THIRTEENTH ANNUAL
WILLEM C. VIS INTERNATIONAL COMMERCIAL ARBITRATION MOOT

MEMORANDUM FOR CLAIMANT

ON BEHALF OF:
OCEANIA PRINTERS S.A.
TEA TRADER HOUSE
OLD TIMES SQUARE
MAGRETON
00178 OCEANIA

CLAIMANT

AGAINST:
MCHINERY EQUIPMENT SUPPLIERS PTY
THE TRAMSHED
BREAKERS LANE
WESTERIA CITY 1423
MEDITERRANEO

RESPONDENT

Faculty of Law, McGill University

BRAM DOV ABRAMSON · DAVID DUBROVSKY · SHUBHA RAJALAKSHMI KRISHNAN · ALEKS ZIVANOVIC

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CIDRA Rules	Rules of the Chicago International Dispute Resolution Association, July 2005 (Cited as: **CIDRA Rules**)
CISG	United Nations Convention on Contract for the International Sale of Goods, 1980 (Cited as: **CISG**)
Hague Convention	Hague Convention on the Law Applicable to Contract for the International Sale of Goods, October 1985 (Cited as: **Hague Convention**)
Limitation Convention	Limitation Convention on the International Sale of Goods, June 1974 (Cited as: **Limitation Convention**)
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Factual Context

1. Oceania Printers S.A. (hereinafter the "Claimant") is a printing firm based in Magreton, Oceania. McHinery Equipment Suppliers Pty (hereinafter the "Respondent") is a seller of new and used industrial equipment, including printing machines, based in Westeria City, Mediterraneo.

2. The Claimant contacted the Respondent on 17 April 2002 to express its interest in purchasing a refurbished flexoprint machine that would meet certain operational capabilities, including the ability to print on aluminium foil which may be of 8 micrometer thickness. The machine was intended to service a lucrative contract which would require the Claimant to print foil confectionary wrappers. The Respondent recommended a refurbished flexoprint machine to meet the Claimant's needs.

3. When the parties concluded a contract for the supply of the flexoprint machine on 30 May 2002, the Respondent was aware of the confectionary contract, of its lucrative implications, and of the Claimant's particular purpose of printing 8 micrometer foil confectionary wrappers. The flexoprint machine recommended by the Respondent arrived in Oceania and was installed and refurbished by 8 July 2002. Once the set-up had been completed, it immediately became apparent that the machine was not capable of printing on 8 micrometer foil. The Respondent's attempts to modify the machine were unsuccessful. As a result, the Claimant lost its lucrative confectionary contract with Oceania Confectionaries.

4. The Claimant notified the Respondent of its intention to claim compensation for the cost of the flexoprint machine, expenses relating to the installation of the flexoprint machine, and for the significant loss of profits resulting from the loss of the Oceania Confectionaries contract. The parties attempted to reach a negotiated settlement to their contractual dispute for over two and a half years. On 27 June 2005, the Claimant commenced international arbitration proceedings against the Respondent with the Chicago International Dispute Resolution Association (hereinafter "CIDRA"), pursuant to clause 13 of the parties' contract. CIDRA acknowledged receipt of the Claimant's request on 5 July 2005, less than three years after the claim first accrued.

5. In Procedural Order No. 1, the Tribunal requested that the parties discuss whether the period of limitation expired prior to the commencement of the arbitration, and the appropriate rule

of choice of law that the Tribunal should follow under Art. 32 of CIDRA; whether the Respondent failed to perform any of its obligations under the contract and the CISG; and whether the claim for lost profits was appropriately calculated.

6. The Claimant respectfully submits that:

a. The Respondent breached its contract with the Claimant by delivering non-conforming goods under Art. 35 CISG;

b. the Claimant's damages amount to $2,756,117; and

c. the Claimant commenced proceedings within the applicable limitation period.

Arguments

A. The Respondent Breached its Contract With the Claimant By Delivering Non-Conforming Goods Under Art. 35 CISG

1. The Respondent Delivered a Machine Which Did Not Conform to the Particular Purpose Contracted For

7. The Claimant and the Respondent subjected their contract to the UN Convention on the International Sale of Goods (hereinafter "CISG") (Claimant's Exhibit No. 7 para.12). Under Art. 35(1) CISG, the seller must deliver goods which are "*of the quantity, quality and description required by the contract.*" Art. 35(2) CISG provides the mechanism by which goods' conformity to this requirement of quality is evaluated "*[e]xcept where the parties have agreed otherwise*." Neither party proposed to contract out of this mechanism, so the Respondent was bound to deliver goods whose quality conformed to the contract under all four branches of Art. 35(2) CISG. Among these is the requirement that the goods be "*fit for any particular purpose expressly or impliedly made known to the seller at the time of the conclusion of the contract*" (Art. 35(2)(b) CISG). It is the Claimant's position that its particular purpose was expressly or impliedly made known to the Respondent, as discussed in paras. 8-12. Further, the machine delivered by the Respondent did not conform to that particular purpose, as discussed in paras. 13-14. This is prima facie evidence that the Respondent breached its contractual obligations under Art. 35 CISG.

1.1. The Particular Purpose was Expressly or Impliedly Made Known to the Respondent

8. The interpretive principles set out in Art. 8 CISG are relevant to determining whether a particular purpose has been communicated under Art. 35(2)(b) CISG (*SARL Bri Production* "*Bonaventure*" *v. Societé Pan African Export (France 1996)*). Art. 8 CISG provides two ways to determine the terms of a contract. Art. 8(1) CISG provides a *subjective* test: one party's "*statements … and other conduct … are to be interpreted according to his intent[,] where the other party knew or could not have been unaware what that intent was*." Where Art. 8(1) CISG does not settle the issue, Art. 8(2) CISG provides an *objective* test: "*statements 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.*"

9. The Claimant made its subjective intention clear in its initial letter to the Respondent (Claimant's Exhibit No. 1): it sought to service a specific type of contract which required that it be able to print on confectionary foil which may be 8 micrometers in thickness. The Claimant did not know precisely which model of machine it needed, but was nonetheless particular and explicit about its functional specifications. With respect to the model it required, the Claimant merely indicated that it sought a "*six colour machine with a varnishing stand.*" With respect to the machine's functional specifications, however, the Claimant was very explicit: it specified the finish ("*coated and uncoated papers*") and types ("*wrapping, polyester and also metallic foils*") of materials on which it would print, the industry it would be servicing ("*the confectionary market and similar fields*"), and the thickness required in that industry ("*[t]ypical …. foil for chocolate wrappers may be of 8 micrometer thickness*"). The Claimant placed additional and particular emphasis on foil products: "*[t]here is no other flexoprint operator in Oceania,*" with the result that "*users of foil products in particular have to import the printed products, which is expensive*" (Claimant's Exhibit No. 1).

10. The Claimant identified only one *technical* specification—8 micrometers thickness, and only one industry—the confectionary industry. The Claimant's letter proceeded to link this specification and this particular industry with its ultimate intention, which was to acquire a specific type of capacity in order to reap the benefits of an import-substitution strategy. Applying Art. 8(1) CISG to the letter's structure, it is reasonable to infer such an intention.

At the very least, the Respondent could not have been unaware that the ability to print on foil products of 8 micrometer thickness for use in the confectionary industry was significant to the Claimant's inquiry. Objectively, no reasonable party could conclude otherwise from the Claimant's initial letter.

11. Notice of a particular purpose is effective even if the particular purpose is impliedly rather than expressly identified (*Enderlein & Maskow, Art. 35 para.11; Schlechtriem-Schwenzer, Art. 35; Rheinland Versicherungen v. S.r.l. Atlarex and Allianz Subalpina S.p.A. (Italy 2000)*). Clear communication of a possible use, and the absence of any disavowal of that possibility, are enough to make a buyer's purpose known to the seller. A good example of this is when a buyer of light-bulbs for an advertising display communicated to the seller that the bulbs *might* be used beyond the lifetime of that advertising display. A German court held that the buyer's failure to disavow that intention and the seller's failure to dispel it were sufficient to render the longer lifetime a term of the contract (*LG München 5HKO 3936/00 (Germany)*). This interpretation is consistent with the stipulation in Art. 35(2)(b) CISG that goods "*be fit for <u>any</u> particular purpose … made known to the seller*" (emphasis added). It is therefore not enough to argue that that a purpose communicated expressly is a "*a rather vague formulation*" (Respondent's Answer, para.25).

12. The Claimant continued to clarify its intention in its letter of 10 May 2002 (Claimant's Exhibit No. 3), confirming that "*[w]e signed a contract with Oceania Confectionaries.*" The Claimant's intent was by now evident. It sought to acquire a machine for the particular purpose of printing confectionary foil. It had stated explicitly that such printing may typically be 8 micrometers in thickness. At no time did it or the Respondent disavow or propose alternatives to that specification (see also discussion at paragraph 30 below). The Claimant's written communication of 10 May 2002 provided no new information that would have allowed a reasonable person to form a different opinion. It reinforced the particular purpose of the flexoprint machine that the Claimant sought to acquire: the ability to print on confectionary foil, where the only thickness stipulated for confectionary foil printing had been 8 micrometers.

1.2. The Respondent's Goods Did Not Conform to the Particular Purpose Made Known to It

13. The Claimant "*made known to the seller*" the fact that the machine contracted for was intended for the "*particular purpose*" (Art. 35(2)(b) CISG) of printing on "*foil for chocolate wrappers [which] may be of 8 micrometer thickness*" (Claimant's Exhibit No. 1). In order for the flexoprint machine delivered to conform to the "*quality … required by the contract*" (Arts. 35(1) & 35(2)(b) CISG), it therefore had to conform to "*any particular purpose*" which the buyer intended, that being the ability to print on confectionary foil which may be of 8 micrometers in thickness.

14. The flexoprint machine delivered by the Respondent did not conform to this particular purpose. After setting up, refurbishing, testing, and adjusting the machine at the Claimant's premises, the Respondent's staff turned the machine over to the Claimant, who immediately began production runs to test the machine. It became immediately obvious that the machine "*wouldn't print properly*" on confectionary foils of 8 micrometers in thickness (Respondent's Exhibit No. 2). As the Respondent explained to the Claimant's foreman on 8 July 2002, and as the Respondent subsequently reiterated in a letter to the Claimant on 1 August 2002, the flexoprint machine did "*not [work] on the foil products for confectionary wrapping. The machine creases the foil and tears it, and multiple color runs on foil are badly out of register*" (Respondent's Exhibit No. 2, Claimant's Exhibit No. 9).

2. The Claimant Reasonably Relied on the Respondent's Skill and Judgment

15. When goods do not meet "*any particular purpose … made known to the seller*," the goods will be found to be non-conforming under Art. 35(2)(b) CISG unless the seller demonstrates that either of two exculpatory tests have been met. The first of these is set out in Art. 35(2)(b) CISG, under which the seller is not liable where "*circumstances show that the buyer did not rely, or that it was unreasonable for him to rely, on the seller's skill and judgement.*" In this case the Claimant did rely on the Respondent's skill and judgement since it was reasonable under the circumstances to do so. Nothing in the latter's communications or conduct would have rendered such reliance unreasonable.

16. The Respondent professed to have sufficient expertise to render the Claimant's reliance on it reasonable. The Respondent had the necessary expertise to promise to "*re-erect [the*

flexoprint machine] on [the Claimant's] premises and refurbish anything that required it" (Claimant's Exhibit No. 4). The Respondent retained staff with sufficient expertise to know that 8 micrometer foil was "*thinner material than [the machine] was designed for*" and familiar enough with its design to attempt to "*adjust the machine*" to accommodate the Claimant's purpose (Respondent's Exhibit No. 2). That the Respondent dealt in industrial equipment generally and not flexoprint machines or even Magiprint Printers exclusively or predominantly is therefore not sufficient to find that it had inadequate expertise, nor that reliance on this expertise was unreasonable.

17. Secretariat Commentary on Art. 35(2)(b) CISG, for instance, illustrates the situation in which "*the buyer had not relied on the seller's skill and judgement*" through scenarios where "*the buyer selected the goods by brand name or that he described the goods desired in terms of highly technical specifications*." Yet, even in such a scenario, the "*requirement of the observance of good faith*" (Art. 7 CISG) would indicate that, "*[i]f the seller knew that the goods ordered by the buyer would not be satisfactory for the particular purpose for which they have been ordered[,] it would seem that he would have to disclose this fact to the buyer.*" Here the onus on the Respondent was even higher. The Claimant clearly relied on the Respondent's skill and judgement since the Claimant did not select the goods by brand name—the Respondent did, by putting the brand name forward in response to the practical considerations expressed by the Claimant. No disclosure of non-conformity was provided by the Respondent. A lack of expertise would therefore have to be evident from the facts, either because "*the seller did not purport to have any special knowledge in respect of the goods in question*" (*Secretariat Commentary*), or because the seller rebutted any presumption of such knowledge by informing the buyer that, for instance, he is a mere intermediary (*Kruisinga p.33*).

18. The Respondent did purport to have special knowledge and it did not rebut that presumption once created. Indeed, in this case, it was the opposite of a disclaimer: the Respondent neither hesitated nor took caution in making a recommendation to the Claimant. In response to Claimant's inquiry referring to "*the confectionary market*," foil which "*may be of 8 micrometer thickness*," and expensive imports of "*foil products*" (Claimant's Exhibit No. 1), Respondent stated explicitly that it had "*a machine for your task*." On 27 May 2002, in the Respondent's final communication to the Claimant prior to installation, the Respondent asserted that "*[y]ou can be assured that with this machine you will be able to meet <u>all</u> the*

needs of your customers.” The Respondent was by now well aware from the Claimant’s letter of 10 May 2002 that the Claimant’s *only* customer was “*the Oceania Confectionaries account that makes the flexoprint machine worthwhile*” (Claimant’s Exhibits Nos. 6 and 3, emphasis added).

19. Any residual presumption under which “*[i]f the buyer uses the goods himself in his factory, he may well be better informed than a seller who is a trader and not a producer*” (*Enderlein p.157*) was similarly dispelled by the Claimant’s stipulation of a particular purpose and the Respondent’s naming of a particular brand of machine to fit that purpose. The burden of skill and judgement is plain. There was no other machine of this type in Oceania, while the Respondent had experienced engineers on hand—the Respondent had demonstrably more expertise than the Claimant. The Claimant’s customer’s requirements were made known to the Respondent and the Respondent twice expressed certainty that the machine in question was the right machine for the Claimant’s customers. Given the Respondent’s familiarity with the Claimant’s purpose at the time of that assertion, that assertion was an “*implied warranty for a particular purpose*” (*DiMatteo et al. p.396*).

20. At no time was the Respondent discharged from its general obligation as seller to counsel the buyer (*Enderlein p.157*). On the contrary, the Respondent’s representations could only be reasonably understood as efforts to meet that obligation by stipulating a particular model to fit the “*particular purpose expressly or impliedly made known to the seller*” (Art. 35(2)(b) CISG). This interpretation is strengthened by the fact that the implied warranty was made only after the Claimant had confirmed the nature of the confectionary contract and pledged to “*put in place a Letter of Credit*” to order the machine whose model and make the Respondent had stipulated (Claimant’s Exhibits Nos. 5 and 2).

3. The Claimant Was Not and Could Not Have Been Aware of the Lack of Conformity

21. The Respondent seeks to excuse the non-conformity of its machine by relying on the exculpatory test set out in Art. 35(3) CISG, arguing that the Claimant “*knew or could not have been unaware of such lack of conformity*” based on two alleged opportunities for discovery. The first such opportunity was the Respondent-arranged visit to the previous owner’s site in Athens. The second was the Respondent’s enclosure of the manual with the printed contract it forwarded to the Claimant.

22. International doctrinal authors mirror their domestic counterparts in their lack of agreement on "*the criteria by which the buyer's supposed knowledge is to be determined*" (*Folsom et al. p.88, cited in Secretariat Commentary on Art. 35 CISG; Enderlein p.159*). Case law, however, suggests that a high burden of proof rests on the seller (*OLG Köln 22 U 4/96 (Germany 1996)*): a buyer who is aware of non-conforming aspects of a good, for instance, may nonetheless have validly "*counted on the seller's expertise*" (*EP S.A. v. FP Oy (Finland 1998)*). Even those interpretations most burdensome to the buyer nonetheless require that the defect be "*clearly recognizable*" and "*obvious to the average buyer*," being "*facts that are before the eyes of one who can see*" (*Welser p.109, cited in Enderlein & Maskow p.148; Honnold p.308; all cited in Secretariat Commentary, Art. 35 CISG*). A single two-pronged test will therefore oust the exculpatory provisions at Art. 35(3) CISG. First, it is necessary that the buyer had a reasonable opportunity to discover the non-conformity. Second, it is necessary that a buyer with such opportunities could not reasonably have been unaware of the lack of conformity.

3.1. The Purpose of the Athens Trip Was a Visual Inspection of a Specimen Printer

23. The Claimant's first alleged opportunity to inspect the goods arose out of its visit to Athens on 6-7 May 2002. This Respondent's invitation to "*visit the works of the former owners*," sent on 25 April 2002 (Claimant's Exhibit No. 2), asserted that "*[w]e have indeed a second hand flexoprint machine for your task*." This assertion was in direct response to the Claimant's communication of its particular purpose (Claimant's Exhibit No. 1). In doing so, the Respondent recommended a *class* of printers appropriate to the Claimant's purpose. The only reasonable interpretation of the purpose of the trip to Athens was that it served as an opportunity for the Claimant to inspect a *specimen* of the class of printers recommended by the Respondent—not to determine if the class of printers was the right one for the task.

24. Because the flexoprint machine to be inspected was a used printer, it was to be expected that the Claimant would use this trip as an opportunity to ascertain the physical condition and good working order of the specimen printer. The Claimant was already relying on the Respondent's recommendation as to the class of printer required for its particular purpose, which in turn had already been communicated to the Respondent. No reasonable buyer in the Claimant's position could assume that a seller would arrange a trip to inspect a specimen

machine that was not capable of meeting the buyer's expressly-indicated needs in the first place. To do so would be a considerable waste of both the Claimant's and the Respondent's resources.

25. Moreover, because the used machine to be inspected was "*not yet ... dismantled ... for refurbishment*" (Claimant's Exhibit No. 2), the physical condition and good working order of the specimen were all that a reasonable buyer could seek to determine through such an inspection. Even with the Respondent's staff working diligently and in full cognizance of the Claimant's need to move things along "*quickly*" (Claimant's Exhibit No. 6), it took at least seven days between the Respondent's staff's arrival in Oceania, refurbishment of the Magiprint Flexometix, and initial test run as of 1 July 2002 (Claimant's Exhibit No. 8), and the "*final adjustments*" which allowed the staff to feel comfortable in "*[turning] over the machine to Mr. Butter [of the Claimant] on 8 July 2002*" (Respondent's Exhibit No. 2). The visit to Athens was not intended to allow for such a week-long refurbishment, test run, and adjustment period. Given the trip's duration and circumstances, its purpose was merely to allow for visual inspection of a used specimen printer of the class recommended by the Respondent.

26. It is therefore unsurprising that the Claimant would state that the machine "*looked to be just what we need*" (Claimant's Exhibit No. 3). The statement confirmed that the specimen machine had passed the visual inspection test, meeting the Respondent's duty under Art. 35(3) CISG to note any defect which is "*clearly recognizable*" and "*before the eyes of one who can see*" (cited above, para.22). The class of machine had already been recommended for the Claimant's particular purpose when the Respondent explicitly advised that such a machine was suitable "*for your task*" (Claimant's Exhibit No. 2). The fact that the manual was neither sought nor offered during the visit, nor were technical specifications queried or volunteered, only demonstrates the depth of this common understanding. Both parties behaved as if the purpose of the visit was a visual inspection of physical condition and working order. Neither party can now claim that the purpose of the visit was in fact an inquiry into the class of printer's technical performance characteristics. Such an inquiry would have been inconsistent with the length of the visit, the conduct of the parties, and their prior and subsequent statements.

3.2. The Manner and Timing of the Manual's Introduction Provided No Reasonable Opportunity to Discover the Lack of Conformity

27. The Respondent argues that the Claimant's failure to consult the manufacturer's manual excuses it from liability under Art. 35(3) CISG (Respondent's Answer, para.13). Yet the circumstances surrounding the receipt of the manual do not reveal a reasonable opportunity to discover the lack of conformity. Both the manner of the manual's introduction, and the point in the transaction at which this introduction took place, indicate that the manual provided the Claimant no reasonable opportunity to discover the non-conformity.

28. The terms and conditions of a contract are to be understood giving "*due consideration ... to <u>all</u> relevant circumstances of the case including the negotiations*" (Art. 8(3) CISG, emphasis added; *Lookofsky 56*). In this case, no manual was mentioned until 27 May 2002 (Claimant's Exhibit No. 6), well after negotiations were essentially concluded; by this point the Claimant had placed an "*Order*" and gave notice that it was "*put[ting] in place a Letter of Credit*" (Claimant's Exhibit No. 5). Even at this very advanced stage, the Respondent mentioned the manual only in the context of a faxed letter which first assured the Claimant that "*[y]ou can be assured that with this machine you will be able to meet all the needs of your customers*," and furthermore urged the Claimant to "*sign and send [the document] to me immediately so that the machine can be sent to you quickly*" (Claimant's Exhibit No. 6). The Respondent's exhortation to act quickly to ensure prompt delivery demonstrates the Respondent's awareness of both the urgency of the Claimant's task and the settled status of the negotiations. Only later in the letter is the Claimant told to expect a manual by post, and then only in the tone of an afterthought: "*[e]ven though the machine is easy to operate and is a very reliable machine, you will certainly wish to have a copy.*" The Respondent neither draws the Claimant's attention to the machine's technical specifications, nor gives it any reason to carefully inspect the manual prior to signing. On the contrary, the Respondent creates the distinct impression that delivery of the manual is a mere formality in the process of fulfilling its obligations.

29. To assert that the Claimant's receipt of the manual provided a reasonable opportunity for discovery of non-conformity is therefore puzzling. As has been discussed, the Claimant's initial reliance on the Respondent was formed after the Claimant's inquiry made specific reference to foil, confectionary printing, and 8 micrometer thickness (Claimant's Exhibit No. 1), and the Respondent replied that it had a machine "*for your task*" (Claimant's Exhibit No.

2). A subsequent visit to inspect a specimen printer neither dispelled this reasonable reliance nor provided the Claimant with a reasonable opportunity to discover the non-conformity. When the Claimant volunteered specific information that the now-signed confectionary contract was the "*only … account that makes the flexoprint machine worthwhile*" and that a specimen of that machine "*looked to be*" fit (Claimant's Exhibit No. 3), the Respondent replied with a warranty that "*[y]ou can be assured that with this machine you will be able to meet all the needs of your customers*" (Claimant's Exhibit No. 6). When the Claimant expressed concern about getting the machine in time to service its confectionary contract (Claimant's Exhibit 3), the Respondent replied by offering to deliver the printer faster and reduced the price by the cost of one shipment (Claimant's Exhibit No. 4). In this context the Respondent's statements on 27 May 2002 have an amplified effect. The casual mention of the manual came after negotiations had essentially been concluded, at the last possible moment, and was worded to create the impression that its forwarding was a mere formality accompanying other formalities. This emphasized that the transaction was a done deal pending speedy return of the signed contract. In these circumstances a reasonable buyer, pressed for time and comforted by assurances, could not be alerted by the mere presence of the manual. The manual's presentation and timing were in the manner of an afterthought, something to receive and file should it ever be needed. This is exactly what the Claimant did.

30. To argue that the parties' negotiations are erased by a last-minute gambit to ensure that the Claimant "*had a copy of the manufacturer's manual in its possession*" (Respondent's Answer at para.25), notwithstanding the circumstances outlined here, is to argue "*last-shot*" or "*parol evidence*" doctrines, neither of which is convincing. The last-shot doctrine's availability as a battle of the forms rule under the CISG is controversial at best (*DiMatteo et al. p.355, citing Gabriel; rejected in UNIDROIT 2.22, 2-207(3) UCC, and 2:209 PECL*) and may in any case be applied only to a new offer made by the offeree (Art. 19 CISG) and not, as is the case here, the offeror. The parol evidence rule barring any oral statement contrary to an understanding memorialized in writing is similarly difficult to reconcile with express CISG provisions to the contrary (Arts. 8(3) & 11 CISG), leading "*most Convention commentators [to argue] that the 'parol evidence' rule … is not compatible with the CISG*" (*Lookofsky p.55*; *Lookofsky on Damages p.56; Mitchell Aircraft Spares v. European Aircraft Service (U.S.); MCC-Marble Ceramic Center v. Ceramica Nuova D'Agostino (U.S.)*).

B. The Claimant's Damages Amount to $2,756,117

1. The Claimant Met its Duty to Mitigate Losses Under Art. 77 CISG

31. The Claimant "*loses the right to rely on a lack of conformity of the goods if he does not give notice to the seller specifying the nature of the lack of conformity within a reasonable amount of time after he has discovered it*" (Art. 39(1) CISG). In addition "*a party who relies on a breach of contract must take such measures as are reasonable in the circumstances to mitigate the loss, including loss of profit, resulting from the breach. If he fails to take such measures, the party in breach may claim a reduction in the damages in the amount by which the loss should have been mitigated.*" (Art. 77 CISG). The Claimant discovered the breach on 8 July 2002, after the delivery, refurbishment, setup and testing of the machine had been completed (Respondent's Answer para.10 & Respondent's Exhibit No. 2). The Respondent was notified immediately, as discussed in paras. 32-33, and the Claimant took all measures to mitigate losses that were reasonable in the circumstances, as discussed in para. 34. This was one week before the Claimant was due to start production for the Oceania Confectionaries account, as discussed in para. 35-37. Therefore, no reduction in damages can be claimed by the Respondent.

1.1. The Claimant Provided Prompt Notice of the Non-Conformity

32. The Respondent did not hand over the machine to the Claimant for use until 8 July 2002. The Claimant could not have been aware of the breach earlier, because the Respondent's workmen were still labouring to ready it for its new use. This was therefore the earliest practicable moment at which the Claimant could discover that the machine did not conform to the contract. The Claimant immediately tested it with 8 micrometer foil, discovered that it would not meet its particular purpose as delivered and installed, and immediately informed the Respondent's representatives that it did not conform to the contract.

33. The Claimant approached the Respondent's representative on the very day the Respondent turned over the machine for use, issued notice specifying the nature of the lack of conformity—its inability to print on 8 micrometer foil—and demanded that the Respondent cure the defect immediately. That prompt action discharged Claimant's responsibility to give notice within a reasonable period under Art. 39(1) CISG; the Respondent does not dispute this notification (Respondent's Exhibit No. 2).

1.2. The Claimant Granted the Respondent Reasonable Time to Cure the Non-Conformity

34. Its prompt notice to the Respondent was only the Claimant's first attempt to mitigate its losses caused by the delivery of a non-conforming machine. The Claimant then granted the Respondent 17 days (15 July to 1 August 2002) to cure the non-conformity before providing a second notice of non-conformity in a letter to the Respondent's head office (Claimant's Exhibit No. 9). The Claimant then granted a further 14 days for the Respondent's representatives to cure the non-conformity before informing the Respondent that the contract with Oceania Confectionaries was cancelled and the machine was now of no use to it. (Claimant's Exhibit No. 10). The Claimant's allowances for non-conforming delivery were more than adequate. A German court found that a buyer who granted an 11-day extension to deliver all components of a printing machine had acted reasonably (*OLG Celle 20 U 76/94 (Germany 1995)*). In this case, the Claimant granted thirty-one days. This period may have been enough time for the Respondent to procure and deliver a replacement machine had it reacted immediately, but there is no evidence that this option was considered. On the other hand, it is clear from the facts that this was not an option available to the Claimant.

1.3. There Was No Other Way for the Claimant to Mitigate Losses Under the Circumstances

35. The Claimant had no other way to mitigate. As early as 8 July 2002, the date on which the non-conformity was discovered and communicated to the Respondent, the Claimant informed the Respondent's representative that "*he had contacted several sellers of such machines and it would not be possible for him to purchase and have delivered another machine that could print on 8 micrometer foil in time to service the Oceania Confectionaries contract*" (Procedural Order No. 2 para.18). A Hamburg Tribunal found that a buyer was justified in failing to purchase substitute goods from another supplier because of the short time available for delivery and alleged difficulty in finding another supplier (*Schiedsgericht der Handelskammer Hamburg, 21 March 1996 (Germany)*). Here the Claimant's available time allowance for delivery was similarly short: a contract signed on 30 May 2002 only yielded initial delivery only on 1 July 2002 and hand-over on 8 July 2002. This was a 38 day time-lag, from date of order to production readiness, while the time left to the Claimant to begin production for Oceania Confectionaries was only 7 days.

36. Under the circumstances, the only reasonable course of action was to allow the Respondent's staff every opportunity to cure the breach by modifying the machine, despite their expressions of doubt as to the likelihood of such a feat. The Claimant was reasonable in its belief that modification of electronic and industrial equipment is not unheard of in the commercial context. Since it did not matter to the Claimant how the Respondent fulfilled its bargain, even a temporary solution that would buy time to deliver a conforming machine would have been satisfactory. It is even arguable that the Respondent shared this belief since it allowed its staff to attempt modification, instead of informing the Claimant that this was an impossible task and that it should seek another solution.

37. Given the information at the Claimant's disposal with respect to replacement machines, the amount of time available for mitigation, and the actions of the Respondent during this time, the Claimant took reasonable measures to mitigate its losses. Therefore, the Respondent is not entitled to any reduction in damages.

2. The Respondent is Liable to the Claimant for Damages

38. The Respondent is liable for "*any lack of conformity which exists at the time when the risk passes to the buyer, even though the lack of conformity becomes apparent only after that time*." (Art. 36 CISG) The machine did not conform to the contract at the time the risk passed to the Claimant (see above paras. 13 to 14). The lack of conformity became apparent after the Claimant attempted to meet its customer's needs. The Claimant met its obligation to take reasonable measures to mitigate its loss, including loss of profit, resulting from the Respondent's breach. The Claimant is therefore entitled to claim damages for breach of contract from the Respondent (Art. 45(1)(b) CISG) which "*consist of a sum equal to the loss, including loss of profit*" (Art. 74 CISG) suffered by the Claimant as a consequence of the breach (discussed in paras. 39-42). These losses were entirely foreseeable, as discussed in paras. 43-45, since the Respondent was informed in advance what the profit expectations were from the Oceania Confectionaries contract (as discussed in para. 46).

2.1. The Claimant's Losses Were Caused by the Respondent's Breach

39. The Respondent became aware of the Claimant's interest in the confectionary market as early as 17 April 2002 when it was told that "*[w]e are interested in printing … metallic foils for*

use in the confectionary market" (Claimant's Exhibit No. 1). The Respondent was made aware on 10 May 2002 that the Claimant "*signed the contract with Oceania Confectionaries yesterday, which we must be able to service by 15 July*" (Claimant's Exhibit No. 3). The value of that contract was immediately impressed upon the Respondent when it was told that "*we can expect to earn a profit of $400,000 a year. The contract runs for four years subject to renewal at the end of that period.…[W]e can anticipate a long period of handsome profits*" (Claimant's Exhibit No. 3).

40. The Claimant's ability to keep the Oceania Confectionaries contract depended on being the first producer to have a "*machine in place and producing*" (Claimant's Exhibit No. 3). The Claimant also made it clear to the Respondent that the Oceania market is "*very small and it is only the Oceania Confectionaries account that makes the flexoprint machine worthwhile*" (Claimant's Exhibit No. 3). In response to this clear and vital information, the Respondent, on 16 May 2002, offered to ship the machine directly from Greece "*rather than by way of [its] workshops*" (Claimant's Exhibit No. 4). Furthermore, on 27 May 2002 the Respondent told the Claimant that it could "*be assured that with this machine you will be able to meet all the needs of your customers*" (Claimant's Exhibit No. 6).

41. On 1 August 2002 the Claimant told the Respondent that the machine was still not printing on its "*foil products for confectionary wrapping*" (Claimant's Exhibit No. 9). The Claimant reminded the Respondent of the value of its contract with Oceania Confectionaries by referring to the requirement communicated in the letter of 10 May 2002 that "*[the Claimant] begin delivery to [Oceania Confectionaries] by 15 July*" (Claimant's Exhibits Nos. 9 & 3). More than two weeks had passed and Oceania Confectionaries was "*threatening to cancel the contract if [the Claimant was] not able to start production promptly*" (Claimant's Exhibit No. 9). Finally, in the letter of 15 August 2002 (Claimant's Exhibit No. 10), the Claimant informed the Respondent that it was still not "*able to print quality foil products for our customers,*" that "*Oceania Confectionaries has cancelled its contract with [the Claimant] since*" the Claimant was "*not able to supply them with the printed foil they needed*" and that "*the machine is useless to [the Claimant].*"

42. It is evident from these facts that the Claimant's losses stem directly from the Respondent's breach of the contract. The delivery of a non-conforming machine under Art. 35(2)(b) CISG directly caused the cancellation of the Oceania Confectionaries contract. The Respondent failed to cure its breach and the Claimant could not mitigate its losses beyond resale of the

machine for less than the price paid. The Claimant's losses were certain, entirely foreseeable as a possible consequence of the Respondent's breach, and untainted by any contributory acts or omissions by the Claimant or any other party.

2.2. It Was Impossible for the Respondent Not to Foresee the Claimant's Certain Losses

43. The CISG limits recovery of damages pursuant to the doctrine of foreseeability (*Gotanda p.81*) through objective and subjective tests (Art. 74 CISG). From a subjective standpoint, "*damages may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a possible consequence of the breach of contract.*" The objective component of the test asks "*whether a reasonable party in the same situation could expect the loss from non-performance*" (*Enderlein & Maskow p.300*).

44. In the present case, it was impossible for the Respondent not to have foreseen the consequences of its breach. The Claimant told the Respondent exactly how much profit it stood to make as a result of the contract with Oceania Confectionaries. The Claimant's expected $400,000 annual profit is beyond dispute (Procedural Order No. 2). Furthermore, the contract was not a mere possibility at that stage, it was a virtual certainty. The only circumstance that could cause the Claimant to lose that contract was not being able to deliver printed foil products on time, the key component of which was the contract for the flexoprint machine with the Respondent.

45. Not only was the Respondent informed of the dollar value of the Oceania Confectionary contract, it was also told exactly why the contract would be so lucrative and so valuable to the Claimant. With the Respondent's machine installed and operating, the Claimant would have a "*commanding lead*" (Claimant's Exhibit No. 1) in a small market. Since it was "*only the Oceania Confectionaries account that makes the Flexoprint machine worthwhile*" no other competitor would make a similar purchase if the Claimant started production first (Claimant's Exhibit No. 3). Under these circumstances, a reasonable party in the Respondent's situation would have foreseen precisely the loss claimed as a result of non-performance. The Claimant's losses were not merely possible, they were certain.

2.3. The Claimant is Entitled to Claim Actual Loss and Lost Profits

46. Art. 74 CISG entitles the Claimant to recover "*loss, including loss of profit*." Tribunals deciding transnational contractual disputes rarely have difficulty finding that a claimant is entitled to lost profits once a breach of contract has been established (*Gotanda p.88*). Indeed, it is well-recognized by international Tribunals that a wrongful breach of contract entitles the injured party to the benefit of the bargain (*Sapphire Int'l Petroleums Ltd. v. Nat'l Iranian Oil Co. p.185-86; Liberian Charterer v. Russian Shipowner*). Similarly, actual loss, i.e. monies expended by a claimant is not hard to determine. The undisputed actual loss in this case is $95,000 (Procedural Order 1 para.10).

3. Damages Amount to $2,756,117 in Real Terms

47. Since the requirement of foreseeability is met, the Tribunal must proceed to calculate the appropriate damages (*Gotanda p.89*). In this regard, the Tribunal's decision in *Indian Mfr. v. German Mfr.* provides a good illustration of the generally-accepted approach. In that case, the Tribunal ruled that a German manufacturer (the respondent) breached a technology licensing agreement that it had entered into with an Indian manufacturer (the claimant) by failing to provide the claimant with certain documents as provided for in the agreement. In determining the damages, the Tribunal ruled that the claimant's loss of profits arose naturally from the respondent's breach of the agreement, explaining that "*[t]he claimant unquestionably expected to make a profit from the local manufacture and sale of products [resulting from the technology licensing agreement], and its inability to do so naturally led to a loss of profits, a result which both parties must have known at the time they entered into the Agreement"* (*Indian Mfr. v. German Mfr.*).

48. The Tribunal then turned to the task of quantifying the lost profits and found that detailed and reasoned estimates of the costs of manufacturing the products, the prices at which they could be sold, its prospective market share and projected sales growth, and the ensuing profit that would have been made, constituted adequate proof of loss. The Tribunal awarded the claimant lost profits for the duration of the agreement, adjusted to the present value, and discounted by a risk factor to take into account uncertainties inherent in future projections (*Indian Mfr. v. German Mfr.*).

49. In the present case, the Tribunal's task is mercifully simpler. The Claimant's contract with Oceania Confectionaries was certain. The end result of all calculations related to costs and

prices are contained in the stipulated profit figure of $400,000 per annum (Procedural Order No. 2). All that is required of the Tribunal is to choose the appropriate method of determining present value and those risk factors to be taken into account.

50. The Claimant's position is that the Discounted Cash Flow method (hereinafter "DCF") is the generally-accepted method for determining present value, see paras. 52-54. Further, the Claimant argues that the initial four-year contract with Oceania Confectionaries and the subsequent renewal should both be included in the calculations, referred to in paras. 55-57. The initial contract was as close to risk-free as possible in the commercial context. The renewal was just as foreseeable to the Respondent as the initial contract and the Claimant was the most likely party to benefit from this term. Consequently, the Tribunal should discount the value of the contract and the renewal at the relatively low-risk prime lending rate of 4%. Subsidiarily, if the Tribunal views the risk factors attached to the renewal to be distinct from those of the initial contract, the renewal should be discounted by no more than the comparatively high-risk average return on investment rate of 9%, see paras. 58-62.

51. These calculations result in a damage award of **<u>$2,756,117</u>** in real terms (or $2,549,421 in nominal terms). The award in the subsidiary argument would be $2,436,854 in real terms (or $2,272,346 in nominal terms), as illustrated in paras. 63-67.

3.1. Discounted Cash Flow is the Accepted Method of Calculating Lost Profits

52. The generally-accepted method of determining a present value for future lost profits is the Discounted Cash Flow method (*Gotanda p.90*). This method brings future values "back" to a current value by applying discount factors in what can best be described as a reverse compound interest process. The discount factors are interest rates that take into account the time value of money (the theoretical cost of borrowing in a risk-free and inflation-free market) and perceived future risks.

3.1.1. The Claimant's Assumptions are Commercially Reasonable

53. The Claimant has made reasonable assumptions in computing the amount of damages. The first assumption is that it has not been settled whether the $400,000 annual profit figure is stated in real or nominal terms. If the amount is expressed in real terms, i.e. net of annual inflation, then the Tribunal should discount future profits by interest rates that are net of

Oceania's 2% inflation (Procedural Order No. 2). If the amount is expressed in nominal terms then the Tribunal should discount future profits without taking inflation into account. However, this would indicate that the Claimant's contract with Oceania Confectionaries was declining in value over the term of the contract—a factor the Tribunal must take into account when determining risk applicable to the damage award. Consequently, until the Tribunal rules on this issue, the Claimant will calculate damages in both real and nominal terms.

54. It is also assumed that the Claimant was entitled to depreciate its initial capital investments on a straight-line (equal) basis over the projected life of the machine, which is 20 years (Procedural Order No. 2). The effect of this assumption is that annual profit figures are reduced by the annual depreciation amount. In this case, that amount is $4,750 per annum (calculated by dividing the $95,000 actual loss by 20 years). The annual profit figure net of depreciation is therefore $395,250. This is consistent with modern practice in determining damages since the failure to take depreciation into account would constitute double dipping. A claimant asking for separate consideration for the capital amount invested should remove capital depreciation from annual profit figures to properly reflect the benefit of the bargain (*Himpurna California Energy Ltd. v. PT Perusahaan Listruik Negara*).

3.2. The Appropriate Discount Factor for the Lost Contract is 4%

55. The Tribunal's task is to determine by what factors, over and above the time value of money, the Claimant's uncontested future lost profits should be discounted to bring them back to a present value. The Claimant has already established that the contract with Oceania Confectionaries was signed before the conclusion of its contract with the Respondent. It has also been established that the contract had an initial term of four years during which there could be no competition for the contract. This is as close to risk-free as the Tribunal is likely to see in a commercial context. The appropriate discount factor that the Tribunal must apply is therefore 4% in real terms, which is 6% in nominal terms (Procedural Order No. 2).

56. Four percent in real terms is the sum of the time value of money and a risk premium. It includes Oceania's 1% prevailing time value of money rate, calculated by deducting inflation from the Central Bank's prevailing 3% Discount rate (Procedural Order No. 2). It also includes a 3% risk premium that commercial banks in Oceania charge to their best customers, calculated by deducting 2% inflation and 1% Time Value of Money from the prevailing 6% prime lending rate (Procedural Order No. 2). This means that some risk is

assumed but that risk is limited to standard commercial credit risk: some things may go wrong, as in any business deal, but this deal is so evident and its terms so certain as to justify the lowest commercial credit rate. This is exactly the view of the risk inherent in the Oceania Confectionaries contract that the Tribunal should adopt by accepting a 4% discount factor.

57. This means that the value of the *lost profits* for the eight years of the Oceania Confectionaries contract is **<u>$2,661,117</u>** in real terms (or $2,454,421 in nominal terms). This is calculated by applying the DCF formula: the sum of the profits net of depreciation in each of the eight years of the contract, where each year's profit is discounted by 4% (6% in nominal terms) on a compound basis. Mathematically: ∑ (from 1 to n) *of* [395,250/(1+r)^n] (where r = 4% in real terms or 6% in nominal terms; n = 1 to 8).

3.3. Subsidiarily, the Appropriate Discount Factor for the Renewal is no more than 9%

58. It has already been established that the Claimant's renewal of the Oceania Confectionaries contract was foreseeable to the Respondent at the time it concluded its contract with the Claimant. Therefore, the contract renewal is relevant to the calculation of lost profits. The rumoured arrival in Oceania of a second customer for foil printing, Oceania Generics (Procedural Order No. 2), is not relevant as a mitigating factor, nor is it relevant as a risk factor to the Claimant's ability to successfully renew the Oceania Confectionaries contract in 2006. The relevant time to determine if a loss was foreseeable is the conclusion of the contract (*Gotanda p.82, Enderlein & Maskow p.301*). The Oceania Generics plant was merely a rumour in 2002 at the time the Claimant contracted with the Respondent.

59. Should the Respondent seek to argue the arrival of Oceania Generics as evidence of the risk of competition surfacing in time for the renewal of the Oceania Confectionaries contract, then the Respondent must concede that the Claimant would be in the best position to capture that business for exactly the same reasons that it would have been in the best position to secure the renewal of the Oceania Confectionaries contract. The Claimant would have been the most established and experienced incumbent producer in Oceania and would have leveraged that status towards securing any and all future business. If the Tribunal accepts the appearance of Oceania Generics as a relevant risk factor, it must accept an amendment of the claim to reflect the foreseeability of $700,000 of annual profit (before depreciation) in 2007, 2008 and 2009. The net effect of such an amendment would be to compensate for any

enhanced risk the Claimant would have faced. Therefore the Claimant urges the Tribunal to disregard any attempt by the Respondent to plead the eventual arrival of Oceania Generics to the market in 2007.

60. With regards to the risk factors to be considered in connection with the Oceania Confectionaries renewal, the Claimant argues that 4% is the most appropriate discount factor, the same rate as argued for the initial contract. However, if the Tribunal is not persuaded that the risks with respect to the initial contract are identical to the risks with respect to the renewal, then 9% in real terms is the maximum discount factor that the Tribunal should choose. This rate takes into account the time value of money of 1% and a risk premium of 8%, calculated by subtracting inflation at 2% and time value of money at 1% from the average return on investment in Oceania of 11% (Procedural Order No. 2). This discount rate implicitly acknowledges the risk related to the renewal to be more than two-and-a-half times the risk of the initial contract.

61. This is a reasonable risk which takes into account the possibility of competition emerging in the market but which also recognizes that the Claimant would have been the incumbent producer with the most experience and the longest relationship with the client. It is also the risk premium demanded by investors in Oceania when investing in projects of average risk (Procedural Order No. 2). While the Claimant could make the argument that it faced less than average risk as the incumbent holder of the Oceania Confectionaries account, this rate is a reasonable compromise in line with Oceania's commercial environment. Therefore, this is the view of the risk inherent in the Oceania Confectionaries contract renewal that the Tribunal should adopt by accepting a 9% discount factor.

62. This means that the value of the lost profits in the subsidiary argument is $2,341,854 in real terms (or $2,177,346 in nominal terms). This is calculated by applying the DCF formula: the sum of the profits net of depreciation in each of the first four years, where each year's profit is discounted by 4% (6% in nominal terms) on a compound basis; plus the sum of the profits net of depreciation in each of the last four years of the contract, where each year's profit is discounted by 9% (11% in nominal terms) on a compound basis. Mathematically: ∑ (from 1 to n) of [395,250/(1+r)^n] + ∑ (from 1 to m) of [395,250/(1+s)^m] (where r = 4% in real terms or 6% in nominal terms; n = 1 to 4; and where s = 9% in real terms or 11% in nominal terms; m = 5 to 8.).

3.4. The Total Damages are Accurate and Fair

63. The *total damages* to which the Claimant is entitled as a result of the Respondent's breach is **$2,756,117** in real terms (or $2,549,421 in nominal terms). This is calculated by adding the actual loss ($95,000) to the lost profits from the contract. In the subsidiary argument, total damages amount to $2,436,854 in real terms (or $2,272,346 in nominal terms). This is calculated by adding the actual loss ($95,000) to the lost profits for the initial contract ($1,434,716 in real terms or $1,369,583 in nominal terms) and the loss of the renewal ($907,138 in real terms or $807,763 in nominal terms).

64. The total damages are an accurate and fair reflection of the Claimant's losses resulting from the Respondent's breach. The amount takes into account careful consideration of the substantive law, and the facts and circumstances of this case. Arguments attacking the Discounted Cash Flow method as arbitrary, or that its results represent an abuse of rights, are unconvincing. The Claimant's entitlement to loss, including loss of profits is well-established. The DCF method is equally well-established as the principal method for calculating future losses since it derives from standard commercial practice. The Claimant is arguing for discount rates that were prevailing market rates in Oceania during the applicable period and which provide a stable point of reference for comparative risk analysis.

3.4.1. Lost Profits were Calculated Using Oceania's Market Rates

65. Far from being an arbitrary method, DCF's greatest strength is that it requires careful consideration of the risks to be taken into account in each and every case. While the DCF method will never provide arbitrators with a "standard" calculation in every case, its flexibility should not be confused with arbitrariness. Any discretion inherent in its logic has been structured in this case through careful analysis of comparable risks facing market players in Oceania. These risks are reflected in the market rates prevalent in Oceania's low-inflation and relatively low-risk environment. It is precisely these market rates, as provided in Procedural Order No. 2, that the Claimant has applied to the calculation of damages. These rates, ranging from commercial credit rates to average investment rates, are consistent with the risks faced by a printing venture in a small captive market and where exorbitant rates of risks such as those used in high-technology ventures would be wholly inappropriate.

3.4.2. An Abuse of Rights Argument is Unavailable

66. The doctrine of abuse of rights has appeared in international arbitration in a few foreign direct investment cases. These typically involve a claim against an already-impoverished developing country for potential profits from investments that were never made (*Himpurna California Energy Ltd. v. PT Perusahaan Listruik Negara*). This exceptional intervention is not warranted in this case. The Respondent is hardly an impoverished nation. The context is not that of foreign direct investment. The Claimant paid the Respondent its price for the non-conforming machine. Further, the abuse of rights doctrine has been resoundingly criticized, especially because it relies on the Tribunal to act as *amiable compositeur* or *ex aequo et bono* to make a ruling in equity when it has been granted no authority to do so (*Gotanda p.105*). The doctrine is not consistently or overwhelmingly viewed as a generally-accepted principle of international commercial law and may have been misapplied in its most famous case (*Gotanda p.106*).

67. The Claimant submits that it has proven the Respondent's breach under Art. 35 CISG and that it met its obligation to mitigate under Art. 77 CISG. Therefore, the Claimant is entitled to its damages for loss and lost profits under Art. 74 CISG. The Claimant has proven that its loss and lost profits were caused by the Respondent's breach and that they were entirely foreseeable to the Respondent. Finally, the Claimant submits that its calculation of damages is based on the generally-accepted DCF method using commercially acceptable and factually sound discount factors. The total damages that the Tribunal should award the Claimant amount to <u>**$2,756,117**</u> in real terms (which is $2,549,421 in nominal terms).

C. *The Claimant Commenced Proceedings Within the Applicable Limitation Period*

68. The Respondent argues that the Claimant's action is time-barred pursuant to Art. 14 of the Private International Law of Mediterraneo, which applies a two-year prescription period to contracts for the international sale of goods. The Respondent asserts that its two-year prescription period applies because, in the absence of a choice of a law on that issue, the Tribunal should apply the law of seller on the basis that the characteristic performance test deems the seller's law to be most closely connected to the contract.

69. The characteristic performance test is a generally-accepted principle of private international law. The Claimant asserts, however, that this principle does not apply here and that the Respondent has erred in its assumption to the contrary. The Claimant argues that the

characteristic performance test is rebuttable and subject to exceptions which render the buyer's law applicable, including where the contract expressly provides that the seller must perform its obligation to deliver the goods in the buyer's state. The present case falls within the exceptions to the characteristic performance test. Further, the factual circumstances overwhelmingly point to the application of the Claimant's law as the law with which the contract is most closely connected. In addition, the Claimant's law should apply as it is most consonant with the underlying spirit of the contract and the hypothetical will of the parties.

70. The Claimant further argues that even if the Claimant's law is inapplicable, the claim is not time-barred. For the Tribunal to apply the Respondent's law would be contrary to both general principles of private international law and the will of the parties as manifested in their contract. The Tribunal is not bound to apply national laws to the issue of prescription, because the contract strongly indicates the parties' intention to subject their contract to general principles of international commercial law. The Tribunal should therefore apply the internationally-recognized minimum standard of three years reflected in the UNIDROIT Principles as the appropriate limitation period; because the Claimant's action was commenced less than three years after the defect in the goods was noticed, the Tribunal should therefore allow the Claimant's action to proceed.

1. The Claimant's Four-year Limitation Period Applies to the Claim

71. The Tribunal should apply general principles of private international law to determine the applicable law in the present case. This approach is more fair and neutral than applying national conflict of laws rules to parties of differing nationalities (*Lando p.108-9*), and accommodates the parties' intention to seek a "denationalised" solution through international arbitration (*Lando p.108-9*). In determining the applicable law based on general principles of private international law, the Tribunal also ensures that the decision rendered will be acceptable to both parties and will promote certainty in the application of international commercial law (*Berger p.572*). The Claimant argues that under these general principles of conflict of laws, the Claimant's law applies.

72. The Claimant's prescription period is also the most appropriate law to apply as it is in keeping with internationally accepted standards on prescription in the international sale of goods context. The contract expressly subjects the parties' substantive agreement to the CISG, reflecting their implicit expectation to apply generally-accepted standards of

commercial law to all substantive aspects of their contract. As the Claimant's law is in keeping with international standards on prescription in the international sale of goods context, it is the most appropriate law to apply in the present case. The application of the Claimant's law will be most consistent with the logic and spirit of the contract.

73. The Claimant's four-year period of limitation should therefore apply. As the Claimant commenced proceedings less than three years after the Claimant noticed the defect in the goods, it did so within the applicable prescription period. The Tribunal should therefore allow the claim to proceed.

1.1. The Tribunal Should Apply Art. 32 of the CIDRA Rules in order to determine the Applicable Prescription Period

74. Clause 12 of the parties' written agreement stipulates that the agreement is subject to the CISG, which is silent on the issue of prescription. Clause 13 stipulates the CIDRA rules for disputes arising from their agreement (Claimant's Exhibit No. 7), and identifies Vindobona, Danubia as the seat of the arbitration (Claimant's Exhibit No. 7). Danubia has adopted the Model Law without amendment. As the contract is between two parties who have their places of business in different states and entails the commercial sale of goods, the Model Law applies to it, as per Arts. 1(2) and 1(3). The Model Law therefore supplements the CIDRA rules as the *lex arbitri* applicable to the dispute (*Redfern p.77*).

75. The Claimant recognizes that prescription should be treated as a substantive issue in the proceedings, as there is a general international consensus that the issue is governed by the law of the contract (*Rabel p.506*). As the parties' choice of substantive law, the CISG, is silent on the issue of prescription, the Claimant concedes that the parties made no express or implied choice of law on the issue. The Claimant therefore agrees with the Respondent that the issue is subject to Art. 32 of the CIDRA Rules, under which the Tribunal should apply the law determined by the conflict of law rules it considers applicable. Additionally, the Tribunal provided that the question of prescription shall be guided by the most appropriate rule of choice of law under Art. 32 of the CIDRA rules (Procedural Order No. 1, para.14).

1.2. The Claimant's Law Applies Under General Principles of Private International Law

1.2.1. The Tribunal Should Apply General Principles of Private International Law

76. Clause 13 of the contract explicitly stipulates that the parties have chosen "*international arbitration*" under the aegis of CIDRA, an international organization engaged in dispute resolution. Such an express reference to an international arbitral body, combined with the application of rules of international procedural law, demonstrates the parties' willingness to subject their dispute to internationally recognized principles of procedural law, including general conflict of laws rules.

77. The very fact that the contract relates to an international commercial transaction, contains an arbitration clause, and that the dispute is between parties from different states, warrants the application of general principles of private international law in the present case (*Croff para.12*). Under such circumstances the parties are assumed to have chosen international arbitration in an effort to "*denationalize*" their dispute (*Lando p.110*). Parties choose international arbitration in an effort to distance themselves from unfamiliar national laws.

78. In addition, it is the goal of international commercial arbitration to have Tribunals render decisions that are mutually acceptable to the parties and that strengthen the use of arbitration as a forum for the settlement of commercial disputes (*Berger p.502*). Further, arbitration aims at creating certainty and predictability in commercial transactions (*Iran v. Westinghouse p.289*). These policy objectives can only be achieved if the Tribunal applies conflict of laws rules to which the parties would have agreed had they turned their minds to this question (*Iran v. Westinghouse para.289, Juenger p.385*). The present dispute arises in the commercial context, the parties are from different states, and their correspondence and contract show no indication of any familiarity with each other's national laws. It is reasonable to presume that businesspersons such as the present parties are unlikely to choose national conflict of laws rules, either singularly or cumulatively, to apply in the present case. Rather, they are more likely to adopt general principles of conflict of laws, particularly those relating to the international sales context. The Tribunal should therefore apply general principles of private international law to determine the applicable law. Such an approach is

most consistent with the parties' intentions in seeking arbitration in the present case, and complies with the underlying objectives of international arbitration.

1.2.2. General Principles Favour the Law Most Closely Connected to the Contract

79. The Claimant recognizes that the principle of closest connection is well established in international commercial law (*Maniruzzaman Issues p.377, Lew p.374*). Art. 4(1) of the Law Applicable to Contractual Obligations (hereinafter "Rome Convention") stipulates that in the absence of choice made by the parties, the contract shall be governed by the law with which it has the closest connection. The Rome Convention has been unanimously adopted in Europe. Further, it has formed the model for national legislation addressing conflict of laws rules in several countries (*Berger p.503*). A similar stipulation is also found in Art. 9(2) of the Inter-American Convention on the Law Applicable to International Contracts (hereinafter "Mexico Convention") which speaks of the law with which the contract has the "closest ties." Art. 13(3) of the Benelux Convention on International Private Law (hereinafter "Benelux Convention") similarly stipulates the principle of "*liens les plus étroits*."

1.2.2.1. The Characteristic Performance Test is Subject to Exceptions Which Render the Buyer's Law Applicable

80. The Claimant accepts that the law most closely connected to the contract is generally presumed to be that of the state in which the party that performs the obligation characteristic of the contract has its place of business or residence. Art. 4(2) of the Rome Convention creates such a presumption (*North p.14*). In a contract for the sale of goods, Art. 8(1) of the Hague Convention on the International Sale of Goods (hereinafter "Hague Convention") creates a similar presumption (*Matić p.65*).

81. The presumption favouring characteristic performance and the seller's law is not, however, absolute. Art. 4(5) of the Rome Convention stipulates that Art 4(2) is rebutted where the party carrying out the characteristic performance is not the most closely connected to the contract; where the characteristic performer cannot be determined; or where, having considered the circumstances of the case as a whole, the law of another state appears more closely connected to the contract (*North p.15*, *Juenger III p.302*). In addition, Art. 8(2) of the Hague Convention lists circumstances in which the buyer's law applies, creating exceptions to the presumption in favour of the seller's law where the negotiations and conclusion of the

contract occur in the buyer's state, where the contract expressly provides that the seller must perform its obligation to deliver the goods in the buyer's state, or where the contract was concluded on terms determined mainly by the buyer and in response to a call for tenders.

1.2.2.2. The Present Circumstances Come Within the Exceptions to the Application of the Seller's Law

82. Art. 8(2)(b) of the Hague Convention creates a presumption in favour of the buyer's law where the contract expressly requires that the seller perform its obligation to deliver the goods in the buyer's state. The official interpretative document on the Hague Convention, *Explanatory Report to the Hague Convention on the Law Applicable to Contracts for the International Sale of Good*s, makes clear that Art. 8(2)(b) of the Hague Convention applies in particular in circumstances where "*the seller has contracted to deliver and install a complex machine in the buyer's factory*" (*von Mehren, para.75*). The report states that "*in view of the complexity and importance of the activities that the seller undertakes to perform at the buyer's place of business, in circumstances where the seller contracts to <u>deliver</u> and <u>install</u> a complex machine at the buyer's factory, it is reasonable to assume that in the absence of a contractual stipulation for another law, the buyer's law applies*" (*von Mehren, para.75*).

1.2.2.2.1. The Contract is for the Delivery of a "Complex Machine"

83. The present contract is for the sale of a sophisticated machine used for printing on special materials of very particular specifications. The first paragraph of the written agreement refers to the machine explicitly as "*one second hand 7 stand Magiprint Flexometix Mark 8 flexoprinter machine*" (Claimant's Exhibit No. 7). The flexoprint machine's complexity is apparent from the fact that the Respondent sent a team of engineers and mechanics to set it up on the Claimant's premises (Claimant's Exhibit No. 4, Respondent's Exhibit No. 2). The Respondent's mechanics took more than one week to render the flexoprint machine fully operational (Respondent's Exhibit No. 2).

1.2.2.2.2. The Seller Contracted to "deliver and install" the Flexoprint Machine

84. The letter dated 16 May 2002 (Claimant's Exhibit No. 4) shows that the Respondent expressly took responsibility for delivering the flexoprint machine, accounting for the cost of the obligation in its price. The price of the machine was reduced by $2,500 to recognize it.

85. The contract further explicitly provides that the seller must perform his obligation to deliver the flexoprint machine in the Claimant's state. Clause 1 expressly states: "*price is 42,000 CIF Port Magreton, Oceania*" (Claimant's Exhibit No. 7). *INCOTERMS 2000* states that "*CIF, followed by named port*" designates that port as the place of delivery of the goods being shipped. Accordingly, the contract sets the place of delivery as Port Magreton, Oceania. In fact, the goods were shipped from Greece, and the Respondent adjusted the price of the flexoprint machine to account for this shipment (Claimant's Exhibit No. 5). The "adjusted price" in conjunction with the INCOTERM expressly stipulated obligates the Respondent to deliver the goods to the Claimant's state.

86. Clause 2 of the written agreement stipulates that the "*[m]achine is to be refurbished by the seller on installation at buyer's premises*" (Claimant's Exhibit No. 7). This obligation to install and refurbish the flexoprint machine is reinforced by the letter of 16 May 2002, in which the Respondent undertakes to have his engineers "*re-erect [the machine] on your premises and refurbish anything that required it*" (Claimant's Exhibit No. 4). The Claimant's letter of 21 May 2002 (Claimant's Exhibit No. 5) reiterates that the flexoprint machine is to be supplied "direct to our plant at Site No 73, New Airport Industrial Development." It is clear from the correspondence through which the contract was formed that the seller was obligated to deliver and install the flexoprint machine in the buyer's factory.

87. In light of the terms of the contract and the correspondence which constituted it, the Respondent bound itself to deliver, install, and refurbish the flexoprint machine in the Claimant's state. The present circumstances therefore come within the exception to the presumption favouring the seller's law, and instead indicate that the contract is more closely connected to the buyer's law. In *ICC Award 1177, 1968* the arbitrators relied on the contract's CIF INCOTERM to conclude that the agreement obligated the seller to deliver the goods in the buyer's state. The existence of this significant nexus led the Tribunal to rule that buyer's law applied as the law most closely connected to the contract. Similarly, in *Netherland Seller v. French Buyer*, the Tribunal relied on a contractual term stipulating "CIF, France" in the absence of the parties' explicit choice, holding that the INCOTERM indicated the place "*of accomplishment of the essential obligation of the contract*" and consequently applying the law of the buyer's state as most closely connected to the contract.

1.2.3. The Facts Demonstrate that the Claimant's Law is Most Closely Connected to the Contract

88. The Respondent has erred in the *singular* weight it attaches to the test of characteristic performance to determine the law most closely connected to the contract (Respondent's Answer, para.22). Characteristic performance is typically used to determine the applicable law of the contract, but it is often applied in conjunction with other connecting factors. In addition to the characteristic performance test, the Tribunal in *Iran v. Westinghouse* took into account the subjective connecting factors in the case, including the relative bargaining position of the parties, the lack of a prior business history, and the fact that one of the parties was a non-commercial entity.

89. The singular application of the characteristic performance test has been criticised. In complex situations, simply choosing one performance over another as being "*most characteristic*" confers a capricious choice of law privilege by invoking the home state law of those who enjoy expertise because they habitually supply goods in international transactions (*Juenger p.205*). The most recently adopted international convention on contractual obligations, the Mexico Convention, deliberately rejected the characteristic performance test to determine the applicable law (*Juenger p.205*). In the absence of choice, the Mexico Convention provides that the Tribunal "*take into account all objective and subjective elements of the contract to determine the law of the state with which it has the closest ties*" (Art. 9(2)). The approach taken in the Mexico Convention has been varyingly described as the "connecting factors test" or the "center of gravity test" (*Maniruzzaman Issues p.379*).

90. In *Syrian Trading Organisation v. Ghanaian Enterprise*, the Tribunal stated that "*decided international awards published so far show a preference for the conflict rule according to which the contract is governed by the law of the country with which is shares its center of gravity.*" In *Netherland Seller v. French Buyer*, the Tribunal rendered its decision by cumulatively considering several connecting factors, including the destination of the goods, the place of payment and the nationalities of the parties involved in the dispute. In that Award, the Tribunal concluded that the majority of the connecting factors pointed to French law, the law of the buyer, as being most closely connected to the contract. Similarly, in *Senegalese Buyer v. Egyptian Seller*, the Tribunal considered such factors as the place of delivery, place of payment, place of negotiations, headquarters of both parties, and the

conclusion of the contract. It concluded on the basis of these and other connecting factors that the law most closely connected to the contract was the buyer's.

91. In the present case, the Claimant's purchase of the flexoprint machine was motivated by its need to secure a lucrative confectionary contract of which the Respondent was made aware (Claimant's Exhibit No. 3). The Claimant had the most to gain or lose from the contract and played an active role in the purchase, going to Athens to inspect a specimen of the machine recommended by the Respondent, then requesting that delivery be hastened to meet its contractual commitments (Claimant's Exhibit No. 3). These circumstances demonstrate the Claimant's substantial reliance on the contract and, consequently, its closer connection to it.

92. In a letter dated 21 May 2002, the Claimant confirmed its order to purchase the flexoprint machine (Claimant's Exhibit No. 5). In a letter dated 27 May 2002, the Respondent sent the Claimant a written agreement to sign and return "*so that the flexoprint machine can be sent to you quickly*" (Claimant's Exhibit No. 6). The phrasing of the letter indicates that once the Claimant had signed the agreement and posted it, no dispute could remain that the contract was concluded. Oceania is consequently the place where the contract was signed and concluded. In addition, the agreement stipulates that the Respondent's obligations to the Claimant included the delivery, refurbishment, and installation of the flexoprint machine, all at the Claimant's premises in Oceania (Claimant's Exhibit No. 7), while only the payment obligation was to be effected in Mediterraneo: the preponderance of the essential obligations under the contract were clearly to be performed in the Claimant's state. The overwhelming majority of factors that point to the Claimant's law lead to the conclusion that both parties would reasonably have seen the Claimant as the party with the greatest stake, and consequently the closest connection to the contract. The Tribunal should therefore apply the Claimant's four-year period of limitation, because that is the law most closely connected to the contract, and the law which the parties would reasonably have anticipated would apply.

1.3. The Claimant's Four-Year Limitation Period Should Apply

93. The four-year limitation period that the Claimant's law prescribes is in keeping with generally-accepted principles relating to prescription in international sale of goods. In subjecting their agreement to the CISG, an international instrument that codifies generally-accepted principles on international sales law, the parties indicated their willingness to subject their relationship to general principles applicable in international sales (*ICC Award*

8502, 1996). Art. 8 of the Limitation Convention on the International Sale of Goods (hereinafter "Limitation Convention") prescribes a four-year prescription period for international sales contracts. The Limitation Convention reflects general principles; the Claimant's law is in keeping with this international standard of four years. Application of the Limitation Convention is therefore most consistent with the logic and context of the contract.

1.3.1. The Claimant's Law Complies with General Principles Relating to Prescription in the International Sale of Goods Context

94. While the Limitation Convention has not been adopted in Europe, 24 countries have adopted it and over 35 states participated in its drafting (*UN Yearbook p.98*). Art. 8 of the Limitation Convention provides for a prescription period of four years, a compromise between states favouring shorter and longer periods of limitation (*Sono p.155*). The compromise was reached after considering the difficulties inherent in resolving disputes between parties in different states, who are often separated by great distances; the time needed to investigate a claim; negotiation for possible settlement; and arrangements necessary to institute legal proceedings (*UN Yearbook p.154*). The four-year period of limitation in the Limitation Convention thus reflects reasoned international consensus on the appropriate period of limitation. In applying the same four-year limitation period to this action, the Claimant's law is consistent with the generally-accepted principles reflected in the Limitation Convention.

1.3.2. The Claimant's Law is Most Consistent With the Logic of the Contract and the Presumed Intentions of the Parties

95. In choosing the CISG, the parties intended to apply general principles of international sales law to their contract. The Tribunal in *ICC Award 8502, 1996* concluded that, even without an express or implied choice of law, references to INCOTERMS and Uniform Commercial Practice indicated a willingness to subject an agreement to general principles of international commercial law. The Tribunal in this case should consider the explicit reference to the CISG as indicative of the parties' intention to subject their agreement to principles of international sales law, and apply the law that complies with such principles. The Tribunal should therefore apply the Claimant's law.

2. Even if the Claimant's Law is Inapplicable, the Claim Should Proceed

96. Even if the Tribunal finds that the Claimant's law is not applicable in the present case, it should not summarily apply the Respondent's law. Applying the Respondent's law would be contrary to general principles on limitation periods in international sales contracts and would frustrate the intentions of the parties, as discussed in paras. 97 to 98. The Tribunal is not bound to apply national law, as the parties' choice of substantive law indicates their willingness to subject their contract to general principles of commercial law, discussed in paras. 100 to 102. The Tribunal should therefore directly apply the UNIDROIT Principles, which are generally accepted as a codification of internationally-recognized principles of commercial law, as discussed in paras. 103 to 105. The UNIDROIT Principles apply a three-year limitation period in the context of international commercial contracts. Because the Claimant commenced proceedings less than three years after it discovered the defect, the Tribunal should allow the action to proceed.

2.1. The Tribunal Should Not Apply the Respondent's Law Because it is Contrary to Minimum International Standards on Prescription

97. Art. 10.2 of the UNIDROIT Principles providing for a minimum prescription period of three years and a maximum of ten years. This range strikes a balance between the conflicting interests of the obligee and obligor of a dormant claim (*UNIDROIT Comment*). The drafting history of the Limitation Convention also demonstrates an international consensus favouring three to five years as a reasonable limitation period for international sales contracts. Of the 35 countries that participated in drafting Art. 8 of the Limitation Convention, 14 favoured a three-year limitation period, 14 favoured a five-year period, and five favoured a four-year period (*Yearbook p.98*). Only two states advocated a limitation period of two years.

98. International instruments like the UNIDROIT Principles and Limitation Convention were prepared by leading experts representing all major legal systems. These instruments represent internationally-recognized and generally-accepted standards on international commercial practice (*Iran v. Westinghouse para.314*). The Respondent's two-year limitation period is therefore contrary to minimum standards for prescription in international contracts.

2.1.1. The Respondent's Law is Contrary to the Intentions of the Parties

99. Adoption of the CISG as substantive law demonstrates that the parties intended to subject their contract to international law (see paras. 95-95). Applying the Respondent's two-year limitation period would therefore be inconsistent with the logic of the contract, as it fails to comply with the internationally-recognized minimum prescription period of three years. The Tribunal should not apply such a law as it is contrary to the reasonable expectations of the parties and is inconsistent with their bargain (*Senegalese Buyer v. Egyptian Seller*).

2.2. The Tribunal is Not Bound to Apply a National Law to the Issue of Prescription

100. Adoption of CIDRA arbitration shows that the parties intended to subject their dispute to generally-accepted international standards. Commercial parties generally seek international arbitration in an effort to avoid the application of unfamiliar national laws (*Lando p.199*); rather, they want to ensure the application of fair and neutral laws (*Wortmann p.97*). As the parties in this case chose arbitration as well as the CISG, it should be presumed that they attempted to subject the substantive law of their contract to generally-accepted rules of commercial law (see paras. 95-95).

101. In *ICC Award 9479, 1999* the Tribunal held that explicit choices of international law with regard to *one* aspect of the contract indicated that *other* aspects could not be governed by domestic law inconsistent with general principles, as applying domestic laws in such circumstances would be contrary to the spirit of the contract. In *Iran v. Westinghouse*, the Tribunal determined that the will of the parties warranted the application of general principles of law and not the national law of either party: "*wherever a contract is ...silent in a particular respect, its terms ... shall be interpreted with a view to giving the contractual provisions the meaning and effect they were intended pursuant to both parties' consent*." It further held that "*this principle is not disputed and reflects the generally recognized notion that an arbitral Tribunal must respect the will of the parties, and has to endeavour to give it, as far as legally possible, the effect which they had intended*."

102. The Tribunal in this case is not, therefore, bound to apply national law to prescription. The parties' intention calls for the application of general principles of commercial law, and should be respected.

2.3. The Tribunal Should Apply the three-year Minimum Limitation Period Contained in The UNIDROIT Principles

103. Art. 10.2 of the UNIDROIT Principles stipulates that prescription for international contracts should be at least three years. International consensus on the three-year limitation period is further evidenced in the working papers of the Limitation Convention (see paras. 97-98).

104. Applying the UNIDROIT Principles to an international contract is justified in arbitral practice because the Principles constitute a *ratio scripta* of generally-accepted principles of international commercial law. In *Iran v. Westinghouse* the Tribunal affirmed that, in the absence of an express choice of law, it would determine the applicable limitation period from general principles as set out in UNIDROIT, international conventions, and arbitral practice. The Tribunal justified applying the UNIDROIT Principles as "*a restatement of those 'principes directeurs' that have enjoyed universal acceptance*" and further lie "*at the heart of those most fundamental notions which have consistently been applied in arbitral practice*." In *ICC Award 8502, 1996* the Tribunal described the CISG and UNIDROIT Principles as reflecting admitted practice under international trade law. In *ICC Award 8240, 1995* the Tribunal ruled that UNIDROIT Principles reflect international standards and current practice of trade law.

105. The Tribunal should therefore apply the UNIDROIT Principles' minimum three-year limitation period in the present case. Such an approach is justified by both international arbitral practice and the clearly-manifested will of the parties (see para. 95).

2.4. The Claimant Commenced Proceedings Within the Internationally Recognized Minimum Limitation Period

106. The Claimant became aware of the defect in the goods on 8 July 2002 (Respondent's Answer para.10 & Respondent's Exhibit No. 2). Once it became clear that the printing machine could not be modified to meet the specifications under the contract, the parties spent two and a half years working toward a mutually acceptable settlement (Statement of Claim para.12). That effort having failed, the Claimant commenced proceedings against the Respondent on 5 July 2005, two months after the settlement process ended. The arbitration proceedings commenced less than three years after the defect in the goods was noticed. The Tribunal should thus allow the claim to proceed.