Seller’s liability in respect of defect of a ‘specific’ property

Defect

- Thing sold must have the quality or performance ordinarily expected given the nature of the sale and intent of the parties.
- Prevalent technology, reasonable economic expectations will also be taken into account.
- Seller’s representations & warranties (regarding the nature, quality, suitability of the thing sold) must be taken into account.
- Applicable only to ‘hidden’ defect (Art. 580(1)):
    - If the buyer had actual knowledge of the defect, then it must surely have been reflected in the price.
    - If the defect is patent enough that a reasonable buyer should have known it, then no need to protect the careless negotiator.
    - Seller has the burden of showing that the buyer knew or should have known the defect.
    - Suppose the seller knew the defect and the buyer negligently overlooked. What if the seller (i) kept quiet about the defect? (ii) deliberately misled the buyer?

- 98Da18506: A plot of land was sold as suitable for building dwelling houses. Buyer decided to build apartments instead and applied for planning permission, which was refused. The court held that inability to obtain the planning permission for building dwelling

houses (as the buyer intimated at the time of the sale) would have constituted ‘defect’ under Art. 580. In this case, however, the buyer changed the plan and applied for building apartments. The plot cannot be viewed as defective at the time of the contract.

- 84Daka2525: A taxi was sold as suitable for commercial operation. It turned out that the taxi was subject to an administrative order banning it from commercial operation for 150 days. Defect under Art. 580.

Remedies

- Unavailable if the sale was concluded in an ‘official’ auction. Art. 580(2) Caveat emptor!
- Reduction of price:
  - Art 575(1) only refers to ‘damage’. But it should be interpreted to mean ‘reduction of price’.
  - the difference between the market value of the defective thing (assuming that the defect is known) and the contract price (which was reached without knowledge of the defect)?
  - the ‘objective’ worth of the defect must be subtracted from the contract price: *quanto minoris essem empturus, si id ita esse scissem,* Dig.19.1.13pr. If the defect was known to the buyer, what the parties would have agreed as the contract price (reflecting their respective bargaining skills and bargaining power). “Where a portion of contractual obligation is impossible to perform from the beginning, the price reduction remedy purports to adjust the contract price in order to maintain the parity of bargain (□□□□ □□□□ □ □□□□ □□□□ □□)” (92Da30580)
  - [Doubtful!]The amount which would put the buyer in the same position as that in which he would have been if there was no defect: performance measure

of damage?
    - The assumption is that the buyer would have paid less if the defect had been known to him (in the event, buyer paid more believing that there was no defect).

- Termination: If the defect is serious enough to defeat the purpose of the contract
- Regardless of whether warranty remedies are available or not, rescission on the ground of mistake is also available separately (assuming that the requirements for rescission are met). 2015Da78703
- **Available for 6 months** from learning the defect. Art. 582
    - 2003Da20190: Grains for shiitake mushroom were sold. The germination rate turned out to be very low (less than 1/100 of ordinary shiitake mushroom germs). Buyer may have remedies under Art. 580 for 6 months from the moment when the buyer learned that the unusually low rate of germination was due to the grains themselves, rather than some other reasons. (Can the buyer have NO remedy after 6 months? Is the seller in 'breach of contract'? Has the buyer not 'performed' as agreed (to deliver the 'specific' good)?)

- Commercial Code, Art 69: Where **both** parties are merchants,
    - the purchaser has an obligation to "immediately inspect and, if a defect is found, immediately notify the seller". So Article 582 of the Civil Code does not apply.
    - where the defect is not immediately discoverable, the purchaser has 6 months to discover the defect.
    - What about a defect which was not discovered and was not discoverable within 6 months and which

only emerges after more than 6 months? (98Da1584 ruled “no remedy under the Commercial Code”. Confirmed by 2013Da522, where it is ruled that no warranty liability exists, but ruled that a breach of contract remedy is available)

- If parties agree upon a warranty period, the court interprets that Art 69 of CommCode is excluded by consent (2008Da3671).
- Regarding extended loss, the court rules that a breach of contract remedy is available. 2013Da522 (A plot of land was sold. The soil turned out to be contaminated. Buyer successfully claimed decontamination costs from the seller although the defect was discovered well after 6 months.)
- 86Daka2446: Packaging material supply contract. The court ruled that it is not a sale contract (as the design of the packaging is “tailered” to the purchaser. CommCode 69 not applied.

- Extended loss: not recoverable under Art. 580.
  - 2002Da35676: Air conditioner was fitted to a green house which was used for cultivating roses. The motor of the air conditioner (which was installed next to a fuel-operated boiler 유리온실 내 기름보일러 방면에서 첫 번째로 설치된 농업용 공기조화기(이하 ‘이 사건 공기조화기’라 한다)의 모터 과열로 그 권선의 절연이 파괴) overheated and caused fire. The entirety of the green house burned down. Seller found to be “not at fault”. (the fire damage was not caused by any fault in the delivery and fitting of the air conditioner. “화재가 이 사건 공기조화기의 인도 및 설치 그 자체의 잘못으로 인하여 발생하였다고 할 수 없으므로,…”)
  - 96Da39455: A burner stopped in the middle of a cold night in winter. The green house which was used for cultivation of flowers was left without any heating for several hours. The flowers perished. The seller/manufacturer of the burner

settled with the farmers. Seller of silicone coupling which was used in manufacturing the burner was sued by the manufacturer of burner as it turned out that the coupling became brittle in low temperature and failed to function properly. (But can the silicone coupling, in this case, be said to be ‘defective’?)

- In order to seek compensation for extended loss, buyer must allege breach of contract and prove breach, causation and foreseeability. The seller may plead ‘no fault’. Art. 390, 393.
    - 89Daka15298: Potato seed was found to have been defective. The harvest was very poor. Damage (for breach of contract) must be calculated by working out the difference between the expected income from normal harvest and the actual income from the poor harvest caused by the defective potato seeds.

- 2002Da51586: Seller buried a substantial quantity of rubbish before selling the land. Buyer entitled to claim damage in respect of the costs of removal and disposal of the rubbish. This claim is available concurrently with Art 580 (which refers to 575(1)) remedy. It is available even after 6 months of discovering the ‘defect’. Extended loss. The costs of removal and decontamination (which exceeded the sale price) were awarded as damage.

Acceptance of goods & buyer’s due diligence

- Seoul Appellate Court: (2014Na2007931): “due diligence is the purchaser’s right. It is not an obligation. As it has to be conducted only during a limited period, on the

basis of limited materials and about matters whose scope is limited, there is no ground to impose on the purchaser a duty to uncover the true circumstances. Also, if we are to deny the purchaser's claim for damage against the seller by attributing knowledge or negligence to the purchaser merely because an extremely small amount of materials relevant to the seller's representations and warranties were included in the vast amount of disclosure materials offered for due diligence, then due diligence would actually be disadvantageous for the purchaser. This would lead to a strange conclusion that a reasonable purchaser would rather forego due diligence because he would be better off without it."

[Questions]

1. Seller sold a company with a warranty that the company's financial statements are accurate. Buyer calculated the acquisition price on the basis of the company's financial statements, applying EV/EBITDA multiple. After the closing, the financial statements turned out to be inaccurate (inflating the earnings by 10%).
2. Specific pieces of timber to be used in building houses were sold. It turned out that the timber was weakened by termites. The house collapsed as a result.
3. A sold to B a used notebook computer to be at 100USD. Unknown to A and B, wifi card was already damaged at the time of the sale. After the notebook computer was delivered, B spilt coffee over the keyboard. As a result, Ctrl and Alt keys on the right-hand side are not working.