<sup>\*14</sup> (pursuant to GPCCA § 92 (3) and DCFR II.–7:201); 2) termination presupposes a fundamental breach of contract (pursuant to LOA § 116 (2) and § 223, and DCFR III.–3:502 (1)), with the presence of a fundamentally erroneous assumption of actual circumstances upon entry into a transaction being required as grounds for mistake (i.e., in the presence of a correct assumption, the transaction would not have been entered into at all or would have been entered into under different conditions (pursuant to GPCCA § 92 (1) and (2), as well as DCFR II.–7:201 (1) (a)); and 3) if one of the grounds for identifying a material breach of contract, prerequisite for termination, pursuant to Estonian law, constitutes failure to eliminate initial (also immaterial<sup>\*15</sup>) non-performance by the additional term (LOA § 114 and § 116 (2) 5), and § 223 (1)), avoidance for mistake is not related to the possibility of eliminating the non-conformity, although the other party is able to eliminate the grounds for avoidance of contract by recognising the contract as understood by the mistaken party (GPCCA § 93, the same in DCFR II.–7:203). These differences, and also similarities of compositions, are discussed next, in sections 2.2–2.3 of this paper.

## 2.2. Fundamental breach and fundamental mistake

Application of termination as a contractual remedy generally presupposes fundamental non-performance of a contractual obligation (see LOA § 116 (1), the Civil Code of the Federal Republic of Germany<sup>\*16</sup> (BGB) § 323 (1) and (5), the Civil Code of Holland<sup>\*17</sup> (BW)'s Article 6:265 (1), CISG Article 49, PICC Article 7.3.1 (1), and DCFR III.–3:502 (1)). As an exception we can cite English law, under which the right of termination depends not on the severity of the breach but on the type of contractual obligation breached.<sup>\*18</sup>

With regard to sales contracts, a breach of contract can be related to delay of performance of obligation and to unsatisfactory performance. The Estonian Law of Obligations Act, unlike the BGB, CISG, and PICC, enables turning a non-fundamental unsatisfactory performance into a fundamental breach of contract through an additional term for elimination of flaws given to the obligor (LOA § 116 (2) 5), and with regard to sales contracts this mostly constitutes the claim for repair of a thing, LOA § 223<sup>\*19</sup>). However, pursuant to DCFR III.–3:503, the institution of fixing an additional period of time is primarily related to delay in performance. That Estonian law allows deeming an immaterial unsatisfactory performance to be a fundamental breach of

<sup>14</sup> See also M. Käerdi (Note 5), p. 73: “[a] mistake always presupposes a non-conformity between the actual situation during entering into a transaction and the situation constituting the content of the declaration of intent aimed at entering into the transaction.”

<sup>15</sup> V. Kõve. *Lepingu ühepoolse lõpetamise võimalused Eesti õiguses (võrdlev käsitlus)*. Magistritöö (Possibilities of Unilateral Termination of Contract in Estonian Law (comparative approach). Master's Thesis). Tartu 2003, p. 125 (in Estonian); P. Varul *et al.* *Law of Obligations Act I* (Note 5), p. 402.

<sup>16</sup> BGBI 1896, 195.

<sup>17</sup> Entered into force on 1.01.1992.

<sup>18</sup> H. Sivesand. *The Buyer's Remedies for Non-conforming Goods*. Sellier. – European Law Publishers 2005, pp. 73, 79.

<sup>19</sup> LOA § 116: “(2) A breach of contract is fundamental if:

1) non-performance of an obligation substantially deprives the injured party of what the party was entitled to expect under the contract, except in cases where the other party did not foresee such consequences of the non-performance and a reasonable person of the same kind as the other party could not have foreseen [...] consequences under the same circumstances;

2) pursuant to the contract, strict compliance with the obligation which has not been performed is the precondition for the other party's continued interest in the performance of the contract;

3) non-performance of an obligation was intentional or due to gross negligence;

4) non-performance of an obligation gives the injured party reasonable reason to believe that the party cannot rely on the other party's future performance;

5) the other party fails to perform any obligation thereof during an additional term for performance specified in § 114 of this Act or gives notice that the party will not perform the obligation during such term.”

“§ 223: (1) The seller is deemed to be in fundamental breach of a sales contract also if, inter alia, the repair or substitution of a thing is not possible or fails, or if the seller refuses to repair or substitute a thing without good reason or fails to repair or substitute a thing within a reasonable period of time after the seller is notified of the lack of conformity. (2) In the event of customer sale, any unreasonable inconvenience caused to the buyer by the repair or substitution of a thing is also deemed to be a fundamental breach of contract by the seller. (3) In the cases specified in subsections (1) and (2) of this section, the purchaser is not required to determine an additional term specified in § 114 of this Act and has the right, inter alia, to withdraw from the contract.”

contract has been pointed out by Justice of the Supreme Court Villu Kõve.<sup>\*20</sup> It has also been found in the comments to the Law of Obligations Act that such a regulation may not be just or justified, and reference has been made to the necessity of amending such a regulation.<sup>\*21</sup> At the same time, the misuse of the right of relevant termination is nevertheless restricted by the principle of good faith<sup>\*22</sup> which, pursuant to LOA § 6, also has the primacy over the law and certainly mitigates the severity of this problem.

Keeping in mind the principle of good faith, Estonian legal discourse has also expressed the viewpoint that the possibility of avoidance for mistake cannot be considered justifiable in a situation where the buyer has no right to terminate the contract on account of non-materiality of the breach but, because of mistake, avoidance could be possible.<sup>\*23</sup> A situation in which a circumstance does not constitute a fundamental breach of contract in a contractual relationship but at the same time can objectively be determined to be a relevant mistake for a reasonable person<sup>\*24</sup> should in reality occur relatively seldom. It is more likely that if certain breach by a seller must be regarded as immaterial, the same situation generally does not include elements of a relevant mistake for a reasonable person. Namely, the standard of a reasonable person is to be implemented normatively, comprising the value judgements of the society<sup>\*25</sup>, and, that being the case, lower standards than those applied upon evaluation of the fundamentality of the breach by a certain party to the contract in a similar situation should not generally be presumed to be established. Considering the above, we do not find it justifiable or necessary to restrict the possibility of avoidance with dependence on the occurrence of a fundamental breach of contract in the same factual circumstances.

### 2.3. Knowledge of circumstances of breach or of mistake, and allocation of risk between parties

Modern transaction theory<sup>\*26</sup> often supports the possibility of using various legal institutions and legal remedies on the principle of risk allocation.<sup>\*27</sup> With regard to avoidance, it is worth bearing in mind that if, as a rule, persons themselves bear the risk that their intention has been formed by means of correct assumptions and, in view of all circumstances, the person's right of avoidance will nevertheless be considered to be an exception if the mistake has been caused by the other party or is mutual (see, for example, DCFR II.–7:201 (1) (b), PICC Article 3.5, BW Article 6:228, and GPCCA § 92 (3)). In these cases, the trust in the contract remaining valid does not deserve protection<sup>\*28</sup>. At the same time, avoidance of contract is excluded if the mistake concerns circumstances the risk of which is borne by the mistaken party (pursuant to GPCCA § 92 (5) and also DCFR II.–7:201 (2) (b)), meaning those belonging to said party's sphere of influence.<sup>\*29</sup> Similarly, termination as a legal remedy is excluded in the event that the non-performance underlying the termination has been caused by the party wishing to terminate the contract or it belongs to its own sphere of influence.<sup>\*30</sup> With regard to sales contracts, this principle is specified in LOA § 218 (4), which provides that the lack of conformity of a thing does not provide grounds for application of contractual remedies to the seller if the buyer was or ought to have been aware of the lack of conformity of the thing upon entry into the contract. A similar principle is established in DCFR III.–3:502 (2) (a). The buyer's awareness or obligation of awareness of the non-conformance of a thing at the time of entry into a sales contract thus excludes the buyer's right of termination of the sales con-

<sup>20</sup> V. Kõve (Note 15), p. 125.

<sup>21</sup> P. Varul *et al.* Law of Obligations Act I (Note 5), p. 402.

<sup>22</sup> I. Kull. Hea usu põhimõte kaasaegses lepinguõiguses (Principle of Good Faith in Modern Contract Law). Tartu University Press 2002, pp. 168–174 (in Estonian).

<sup>23</sup> P. Varul *et al.* Law of Obligations Act II (Note 5), p. 38.

<sup>24</sup> Fundamental breach of contract, as a basis for termination, is determined in law as a partially subjective criterion depending on what the *injured party* was entitled to expect under the contract, or what was the precondition of his continued interest (LOA § 16 (2)); however, in identifying a relevant mistake, only the objective criterion — a reasonable person — is followed (GPCCA § 92 (2)).

<sup>25</sup> M. A. Simovart. The Standard of Reasonableness in Estonian Law. – I. Kull (ed.). Development of Estonian Contract and Company Law in the Context of the Harmonized EU Law I. Tartu 2007, p. 69.

<sup>26</sup> This can be opposed by the classical transaction theory, which mainly proceeds from the intention theory and which consider a mistake to constitute the divergence between a person's actual intention and the objective declaration of intent. See K. Saare, K. Sein, M. A. Simovart. Differentiation of Mistake and Fraud as Grounds for Rescission of Transaction. – *Juridica International* 2007/1, p. 143. This article only comparatively discusses the institution of mistake based on the viewpoints of contemporary transaction studies, and termination as a legal remedy.

<sup>27</sup> K. Sein. Ettenähtavus ja rikutud kohustuse eesmärk kui lepingulise kahjuhüvitise piiramise alused. Doktoritöö (Foreseeability and the Purpose of the Obligation Theory as Grounds for Limitation of Damages in Contractual Relationships. Dissertation). Tartu 2007, p. 97 (in Estonian).

<sup>28</sup> K. Saare *et al.* (Note 26), p. 143.

<sup>29</sup> On the principles for determination of risk allocation see K. Sein (Note 27), pp. 97–103.

<sup>30</sup> LOA § 101 (3): “An obligee shall not rely on non-performance by an obligor nor resort to legal remedies arising therefrom insofar as such non-performance was caused by an act of the obligee or by circumstances dependent on the obligee or by an event the risk of which is borne by the obligee.”

tract; neither can the buyer in such cases avoid contract for a fundamental mistake, as in that case the buyer will bear the risk of the mistake (GPCCA § 92 (5), DCFR II.–7:201 (2) (b)).

The principle that restricts or excludes the possibility of avoiding a contract for mistake in a situation in which the mistake is caused by the mistaken party — i.e., where the mistaken party bears the risk of mistake — is recognised by some other European countries besides Estonia.<sup>\*31</sup> The above can be considered the view of contemporary transaction studies addressing the questions of mistake, but this view is not, however, widespread.<sup>\*32</sup> The mistake-related provisions of the DCFR have been drawn up for the purpose of achieving a justified balance between the voluntary nature of a contract and the reasonable expectations of the other party.<sup>\*33</sup> It is considered unfair to give a person the right to avoid the contract if that person has mainly caused the mistake, except if the other party can be at least equally 'blamed' for causing the mistake.<sup>\*34</sup> Among the more important key concepts related to delimiting the possible common compositions of termination of sales contract and avoidance of sales contract are the allocation of risks between the parties and satisfactory performance of the duty to inform by the seller. If a buyer's erroneous assumption of the actual qualities of a thing has been the result of a circumstance the risk of which is borne by the buyer, avoidance of the sales contract for mistake is excluded by the buyer directly. This situation resembles (but is not necessarily identical to) the buyer's obligation of awareness of the flaws of the object of the sales contract, excluding avoidance of the contract by the buyer as a legal remedy.

It must be noted that overlap of termination and avoidance of sales contract does also not occur if the circumstance underlying the mistake does not become a condition of the contract — e.g., if the buyer during pre-contractual negotiations refers to qualities of the thing that are not present in reality and if in the sales contract itself all previous agreements and promises are excluded (LOA § 31).<sup>\*35</sup> In this case, the buyer would merely retain the right to avoid the contract, the grounds for avoidance being the circumstances that were reported by the other party during the pre-contractual negotiations and that influenced the mistaken or deceived party to the contract in the direction of entering into a contractual relationship. Termination of contract is not possible in such a case, as there is no breach of the contract itself.

The analysis above has shown that termination and avoidance can be possible in one and the same factual situation. It is nevertheless unclear whether a buyer who, presumably, could be entitled to both avoidance and termination of a sales contract is legally allowed to resort to one of these two choices at his own discretion, or should the law set forth a mandatory provision as to which of the two to prefer? In order to clarify this question, we next examine whether differences are present in the implementation of the two institutions, and what they are, and the extent to which such differences influence the interests of either party.

## 3. Execution of termination and avoidance

### 3.1. Form and content of notices of termination and avoidance

Both termination and avoidance occur by an entitled person's submission of notice to the other party (LOA § 188 (1) and GPCCA § 98 (1)); i.e., in both cases we are dealing with a unilateral formative right and not claims.<sup>\*36</sup> As this is a formative right, neither of the rights is subject to a limitation period.<sup>\*37</sup> Termination and avoidance are set forth as a self-help right remedies also in DCFR II.–7:209 and III.–3:507, with the same being done in the national laws of many European countries, among them the United Kingdom<sup>\*38</sup>, Ireland, the Czech Republic, Finland, Sweden, Portugal, Holland, and Spain.<sup>\*39</sup> Under Scottish law, it is sufficient

<sup>31</sup> DCFR II.–7:201, Notes VIII–41, 42, Comments, A.

<sup>32</sup> Germany and Switzerland, for instance, do not proceed from the principles of modern transaction theory upon discussing mistake. See DCFR II.–7:201, Notes VIII–43.

<sup>33</sup> DCFR II.–7:201, Comments, A.

<sup>34</sup> DCFR II.–7:201, Comments, J. Identification of the so-called self-induced mistake is dependent upon both the content of the transaction and the circumstances of entering thereinto.

<sup>35</sup> P. Varul *et al.* Law of Obligations Act II (Note 5), p. 38.

<sup>36</sup> In the case of some types of transaction, avoidance of contracts by unilateral declaration of intent is either excluded or restricted under Estonian law. In those cases, special regulation is applied in the form of subjecting to court or other dispute resolving authority (e.g., contracts of employment pursuant to § 125 (1) of the Contracts of Employment Act (*töölepingu seadus*). – RT 1992, 15/16, 241; RT I 2007, 44, 316, (in Estonian); marital property contracts pursuant to § 11 of the Family Law Act (*perekonnaseadus*). – RT I 1994, 75, 1326; 2006, 14, 111 (in Estonian).

<sup>37</sup> P. Varul *et al.* Law of Obligations Act I (Note 5), p. 411.

<sup>38</sup> See J. O'Sullivan. Rescission as a self-help remedy: a critical analysis. – Cambridge Law Journal 2000 (59), pp. 509–543.

<sup>39</sup> DCFR II.–7:209, Notes, 2; III.–3:507 Notes I–2.

for termination if a person behaves in such a way as to implicitly declare the contract terminated.<sup>\*40</sup> On the other hand, for instance, French and Austrian law require, as a general rule, a court decision in order for a transaction to be avoided<sup>\*41</sup>, and in several countries (e.g., Belgium, Luxembourg, and Italy) a contract may be terminated also by a court decision.<sup>\*42</sup>

Estonian law does not set forth specific requirements related to the content or form of a notice of termination and avoidance.<sup>\*43</sup> Thus, a buyer may, for instance, terminate or avoid a notarised sales contract by submitting an unattested notice to the seller. Furthermore, the LOA's § 13 (2) provides that if a contract is entered into in a specific format pursuant to an agreement between the parties, amendment or termination of the contract need not be in such a format — similarly, it may be presumed that the parties are not required to adhere to the form they have agreed upon in the case of giving notice of termination (as essentially unilateral termination). Notice of termination may, pursuant to the commentaries to the LOA, also be conclusive<sup>\*44</sup> or given in the form of an indirect declaration of intent as defined in GPCCA § 68 (3); however, the authors still find that “the power of a self-help remedy cannot be vested in an ambiguous [...] declaration of intent, as the exercise of such a right must be clear”.<sup>\*45</sup>

At the same time, in the case of the CISG, it is not unambiguously clear whether an indirect declaration is sufficient for termination. On the one hand, it has been found that, on the basis of the general principles of the CISG, mutual notification is crucial<sup>\*46</sup>, but, on the other hand, because of the principle of freedom of form, an indirect declaration of intent should be acceptable for termination, provided that it has been ‘communicated’ to the other party and that it is clearly understandable — for instance, the mere return of the goods supplied cannot be interpreted as valid termination, because the conclusions that can be drawn from such an act may differ.<sup>\*47</sup> Court practice exists pertaining to termination notice given under CISG Article 49; however, the conclusions that have been drawn are somewhat inconsistent.<sup>\*48</sup> Nevertheless, in order to terminate a contract, the related declaration of intent need not directly refer to termination.<sup>\*49</sup>

Neither does Estonian law establish very clear requirements as to the exact content of a termination or avoidance notice — what is important is that the intent of the person be comprehensible. It is not required that a person refer to the legal basis (relevant provision of law) for his claim, nor is it necessary to express the actual reason underlying the termination.

In connection with the above, however, the following problem arises: if a person expresses the intent to **be free from the contract**, without specifying the legal content, then how should one interpret such a declaration — as termination or as avoidance of a contract? The authors of the commentaries to the LOA hold the position that there is no problem concerning the understandability of the content of a declaration of intent if termination is referred to as ‘termination of the contract’, ‘suspension of the contract’, or ‘discontinuance of the contract’, because all of these expressions refer to the cancellation of an existing contract. They do, however, accept tacitly that there may be a problem in delimiting a declaration of intent from avoidance<sup>\*50</sup>. This may prove to be especially complicated where the parties use English for communication purposes, because certain terminological inconsistencies may be observed in English-language materials that deal with termination and avoidance.<sup>\*51</sup> Some problematic terms in this context are ‘termination’, ‘nullification’, ‘repudiation’,

<sup>40</sup> DCFR III.–3:507, Notes I–2.

<sup>41</sup> F. Ranieri (Note 1), p. 336. The same regulation was effective in Estonia before the entry into force of the new GPCCA in 2002.

<sup>42</sup> DCFR III.–3:502, Notes I–1, III.–3-507, Notes I–3.

<sup>43</sup> CCSCd, 19 April 2006, 3-2-1-29-06, p. 20; CCSCd, 12 June 2006, 3-2-1-50-06, p. 23; CCSCd 3-2-1-59-06, p. 16; CCSCd, 13 February 2008, 3-2-1-140-07, p. 35.

<sup>44</sup> CCSCd 3-2-1-50-06.

<sup>45</sup> P. Varul *et al.* Law of Obligations Act I (Note 5), p. 623.

<sup>46</sup> L. A. DiMatteo, L. Dhooge, S. Greene, V. Maurer, M. Pagnattaro. The Interpretive Turn in International Sales Law: An Analysis of Fifteen Years of CISG Jurisprudence. – Northwestern Journal of International Law and Business 2004 (34), pp. 299–440, p. 434, footnote 646. Available at <http://www.cisg.law.pace.edu/cisg/biblio/dimatteo3.html#646>.

<sup>47</sup> U. Magnus. Remedy of Avoidance of Contract under CISG — General Remarks and Special Cases. – Journal of Law and Commerce 2005–2006 (25), p. 427.

<sup>48</sup> L. A. DiMatteo *et al.* (Note 46), p. 405.

<sup>49</sup> For instance, a court decision dated from 3.03.1989, treated as a declaration of intent the telegram sent by a purchaser where he unambiguously declared that in the future he would buy similar goods (shoes) from another manufacturer and terminated co-operation with the seller. The seller who was in breach of the contract could not doubt, because of the circumstances surrounding the case, that the purchaser refused to accept the goods supplied by the seller and therefore the purpose of dispatching the goods remained unfulfilled. It is sufficient that the notice given by the purchaser is clear on the point that due to the seller's breach of the contract the purchaser will not pay the seller because the supply of goods has become useless for the purchaser. Germany, 17 September 1991, Appellate Court Frankfurt (Shoes case). Available at <http://cisgw3.law.pace.edu/cases/910917g1.html>.

<sup>50</sup> P. Varul *et al.* Law of Obligations Act I (Note 5), p. 623.

<sup>51</sup> H. Sivesand (Note 18), p. 9.

‘cancellation’, ‘rescission’, and ‘avoidance’. It is notable for instance that the CISG and related literature use the term ‘avoid’ in the meaning of termination of a contract.<sup>\*52</sup>

The authors of this article believe that if interpretation really would be of no avail in ascertaining which of the two alternatives the person had in mind when giving notice — especially in a situation where the said person was actually unaware of the two potentially differing implications of the notice, one should proceed from the principle of good faith and take the position that the person made the declaration that is more favourable to him.

### 3.2. Temporal limits on termination and avoidance

Insofar as the institutions of both termination and avoidance significantly affect the future relationship between the parties and their trust in the continuing validity of the contract, the exercise of both is temporally limited. Termination as a legal remedy is regulated by LOA § 116 (1) and provisions complementing it — namely LOA § 223 and § 226 in case of a sales contract — and it occurs by submitting a notice of termination to the other party to the contract. Similar provision can be found in DCFR III.–3:503. A notice of termination should be preceded by notification of the seller as to any lack of conformity of a thing within a reasonable period after the buyer became or should have become aware of the lack of conformity (LOA § 220 (1)). The buyer reserves the right to termination without prior notification of lack of conformity only in some exceptional cases (LOA § 221 (1) 1)–2)).

The buyer’s obligation to report any lack of conformity also holds under German law and is one of the reasons that in Germany the priority of a contractual legal remedy is honoured: it is believed that if the buyer were entitled to avoid a contract of sale irrespective of his failure to notify the seller in a timely manner of any lack of conformity, the entire system of regulation of termination and the obligation of notification as to lack of conformity would be rendered senseless.<sup>\*53</sup> Such argumentation is only partially transferable into Estonian law. The authors believe that in the case of a mistake caused by the seller or in that of a recognised mistake (GPCCA § 92 (3) 1) and 2)), free competition between termination and avoidance should be allowed because in that case, similarly to those of intent on the part of the seller, gross negligence, or breach of the notification obligation, the buyer is free to terminate the contract even if he fails to comply with the obligation to notify the other party of lack of conformity (LOA § 221 (1)<sup>\*54</sup>). In the case of a mutual mistake (GPCCA § 92 (3), 3)), if the circumstances cannot be attributed to the seller, it is theoretically possible to apply the principle of good faith and accept the priority of a contractual legal remedy: However, for practical reasons, such a distinction between different types of mistake is inexpedient or altogether impossible — upon becoming aware of a mistake, the buyer need not necessarily know whether it was his own or a mutual mistake.

In connection with the time limit on termination, one also faces the question of whether the buyer who fails to comply with the deadline agreed upon between the parties for the inspection of a thing and for notification of any lack of conformity (e.g., two weeks after delivery of the goods) will, in addition to suffering the loss of the right to terminate the contract, also lose the option of avoiding the contract on the basis of the existence of a mistake, although under GPCCA § 99 (1) 2) said party still has time to exercise that right (as six months have not passed since he became aware of the mistake). The authors believe that the matter depends on the content of the agreement between the parties, which needs to be clarified by way of interpretation. If the agreement concerned just the deadline for termination, there is no basis for extending it to avoidance; if this is the case, the buyer will reserve the right to avoid the contract on the basis of a mistake also after the deadline specified in the contract has passed.

At the same time, the authors also believe that in principle it is possible to agree on the deadline for exercise of the right of avoidance on the basis of a mistake, and thus the parties may agree on a deadline other than that set out in GPCCA § 99 (1) 2).

Until now, Estonian legal theory has not studied the issue of applicability of party autonomy towards the deadline for avoidance based on a mistake, nor is there any related Supreme Court practice. The authors of this article believe that extending party autonomy to this rule should not be considered to be contrary to the spirit of the law or violate the fundamental rights of the parties concerned, i.e., the parties should be entitled to determine the time period during which avoidance based on mistake is acceptable. This would not be the

<sup>52</sup> CISG Advisory Council Opinion No. 5, footnote 9. Available at <http://www.cisg.law.pace.edu/cisg/CISG-AC-op5.html#9>.

<sup>53</sup> Münchener Kommentar zum Bürgerlichen Gesetzbuch. Band I: Allgemeiner Teil. 5. Aufl. Commenter: Kramer. C. H. Beck 2006, § 119, margin number 33.

<sup>54</sup> LOA § 221: “(1) A purchaser may rely on the lack of conformity regardless of the purchaser’s failure to examine a thing or give notification of the lack of conformity of the thing on time if:

1) the lack of conformity of the thing has been caused by the intent or gross negligence of the seller;

2) the seller is aware or ought to be aware of the lack of conformity of the thing or the circumstances related thereto and does not disclose such information to the purchaser.”

case with other grounds for avoidance, such as fraud or taking advantage of aggravating circumstances. The position that the regulation of the deadline for the right of avoidance on the ground of mistake should be treated as dispositive is in accord with DCFR II.–7:215 (2), according to which remedies for mistake may be excluded or restricted unless that exclusion or restriction is contrary to good faith and fair dealing. Therefore, the parties to a transaction are free to agree on a deadline for avoidance on the basis of a mistake that differs from that provided for by the law.

Neither does Estonian law preclude freedom of such agreement, and thus the authors believe that, as a general rule, the parties may agree on a deadline for avoidance that is either shorter or longer than that provided for in the law.

Another factor considered in German law to justify the priority of contractual legal remedies is the requirement that, unlike avoidance, termination must as a rule be preceded by notification of the other party of an additional deadline for proper performance of the contract.<sup>55</sup> The requirement of granting an additional deadline is also present in Estonian law (LOA § 116 (4), § 114, and § 222, as well as § 223 (1)). If an additional deadline is not granted, termination is allowed in all of the cases cited in LOA § 116 (2) 1)–4), including the case where “pursuant to the contract, strict compliance with the obligation that has not been performed is the precondition for the other party’s continued interest in the performance of the contract” (LOA § 116 (4), 2<sup>nd</sup> sentence and § 116 (2) 2)) or where the other party gives notice that said party will not perform the obligation (LOA § 116 (4), 2<sup>nd</sup> sentence). In the event of other types of fundamental breach of contract<sup>56</sup>, termination of the contract without granting of an additional deadline for performance is prohibited if the damage suffered by the non-performing party in the event of termination would be disproportionate in relation to the expenses incurred in the performance or preparation for the performance of the obligation (LOA § 116 (4)). When an additional deadline for performance is granted, it must be reasonable (LOA § 114 (1)). The reasonableness of such a deadline is decided upon on the basis of the general regulation provided in LOA § 7<sup>57</sup>, taking into account all of the circumstances specified therein.<sup>58</sup> Language regulating an additional period of time of reasonable length is also contained in, for example, articles 47 and 53 of the CISG. The obligation to grant an additional deadline — if it exists — distinguishes the procedure of termination from that of avoidance: The GPCCA does not provide for such an obligation in the case of avoidance on the basis of a mistake.

Nevertheless, the GPCCA’s § 93 provides the other party with the option of understanding performance of the transaction as desired by the mistaken party. If this is the case, the option of avoidance is lost (GPCCA § 93 (1)), or, if the right of avoidance has already been exercised, the notice of avoidance shall be deemed invalid (GPCCA § 93 (2)). For instance, a buyer who has entered into a contract on the sale of an immovable discovers, after signing the contract, that the immovable is polluted. The seller failed to disclose this fact to the buyer when the two parties signed the contract and, thus, the buyer submits a notice of avoidance relying on the mistake. If after receiving the notice of avoidance the seller promptly gives notice of his willingness to remove the pollution at his own cost — i.e., to perform the contract on sale as understood by the buyer — the buyer’s notice of avoidance should be deemed invalid and the contract shall be deemed valid on the condition that the seller transfers the immovable free of pollution. If, in the same case, the buyer would prefer to terminate the contract on the basis of a fundamental breach by the seller and grants the seller an additional deadline for removal of the pollution, the final outcome of the case would still be the same: the seller must transfer the immovable free of any pollution. On the basis of this reasoning, priority of termination over avoidance is unnecessary because the seller’s rectifying the lack of conformity after its discovery excludes both options, terminating and avoiding the contract, for the buyer.

Notice of termination must be provided within reasonable time after a party to the contract has become or must have become aware of a fundamental breach of the contract (LOA § 118 (1) 1)) or after passing of the previously described additional deadline granted in accordance with the LOA’s § 114. Similar regulation of the deadline for notice of termination can be found in the PICC’s Article 7.3.2 (2), in the DCFR’s III.–3:508 (2), and also according to Article 49 (2) (b) of the CISG in the cases in which the seller has already delivered the goods to the buyer. The CISG’s Article 49 (1) regulates termination in a situation wherein the delivery has not occurred; in such a case, termination must occur either during the limitation period or by the deadline provided for in national law. Therefore, under Article 49 (1), termination is possible over rather a lengthy period of time.<sup>59</sup>

As mentioned above, the determination of a reasonable deadline depends on the various factors listed in § 7 of the LOA and, accordingly, may be rather different for different contracts. One finds in official commentaries to the PICC<sup>60</sup>, for example, that termination within reasonable time may mean immediate or prompt termination

<sup>55</sup> Münchener Kommentar/Kramer (Note 53), § 119, margin number 33.

<sup>56</sup> A sample list of fundamental breaches of contract is provided in § 116 (2). See Note 19.

<sup>57</sup> M. A. Simovart (Note 25), pp. 65, 70.

<sup>58</sup> CCSCd 3-2-1-44-04.

<sup>59</sup> U. Magnus (Note 47), p. 429.

<sup>60</sup> Available at <http://www.unilex.info/dynasite.cfm?dssid=2377&dsmid=13635>.



if a party is able to easily enter into a substitute transaction; where the possibility of a substitute transaction needs to be investigated, what constitutes reasonable time before the deadline is deemed to be longer. According to the commentaries to the Estonian LOA, a **reasonable** deadline cannot, as a rule, be construed as immediate or prompt notification and must, as a rule, in addition to searching for other options, take into account the time needed to become aware of the breach and weigh one's options (e.g., involving a lawyer).<sup>\*61</sup>

The main factors affecting the amount of time for a reasonable deadline for termination in application of the CISG's Article 49 (2) (b) are the nature of the goods that are the object of the contract and the other facts of the case.<sup>\*62</sup> Court practice reflects the position that the term for termination on grounds of fundamental breach starts at the moment when the buyer becomes aware of the **fundamental** nature of the breach and not the moment when the breach actually began.<sup>\*63</sup> We present here some examples from court cases in which Article 49 was applied: notice of termination given after five months<sup>\*64</sup>, eight months<sup>\*65</sup>, or three years<sup>\*66</sup> from one's becoming aware of a fundamental breach does not constitute notice within reasonable time; by contrast, one day<sup>\*67</sup>, 48 hours<sup>\*68</sup>, approximately 2.5 months<sup>\*69</sup>, and also three months<sup>\*70</sup> after discovery of a fundamental breach have been deemed to constitute a reasonable period for giving notice of termination. What is important here is that the reasonableness of the deadline is in any case dependent on the specifics of the case in question<sup>\*71</sup>, although a reasonable deadline is generally shorter rather than longer, usually being a couple of months at most.<sup>\*72</sup> German law, however, ties the deadline for exercising one's right of termination to the general limitation period applicable for claims (BGB §§ 218 and 323).<sup>\*73</sup>

The third reason German legal practice has treated contractual legal remedy (i.e., termination) as primary where there is competition between termination and avoidance is the short limitation period applicable for claims related to lack of conformity (up to six months before the BGB was reformed), which protects the seller and which should not be suppressed by the right of avoidance arising out of the BGB's § 119 (2). In the post-reform BGB and following introduction of changes to the regulation of the limitation period (BGB § 438), the issue of the deadline is no longer relevant in the context of protection of the rights of the seller.<sup>\*74</sup> Different countries employ rather different periods for giving notice of avoidance.<sup>\*75</sup> Pursuant to the BGB's § 121, notice of avoidance is to be given, without wrongful delay, from the moment when the party entitled to avoidance becomes aware of the basis for avoidance, while in German judicial practice promptly given notice has been understood to be notice given within two weeks after discovery of breach.<sup>\*76</sup> Under Swiss law, a person entitled to avoidance has one year after finding out about a mistake to give notice of avoidance (see Part 5 of the Swiss Civil Code: Article 31 of the obligation law (OR)<sup>\*77</sup>), and that time is three years under Austrian law (Article 1487 of the Austrian Civil Code<sup>\*78</sup>) and, in Holland, three years after discovery of a mistake (BW Article 52 (1)). Pursuant to DCFR II.–7:210, notice of avoidance has no legal effect unless given within reasonable time, with due regard to the circumstances, after the avoiding party knew or could reasonably be expected to have known of the relevant facts.

Under Estonian law, preference for termination over avoidance based on deadline is irrelevant, as the deadlines set for the exercise of the rights of termination and avoidance are, as a rule, not dramatically different temporally. As mentioned above, the right of termination ends upon a reasonable period of time having elapsed from

<sup>61</sup> P. Varul *et al.* Law of Obligations Act I (Note 5), p. 413.

<sup>62</sup> R. Koch. Commentary on Whether the UNIDROIT Principles of International Commercial Contracts May Be Used to Interpret or Supplement Articles 47 and 49 of the CISG. December 2004. Available at <http://www.cisg.law.pace.edu/cisg/principles/uni47,49.html#rkiii>; U. Magnus (Note 47), p. 428.

<sup>63</sup> Italy, 13 December 2001, District Court Busto Arsizio (Machinery case). Available at <http://cisgw3.law.pace.edu/cases/011213i3.html>.

<sup>64</sup> Germany, 15 February 1995, Supreme Court (Key press machine). Available at <http://cisgw3.law.pace.edu/cases/950215g1.html>.

<sup>65</sup> France, 14 June 2001, Appellate Court Paris (*Aluminium and Light Industries Company v. Saint Bernard Miroiterie Vitrierie*). Available at <http://cisgw3.law.pace.edu/cases/010614f1.html>.

<sup>66</sup> Finland, 12 April 2002, Turku Court of Appeal (Forestry equipment case). Available at <http://cisgw3.law.pace.edu/cases/020412f5.html>.

<sup>67</sup> Germany, 17 September 1991, Appellate Court Frankfurt (Shoes case). Available at <http://cisgw3.law.pace.edu/cases/910917g1.html>.

<sup>68</sup> Spain, 3 November 1997, Appellate Court Barcelona (Rolled steel case). Available at <http://cisgw3.law.pace.edu/cases/971103s4.html>.

<sup>69</sup> Canada, 20 September 2002, Court of Queen's Bench of Manitoba (*Brown & Root v. Aerotech*). Available at <http://cisgw3.law.pace.edu/cases/020920c4.html>

<sup>70</sup> Germany, 22 August 2002, District Court Freiburg (Automobile case). Available at <http://cisgw3.law.pace.edu/cases/020822g1.html>.

<sup>71</sup> L. A. DiMatteo *et al.* (Note 46), p. 406.

<sup>72</sup> "In this kind of commercial transaction, a reasonable time for notice is most often very short, at most a few months. To extend this period would require pressing circumstances indeed." HO Turku, 12 April 2002.

<sup>73</sup> Palandt. Bürgerliches Gesetzbuch. 65. Aufl. München 2006. C. Grüneberg § 323, comm. 33 (p. 526).

<sup>74</sup> K. Larenz, M. Wolf. Allgemeiner Teil des Bürgerlichen Rechts. München: C.H. Beck 2004, § 36, margin number 50 (p. 665).

<sup>75</sup> DCFR II.–7:210, Notes I–1, 2.

<sup>76</sup> Palandt. Bürgerliches Gesetzbuch. 65. Aufl. München, 2006. Helmut Heinrichs § 121, commentary 2 (p. 93).

<sup>77</sup> Adopted on 30 March 1911.

<sup>78</sup> Adopted on 1 June 1811.

the moment a party to the contract became or must have become aware of a fundamental breach of contract, while the right of avoidance expires six months after discovery of a mistake (GPCCA § 99 (1) 2)) but not later than three years after the entry into the transaction (GPCCA § 99 (2)).

In addition to the restriction based on the reasonableness of the deadline, Estonian law enables the party in breach to transform the notice of termination invalid in case the claim for the performance of the obligation has expired (LOA § 118 (2)). If the other party does not rely on the limitation period, termination is still possible, provided that the material prerequisites for termination exist. Pursuant to the GPCCA's § 146, the limitation period for a claim is, as a rule, three years (under subsection 1) and in exceptional cases it is either five (subsections 2 and 3) or 10 years (subsections 4 and 5) since the time the claim falls due (§ 147).

A notable situation concerns limitations of termination and avoidance of consumer sale contracts. Namely, in the case of consumer sale, the seller is, under § 218 (1) of the LOA, only liable for any lack of conformity of a thing if that non-conformity becomes evident within two years after the thing was delivered to the buyer. It is often the case with cars, home appliances, furniture, etc. that the buyer discovers the lack of conformity only after two years have passed since the receipt of the thing. There arises a question as to whether the buyer may terminate the contract on the basis of the existence of a relevant mistake under § 92 of the GPCCA in the case wherein more than two years have passed since the delivery of the thing but less than three years have elapsed since entry into the transaction<sup>\*79</sup> and the material elements necessary to constitute a mistake are present. Allowing this option would not be contrary to EU law, as, according to Article 8 (1) of the consumer sales directive<sup>\*80</sup>, the rights resulting from the directive are exercised without prejudice to other rights that the consumer may invoke under the national rules. Therefore, if national provisions foresee an alternative for avoiding a contract because of a mistake, such avoidance complies with the directive. The authors of this article consider that such an option should be permissible under Estonian law because avoidance of a contract of sale instead of termination would help — especially in cases like the one described above — to protect the buyers much more effectively, as compared to termination.<sup>\*81</sup>

To summarise, the duration of the option to terminate or avoid a contract of sale are regulated on different terms in Estonian law. Presumably, the reasonable time period for terminating a contract of sale is shorter than the time for avoiding a contract based on a mistake — although exceptions to this rule may be found. The regulation of the length of the period for avoidance on the basis of a mistake is subject to agreement by the contracting parties. However, agreement of parties as to the deadline for the right of termination does not automatically extend to the deadline for exercising the right of avoidance.

## 4. Effects of termination and of avoidance

The main difference between the consequences of termination and avoidance is that in the event of termination, the contract is terminated *ex nunc*, while in case of avoidance the contract becomes void since inception.<sup>\*82</sup> Termination creates a liquidation obligation including mutual reversal obligations (3-2-1-129-05) and, while the contractual obligations are in the main part terminated but not entirely, what clearly expire are the obligations directed at performance.<sup>\*83</sup> Termination normally does not terminate obligations *ex tunc*; instead, what was transferred is returned under a return obligation in compliance with the LOA's §§ 189–191. For instance, the parties will still be liable for the breaches that have occurred to date; agreements related to jurisdiction and arbitration, non-competition, and confidentiality clauses will continue to apply.<sup>\*84</sup> Similar principles can be found in DCFR III.–3:509.

However, with avoidance a contract becomes void; i.e., the legal basis for performing contractual obligations is lost. That which was received on the basis of an avoided transaction is to be returned pursuant to the provisions concerning unjust enrichment (GPCCA § 90 (2), the same in DCFR II.–7:303). Compared with termination, the duty to hand over is somewhat more restricted under the unjust enrichment provisions than those governing termination and only that must be handed over which actually made the recipient richer<sup>\*85</sup>, with, for

<sup>79</sup> Pursuant to GPCCA § 99 (2), a transaction shall not be avoided until after three years have passed from entry into the transaction.

<sup>80</sup> Directive 1999/44/EC of the European Parliament and of the Council of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees. – OJ L 171, 7.07.1999, pp. 0012–0016.

<sup>81</sup> As a marginal note, the authors would like to point out that with consumer sale contracts, the requirement under LOA's § 118 (1) that the buyer must terminate the contract within reasonable time period should not apply. Such a requirement is not included in the directive and the Member States are not allowed to establish consumer-related requirements in their national rules that would be stricter than the terms of the directive.

<sup>82</sup> See also DCFR II.–7:212, Comments, A.

<sup>83</sup> P. Varul *et al.* Law of Obligations Act I (Note 5), p. 624.

<sup>84</sup> *Ibid.*, p. 625.

<sup>85</sup> *Ibid.*, p. 638.

example, his subjective intentions regarding the object of the contract taken into account (LOA § 1033 (1), as in DCFR VII.–6:101). However, in the case of a void mutual contract — including mutual contracts subject to avoidance<sup>86</sup> — one may appeal successfully to the lack of basis for enrichment only in the case where the contract is void because of the restricted active legal capacity of the recipient, or due to threats or violence on the part of the transferor (LOA § 1034 (1)). Thus, in the case of a contract of sale as a mutual contract being avoided on the basis of a mistake, it is not, as a rule, possible to rely on the lack of basis for enrichment and the buyer is required either to return the thing purchased or, if this is not possible, to compensate for the value of the thing, pursuant to the LOA's § 1032 (2). Likewise, the seller cannot rely on, for example, the fact that the money he received has been stolen from him and that thus he is not any richer by that amount. In this respect, the consequences of terminating or avoiding a contract of sale are largely overlapping.

Here the following difference may be observed: in the case of termination by the buyer, it is always possible to demand payment of interest on the transferred funds (LOA § 189 (1), 3<sup>rd</sup> sentence), while in the case of unjust enrichment (i.e., avoidance of the contract), this can be done only if the recipient knew or must have known at the time of transfer that the contract was avoidable (LOA § 1035 (1) and (3) 2), GPCCA § 91). Thus, if the seller was or must have been aware of a relevant mistake on the part of the buyer (GPCCA § 92 (3) 1) or 2)), the buyer has the right to demand payment of legal interest on the refunded money on the basis of the LOA's § 1035 (1) or (3) 2); however, if both parties made a mistake (*ibid.*, clause 3), the buyer does not have that right. But if both parties' fundamental mistake gives rise to termination, the buyer may in any case demand interest on the refunded purchase price, and from this angle it would be more beneficial to the buyer to terminate and not avoid the contract.

Claims for compensation of damage are also different with termination and avoidance. In the case of avoidance, the buyer has just a negative claim for compensation (reliance measure); that is, he may demand to be put in the position he would have been in if he had not entered into the transaction (GPCCA § 101, also DCFR II.–7:304). With termination, however, the buyer has a positive right to claim compensation (expectation measure); i.e., he may demand to be put in the position that he would have had if the contract had been properly performed (LOA § 115, with the same principle being mirrored in DCFR III.–3:509).

To sum up, in cases where the seller is in fundamental breach of contract, as far as the consequences of restitution are concerned, it is somewhat more beneficial for the buyer to terminate and not to avoid the contract. Primarily this holds true to the extent of the buyer's potential claim for compensation and, in part, also to the claim for payment of interest. On the other hand, the buyer should be aware that, with termination, the seller will continue to have the right to make a claim for compensation or contractual penalty against the buyer.

## 5. Conclusions

Having examined possible cases of overlaps of termination and avoidance, it becomes clear that such overlaps are indeed possible. Since the deadlines for giving notice of termination and avoidance are subject to different regulation, the time periods for exercising the two alternative options might not necessarily be identical: although under Estonian law the entitled person normally retains the right of avoidance over a longer period than is seen with termination, the opposite may hold true exceptionally and in view of the facts of specific cases. Also, legal consequences of termination and avoidance are not the same: the two significant differences are that it is not always possible to demand payment of interest on the amounts refunded on the basis of the avoidance and unjust enrichment provisions, although this can be done with termination. In the case of termination, the parties will continue to have to perform certain requirements and obligations arising out of the previous performance of the contract.

Taking into account the general principles of private law — the principles of good faith and private autonomy, including freedom of contract — the authors of this article are not proponents of restricting the freedom of an individual to choose between these two institutions. The regulation provided in the DCFR is generally justified, and in Estonian law as well we should observe the principle that where circumstances of fact arise enabling a person to choose either to terminate or avoid a contract, the person is free to choose the remedy he prefers.

At the same time, the regulation of the deadline for avoidance of contract for mistake should be treated as dispositive, and in this respect the parties may themselves restrict their freedom of choice. If it is not obvious which remedy (termination or avoidance) a person is employing, that person's declaration of intent should be interpreted in the way most favourable to him.

<sup>86</sup> T. Tampuu. *Lepinguväliste võlasuhete õigus* (Non-contractual Obligations Law). Tallinn: Juura 2007, p. 102 (in Estonian).