C.A. 7833/06 Pamesa Ceramica v. Mendelson Ltd.

Judgment by the Israel Supreme Court (Justices Rivlin, Grunis & Rubinstein) delivered on 17 March 2009. Abstract prepared by Arie Reich.

Facts: In 1996, Eisenberger built a building using tiles made by the Appellant Pamesa Ceramica (a Spanish company), imported by Gafni Sadeh, and purchased partially from Gafni and partially from Avnei Gazit. Gafni and Avnei Gazit made an arrangement of some kind under which Gafni assumed any liability that Avnei Gazit might have for the tiles. The Respondent, Mendelson Ltd., later purchased Gafni. In 1998, one of the residents in the building complained about the tiles. Mendelson was willing to contribute to the replacement. Later, it became clear that all the tiles had defects and would need to be replaced and Mendelson refused to accept liability. In 2001, Eisenberger, who was forced to replace all the tiles, filed suit against Mendelson for compensation for costs and damage to reputation; Mendelson sent third-party notice to Pamesa.

The Haifa District Court found Mendelson liable vis a vis the builder Eisenberger and accepted Mendelson's third-party notice against Pamesa. Eisenberger appealed the assessment of damages to reputation and Mendelson and Pamesa appealed the decision finding them liable.

The important questions: Does article 40 of the Sale (International Sales) Law, 5731-1971, apply? Does the Convention permit concurrent claims under tort law or unjust enrichment?

[Since this case occurred before the CISG had entered into force in Israel, the old law based on the 1964 Hague Convention (ULIS) still applied. However, as noted by the Court itself, the relevant provisions of the CISG are in substance identical to the provisions of ULIS, so that the Supreme Court's ruling in this case is equally relevant to the CISG.]

Held: The requirements of examination and notification found in article 38-39 were not met in this case. The subsequent prescription of the buyer's right is binding and substantive. However, article 40 limits the seller's ability to rely on article 39. Article 40 is primarily an application of the principle of good faith, as has been noted in the literature on both ULIS and the CISG and held by various national courts. In addition, art. 40 is based on the rationale that notice under article 39 is unnecessary in this case, since the buyer was already aware of the defect, so that the seller cannot rely on the buyer's failure to notify him about what he already knew. Since article 40 is an exception to articles 38-39, it should be interpreted narrowly and limited to exceptional circumstances. It should also be noted that Israel's domestic Sales Law (art. 16) states that this exception only applies when the buyer gave notice of the defect immediately upon discovery, thus supporting a more narrow interpretation of art. 40.

What mental element is required by article 40? Does the phrase "of which he could not have been unaware" require *de facto* awareness or does it set a normative standard of reasonableness? It seems that the Israeli legislature interpreted the requirement as factual, since in the domestic law it changed the language to include negligence ("should have known"). However, various courts have interpreted the article to imply a normative standard, so that it can be used in cases of negligence or at least gross negligence on the part of the seller in relation to awareness of the defects. In this case, no precise

determination on the required mental element is necessary, since even the broadest interpretation requires *at least* negligence in being unaware of the defect (as is required by the domestic law), which is not met in our case.

Our case does not seem to fall within the narrow scope of the exceptional cases in which art. 40 applies. Pamesa was not aware of the defect in the specific shipment. Secondly, the testimony that implied that they knew of defects in general relies on complaints made after the sale to Mendelson, which means that the transaction was not in bad faith. Thirdly, general awareness that some products are sub-par is not enough to satisfy the requirements of article 40. At the very least, the seller must have had knowledge of past defects *of the type being alleged* in the *same type* of product; perhaps the awareness should even be limited to a certain production line. Since general notice about "problems" in these goods is not sufficient under 39, *a fortiori* general awareness of past problems does not meet the requirements of 40. Further, even if Pamesa was aware of the problems, they cannot be seen as facts that need not be brought to its attention, given the fact that they had passed an examination by the Israel Standard Institution. Thus, Pamesa could not have foreseen that there would be a claim.

Furthermore, article 40 is intended as a 'safety valve' for article 39 and should not be applied when the buyer is aware of the non-conformity for years but does nothing until it is sued by another party. This is supported by the principle of good faith. Article 40 does *not* include an exemption from the duty to give notice- it creates only an *estoppel*, preventing the seller from relying on the failure to give notice. In conclusion, article 40 cannot apply in this case, which means that the suit is barred under article 39. (The court also questioned whether non-conformity of the tiles had in fact been proven, or perhaps the problems with the tiles were due to improper use or installation, but did not make any finding in this regard.)

Does this preclude the concurrent application of tort law or the law of unjust enrichment? In other words, was the Uniform Sales Law convention intended to replace only sale/contract law or to handle all legal claims arising from an international sale contract? ULIS Article 8 (as well as CISG Art. 4) limits the Law's application to obligations arising from a contract of sale.

It is clear, however, that the purpose of the convention- to achieve uniform international law- is frustrated by allowing tort claims under domestic law. Regarding the CISG, there are two schools of thought. Under the narrow approach, if the elements of the claim under domestic law are similar to the elements under the CISG, domestic law does not apply. In our case, the non-conformity of the tiles is the basis for both claims, so the CISG cannot be circumvented. Under the broad approach (Schlechtriem), a concurrent claim is possible when three conditions are met:

1. The grounds for the remedy cannot fall within the scope of the CISG;

2. To grant such a remedy does not conflict with the goals of the CISG, and

3. The domestic law permits concurrent assertion of the remedy.

The courts will be more lenient when the damages are less related to the sale contract (e.g. property damage caused by the defect goods).

However, the Hague Convention has a special provision (not paralleled by the CISG) that seems to preclude any concurrent tort action – namely art. 34. Nevertheless, the Supreme Court concludes that the proper interpretation of this provision, as has been written by several commentators, is that it excludes only contractual claims. In Israeli domestic law, the same question has arisen regarding the relationship between the (domestic) Sales Law and other laws. In *Solondz*, the District Court did not permit concurrent application, which has led to criticism in the literature. The Court holds that when interpreting the convention, due attention should be given to its international nature and to the need to promote interpretative uniformity among its signatories.

In our case, the court allows consideration of a tort claim for negligence in manufacture, since the protected interests are not identical. Firstly, the negligence relates to violation of general duties of manufacturers, not duties created by the contract. Secondly, the Convention applies to the obligations of a seller, while the negligence relates to the duties of a manufacturer. Thirdly, the tort claim requires proof of negligence, whereas the contractual claim is based on strict liability. Indeed, in this case, although tort claim was permitted, the Supreme Court held that Mendelson had not proven negligence by Pamesa, and thus the claim on this account was dismissed.