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Memorandum for Claimant

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International Court of Arbitration of the International Chamber of Commerce

Case No. Moot 8
Legal positions in response to the issues
in the Terms of Reference

ON BEHALF OF:

Sports and More Sports, Inc.
214 Commercial Avenue
Oceanside
Danubia

Claimant

AGAINST:

Vis Water Sports Co.
395 Industrial Place
Capitol City
Equatoriana

Respondent

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Abbreviation Index

AG	Amtsgericht (German Petty Court)
Arb	Arbitration
Aus	Austria
BGE	Entscheidungen des Schweizerischen Bundesgerichts (The official reporter of cases decided by the Federal Supreme Court of Switzerland)
BGH	Bundesgerichtshof (German Federal Supreme Court)
BGHZ	Sammlung von Entscheidungen des Bundesgerichtshofes in Zivilsachen (The official reporter of cases decided by the German Federal Supreme Court on civil matters)
c.f.	confer (compare)
CISG	United Nations Convention on contracts for the International Sale of Goods of 11. April 1980
CoP	Conditions of Purchase
Dist. Ct.	District Court
E.D.	Eastern District
EDI	Electronic Data Interchange
e.g.	exemplia gratia (for example)
EML	Model Law on Electronic Commerce
Ewir	Entscheidungen zum Wirtschaftsrecht
EuZW	Europaeische Zeitschrift fuer Wirtschaftsrecht
ff.	following
FOB	free on board (Incoterm)
ForInt	Fordham International Law Journal
F. Supp.	Federal Supplement
F.R.G.	Federal Republic of Germany
GATT	General Agreement on Tariffs and Trade
ICC	International Chamber of Commerce
ICC Bull.	Bulletin of ICC
ICCRA	ICC Rules of Arbitration 1998
i.e.	id est (that means)
IPRax	Praxis des Internationalen Privat- und Verfahrensrechts
LG	Landgericht (German Regional Court)
J.D.I.	Journal du Droit International
ML	Model Law on International Commercial Arbitration
NJW	Neue Juristische Wochenschrift
NYC	Convention on the recognition and enforcement of foreign arbitral awards
OG	Obergericht
OLG	Oberlandesgericht (German Regional Court of Appeal)
p.	page
pp.	pages
para.	paragraph
PO	purchase order
R.D.A.I. Law	Revue de Droit des Affaires Internationales/International Business Journal
RIW	Recht der Internationalen Wirtschaft

RTD com.	Revue trimestrielle de droit commercial et économique
S.D.	Southern District
S.J.Z.	Schweizerische Juristenzeitung
SZIER	Schweizerische Zeitschrift fuer Internationales und Europaisches Recht
ToR	Terms of Reference
TRIPs Rights,	Agreement on Trade-Related Aspects of Intellectual Property Including Trade in Conterfeit Goods
UCC	Uniform Commercial Code
ULIS	Uniform Law on the International Sale of Goods
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNIDROIT	International Institute for the Unification of Private Law
U.S.	United States
v.	versus
YCA	Yearbook of commercial arbitration
ZIP	Zeitschrift fuer Wirtschaftsrecht

Statement of Facts

On 31 March 1999, Claimant, Sports and More Sports Inc. (hereinafter referred to as Claimant), received an announcement of Respondent, Vis Water Sports Co. (hereinafter referred to as Respondent), referring to its web site containing the list of sport goods with prices manufactured by Respondent. Claimant, a retailer in Danubia, contacted Respondent in email on the same day, trying to negotiate more preferable terms than those offered on the web site. Respondent replied on 2 April 1999, informing Claimant that at the purchase of certain amount of goods, discount was available. In the same email URL reference to the General Conditions of Sale was included. Claimant placed its order in email on 5 April 1999, with reference to its General Condition of Purchase, which were attached to the email. The General Conditions contained an ICC Arbitration clause. Respondent answered on 6 April 1999, accepting the order No. 6839 of a value of \$100,000. On 27 May 1999, Claimant placed a subsequent order of \$500,000, referring to its General Conditions again. The order was accepted by Respondent on the following day. For both orders, the goods were duly shipped and paid by letters of credit. In two letters (20 September and 15 October 1999) Vis Fish Company claimed that Respondent's goods were infringing its registered trademark. After receiving legal advice (28 October 1999) Claimant withdrew the goods and declared the contract avoided in its letter of 3 November 1999. Claimant sought restitution of the purchase price and the damages suffered. Respondent refused restitution in its reply. Claimant reaffirmed its avoidance on 16 November 1999.

Claimant contends:

- I. The dispute should be settled in ICC arbitration as stipulated in the arbitration clause incorporated into the sales contract
- II. Claimant had the right to avoid the contract
- III. Claimant is entitled to restitution and damages.

I The Arbitral Tribunal has jurisdiction

The arbitration clause in Clause 14 (Arbitration Clause) of the Conditions of Purchase constitutes a valid arbitration agreement and thus the Arbitral Tribunal (Tribunal) has jurisdiction. The ICC Court of Arbitration has already established the Tribunal's competence to assess the validity of the arbitration clause.¹ Accordingly, the Arbitration Clause is formally valid as it fulfils the requirements under the New York Convention (I.1). The substantive validity of the arbitration agreement is governed by the CISG, and in accordance with its rules governing formation of contracts there is an agreement between the parties (I.2).

I.1 The Arbitration Clause meets the formal requirements of the NYC

The New York Convention (NYC) and the Model Law in International Commercial Arbitration (ML) are applicable to assess the formal validity of the arbitration agreement since the Tribunal should pursue an enforceable award according to Article 35 ICCRA. Thus, although the CISG applies to the merits of the dispute, the NYC and ML should be applied to ensure enforceability (I.1.1). Moreover, as the NYC is stricter than the ML, enforceability in both Danubia and Equatoriana may only be pursued through compliance with NYC (I.1.2). Finally, the arbitration clause meets the formal requirements of the NYC (I.1.3).

¹ Letter from the ICC International Court of Arbitration of 26 July 2000.

I.1.1 The formal requirements for arbitration agreements under the New York Convention and the Model Law must be applied

Although the CISG applies to the main contract, both the New York Convention (NYC) and the Model Law on International Commercial Arbitration (ML) apply, since compliance with the formal requirements under NYC and ML will guarantee enforceability of a future award as required by Article 35 ICCRA.²

The parties have agreed upon CISG as the applicable law to the merits of the dispute in accordance with Article 17 ICCRA,³ as it applies in both Danubia and Equatoriana.⁴ However, although the CISG applies to sales contracts regarding goods, domestic laws may still govern individual clauses included in the contract, such as arbitration clauses.⁵

Even in cases where parties have agreed upon the main contract under CISG, it has been held that the arbitration clause included in that contract may be invalid due to non-compliance with formal requirements.⁶ It follows that a distinction has to be made between formal and substantive validity of an arbitration clause, since these two separate questions are not necessarily governed by the same law.⁷ For instance, in *Filanto v. Chilewich*,⁸ the District Court of New York made a clear distinction between the two questions, applying the New York Convention to the form and the CISG to determine whether there had been an agreement between the parties regarding the arbitration clause.

Consequently, in the present case, the Tribunal should consider the formal requirements for valid arbitration agreements in countries where enforcement may be sought by the parties. Naturally, it would be excessive to ask the Tribunal to investigate the rules governing arbitration agreements in every country where there exists a remote possibility that the award will be enforced. For this reason, Claimant asks the Tribunal only to pursue the enforceability of the award where enforcement is most likely to be sought. As the winning party would seek enforcement where the other party has assets, in the present case the enforcement of the award would presumably take place in either Equatoriana, the seat of Respondent, or Danubia, the seat of Claimant.

Both countries have ratified the NYC and Danubia has adopted the ML.⁹ Even though the aforementioned laws do not in particular rule the validity of arbitration agreements, they must be considered as *lex specialis* which apply to arbitration agreements.¹⁰ The ML applies to international arbitration procedure within the territory of Danubia and thus imposes formal

² *Berger, Klaus Peter* (1993), 'International Economic Arbitration', Kluwer Law and Taxation Publishers, pp. 134 and 238.

³ See Request for Arbitration, paragraph 22, and Answers to Request for Arbitration, paragraph 19.

⁴ Request for Arbitration, paragraph 22.

⁵ See *Schlechtriem, Peter* (1998), 'Commentary on the UN Convention on the International Sale of Goods', 2nd ed., Clarendon Press, Oxford, at 211.

⁶ As in the decision of the *Oberlandesgericht Munchen*, Decision of 8 March 1995, 7 U 5460/94.

⁷ *Lew, Julian D.* (1999), 'The Law Applicable to the Form and Substance of the Arbitration Clause', in ICCA Congress, vol. 9, pp. 114-145, at 119.

⁸ *Filanto S.p.A., v. Chilewich International Corp.*, United States District Court for the Southern District of New York, 789 F. Supp. 1229; 1992 U.S. Dist. LEXIS 5011.

⁹ See Request for Arbitration, paragraph 23.

¹⁰ *Alvarez, Guillermo Aguilar* (1998), 'Article II(2) of the New York Convention and the Courts', ICCA Congress no. 9, pp. 67-81, at page 71, *Craig/Park/Paulsson* (1990), 'International Chamber of Commerce Arbitration', 2nd ed., at 79.

requirements as regards the arbitration agreement.¹¹ The NYC lays down rules for enforceability of awards before national courts.¹² A party cannot invoke the NYC unless the arbitration agreement satisfies the formal requirements of the NYC. Hence, the NYC and ML lay down formal requirements, which applies to the Arbitration Clause.

I.1.2 Enforceability in both Equatoriana and Danubia is only guaranteed through compliance with the New York Convention

Claimant contends that the Tribunal should apply primarily the NYC, since only compliance with NYC ascertains enforceability in both Equatoriana and Danubia.

The NYC applies in both countries as uniform treaty law superseding domestic law¹³ and thus it expresses the minimum requirement in both countries. However, Claimant points out that the agreement must also comply with Article 7 (2) ML as the current arbitration proceedings are taking place in Danubia and thus fall within the scope of the ML. If the arbitration agreement does not comply with Article 7 (2) ML, it could subsequently be declared invalid under the ML by a domestic court in Danubia.¹⁴ Nevertheless, as the interpretation of Article 7 ML is generally more liberal than the NYC,¹⁵ the Arbitration Clause will comply with ML as long as it complies with the NYC.

In addition, it could be argued that the ML could apply to the present case through Article VII NYC. This provision allows a party to rely on the application of more lenient domestic rules regarding the form of the arbitration agreement of the country where enforcement is sought. However, only Danubia has adopted the ML. Consequently, reliance on the more liberal rules of the ML when issuing an award in favor of Claimant may lack enforceability in Equatoriana due to the non-compliance with the formal requirements for arbitration agreements in the NYC. The ML may therefore only be taken into account to a limited extent when interpreting individual provisions in the NYC, as the ML has not only been designed on basis of the NYC but also has modified some of the concepts in the latter.¹⁶ Hence, the formal validity of the arbitration clause should be assessed in the light of the NYC.

I.1.3 The Arbitration Clause is an "agreement in writing" within the meaning of Article II New York Convention

Claimant contends that the arbitration agreement meets the formal requirements laid down in Article II New York Convention (NYC). As follows, this arbitration agreement consists of an exchange of e-mails between the parties, a reference to the Conditions of Purchase (CoP) incorporated in the said exchange, and the Arbitration Clause contained in the CoP.

Article II (1) NYC states that the arbitration agreement between the parties must be "in writing". According to Article II (2) NYC, "agreement in writing" should be interpreted as including "an arbitration clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams".

¹¹ Article 1 (1) ML.

¹² Article I (1) NYC.

¹³ Alvarez (1999), supra note 10, at page 71, and Berger (1993), supra note 2, page 133.

¹⁴ Article 34 ML.

¹⁵ Kaplan, Neil (1996), 'Is the need for Writing as Expressed in the New York Convention and the Model Law Out of Step with Commercial Practice?', *Arbitration International*, vol. 12., no. 1, pp. 27-45, at page 29.

¹⁶ Holtzmann, Howard M./Neuhaus, Joseph E. (1989), 'A Guide to UNCITRAL Model Law on International Commercial Arbitration', Deventer, Boston, pp.262-263.

In the present case the contract has been formed through an exchange of e-mails and thus *appears* not to fall within the scope of Article II NYC. Moreover, the arbitration clause is not *contained* in the e-mails as such but is only incorporated in the contract by reference to the General Conditions of Purchase.¹⁷

Nevertheless, Claimant submits that in spite of these obvious disparities between the facts and the wording of Article II NYC, the said article must be interpreted in such a way as to uphold the validity of the Arbitration Clause.

1.1.3.1 Electronic messages are equivalent to "in writing" in Article II NYC

Article II (2) NYC should not be interpreted as restrictively as to exclude electronic messages. Such a view would not only go contrary to the everyday needs of international trade but also deny a large part of the commercial community effective means of dispute settlement. Accordingly, Article II NYC must be interpreted in the light of the case law interpreting both the NYC and ML, and the provisions in the Model Law in Electronic Commerce (EML) which have been adopted by both Danubia and Equatoriana.

It has long been established that the interpretation of Article II NYC goes beyond the wording and also includes other types of telecommunications.¹⁸ The NYC was signed in 1958, a time when telegrams was the most modern form of communication and the drafters of the Convention could not possibly have foreseen the means of communication which would be applied in international transactions in the future. Accordingly, the NYC has been given an interpretation by national judges and arbitrators going beyond its wording in order to adapt to commercial reality.¹⁹ For instance, in *Bomar Oil v. ETAP*, an exchange of telexes were found to fall within the scope of Article II NYC.²⁰

This view has also been expressed in the Article 7 (2) of the ML, which has been modeled on Article II NYC.²¹ An agreement is in writing if it is contained in "... an exchange of letters, telex, telegrams or other means of telecommunication which provide a record of the agreement...". It must be noted that this provisions in the ML was also meant by the drafters to extend to Article II NYC, since it had been acknowledged that the formulation in Article II NYC was not up to date with commercial practice.²²

Moreover, the EML, which has been adopted by both Danubia and Equatoriana,²³ states that "[w]here the law requires information to be in writing, that requirement is met by a data message if the information contained therein is accessible so as to be usable for subsequent reference".²⁴ UNCITRAL's Working Group on Arbitration has expressly stated that Article II

¹⁷ See Claimant's e-mail of 5 April 1999, Exhibit No. 3.

¹⁸ See YCA (1994), vol. XIX, at 512, and *Sanders, Pieter* (1999), 'Quo Vadis Arbitration', Kluwer Law International, The Hague, Netherlands, at page 101.

¹⁹ Thirty-second session of the UNCITRAL Working Group on Arbitration, see Report of the Secretary-General, A/CN/WG.II/WG.110, 22 September 2000.

²⁰ *Bomar Oil NV v. ETAP*, Cour de Cassation, 9 November 1993, YCA 1995, vol. XX, pp. 660-662. See also *decision Austrian Supreme Court* 17 November, YCA 183.

²¹ *Kaplan* (1996), and *Sanders* (1999), page 101, and *Holtzmann, Howard M./Neuhaus* (1989), at 260, First Secretariat Note A/CN.9/207, paragraph 40, and First Working Group Report, A/CN.9/216 paras. 22-23.

²² *Holtzmann/Neuhaus* (1989), pp.262-263.

²³ See Clarification Answers, Procedural Order No. 1, question 2.

²⁴ Article 6 (1), Model Law on Electronic Commerce.

NYC should be interpreted to cover the use of electronic means as defined in EML.²⁵ Accordingly, the Working Group has also proposed a revised Article 7 (2) ML which includes electronic messages.²⁶ In addition, the Working Group has issued a draft proposal to issue a recommendation to signatory states of the NYC to interpret the NYC in accordance with the proposed revised Article 7 (2).²⁷

As "electronic mail" is explicitly enumerated as a form of data message in Article 2 EML, it must be concluded that the e-mails exchanged between the parties are to be equivalent to messages "in writing". Moreover, the attachment of the CoP to the e-mail of 5 April falls within the definition of Electronic Data Interchange (EDI) in Article 2 EML, since the electronic document generated in Claimant's computer was transferred to Respondent by e-mail. As data messages may also be interchanged through EDI,²⁸ the CoP must also be considered to be "in writing" according to Article II NYC.

1.1.3.2 There was an exchange of communications between the parties according to Article II (2) New York Convention

As regards the requirements for an "exchange of communications" under Article II NYC, it is general practice that a communication incorporating an arbitration clause by one party must be followed by a communication from the other party which together lay down the terms and conditions for the main contract.²⁹ However, as in present case the arbitration clause is not included as such in the exchange of communications, this rule must be combined with the rules on incorporation of arbitration clauses by reference to general conditions.³⁰ Thus, the *reference* to the general conditions must be contained in an "exchange of communications".

Article II NYC does not expressly refer to the case of incorporation by reference of arbitration clauses. Nevertheless, in *Tradax*,³¹ it was established that incorporation by reference of an arbitration clause meets the formal requirements under Article II NYC even though the reference does not specifically refer to the arbitration clause but only to a text such as standard conditions. However, the Court explicitly held that it had to consider whether the party, which had entered into the agreement was a "seasoned" businessman or a party with little experience. As the parties were familiar with the terms referred to in the case, which were used in their line of business, the Court upheld the formal validity of the arbitration clause.

Subsequently, in *Société Bomar*,³² it was held that a party may accept an arbitration clause incorporated in separate document referred to if that party was aware of the contents of the document at the conclusion of the contract. This requirement implies that the recipient must be in such a position as to be able to check the reference.³³ However, in order for this rule to apply it is also required that the reference is clear and unambiguous as regards the inclusion of

²⁵ See A/CN.9/468 para. 101.

²⁶ See also Report of the Secretary-General (September 2000), see Draft paragraph (2) at page 7.

²⁷ Report of the Secretary-General (September 2000), at 19.

²⁸ Article 2 EML

²⁹ *Van den Berg, Albert Jan* (1981), 'The New York Convention of 1958', Deventer, Antwerp, Boston, London, Frankfurt, at page 199.

³⁰ *Berger* (1993), at page 150.

³¹ Decision of the Swiss Federal Supreme Court, BGE 110 II 54 (*Tradax*), YCA (1986), vol. XI, at 536.

³² *Bomar Oil NV v. ETAP*.

³³ *Rubino-Sammartano, Mauro* (1990), 'International Arbitration Law', Kluwer Law and Taxation Publisher, the Netherlands, at page 124 and *Berger* (1993), at page 153.

the contents of the separate document in the terms of the contract.³⁴

These requirements are met in the present case. First, Claimant submits that Respondent is an experienced merchant, aware of the practice of arbitration clauses incorporated in general conditions, and thus the inclusion of the Arbitration Clause in the CoP cannot have been a surprise for Respondent. In addition, as it has been established in the facts, Respondent itself made use of a dispute settlement clause incorporated in its General Conditions of Sales. Thus, the requirement laid down in *Tradax* is fulfilled.

Secondly, the first exchange of communications took place through the e-mails of 2 and 5 April.³⁵ The wording of the e-mail of 5 April does not leave any room for another interpretation than that the conditions were to be included in the contract. It is stated that "I have attached our General Conditions of Purchase, which *are part of our purchase order*" [emphasis added].³⁶ Accordingly, the reference was clear and unambiguous.

Moreover, Respondent was put in such a position that the Conditions of Purchase including the Arbitration Clause could easily have been controlled and retrieved. The attachment to the e-mail of 5 April must have upon reception been stored in Respondent's hard disc. Consequently, Respondent was in possession of a copy of the conditions as they were at the time of the conclusion of the contract. In fact, Respondent opened the attachment containing the CoP, and must therefore have been aware of the arbitration clause.³⁷ Subsequently, Respondent confirmed the receipt of this purchase order and communicated that it was making arrangements for the shipping.³⁸ Both e-mails contain elements forming part of one or two contracts between the parties. It follows that there was an exchange of communications containing a valid reference to the CoP and the Arbitration Clause.

Thirdly, in the second exchange of communication,³⁹ Claimant states in its e-mail that "[s]ince you *already have a copy* of our General Conditions of Purchase, I need not *attach them to this order*" [emphasis added].⁴⁰ The implied meaning of this sentence is unambiguous. The word "attach" implies that the Conditions of Purchase were an integrated part of the order, which under normal circumstances in negotiations with a new customer would had been attached to the order so it could have been examined by the recipient. However, in this order it was not necessary, since Respondent was already in possession of the Conditions of Purchase and thus Claimant could only refer to them.

Furthermore, as Respondent was already in possession of the CoP, they could be controlled and retrieved as easily as following the first exchange. In addition, Respondent confirmed this order in its subsequent e-mail and referred explicitly to the order number PO 6910. Again, the two e-mails between the parties became part of one or two contracts between the parties. Thus, the e-mails constitute a valid exchange of communications incorporating an arbitration agreement through reference to general conditions. On these grounds, the formal requirements under Article II (2) NYC are met by the Arbitration Clause in dispute.

³⁴ Decision of the *Geneva Court of Appeal* of 16 December 1988, YCA 1991, at page 612. See also *Berger* (1993), at page 154. See also *Craig/Park/Paulsson*, at 95.

³⁵ Exhibits no. 2 and 3.

³⁶ Respondent's e-mail of 5 April 1999. See Exhibit No. 3.

³⁷ Clarification Answers, Procedural Order no. 1, Question no. 36.

³⁸ Respondent's e-mail of 6 April 1999, Exhibit no. 4.

³⁹ E-mails of 27 and 28 May, Exhibits no. 5 and 6.

⁴⁰ See Claimant's e-mail of 27 May 1999. Exhibit No.5.

I.2 The Arbitration Clause constitutes a valid arbitration agreement between the parties

Claimant contends that CISG applies to the Arbitration Clause as regards the substantive validity of the arbitration agreement (I.2.1). Notwithstanding whether the parties concluded one or two contracts, the Arbitration Clause constitutes a valid arbitration agreement pertinent to the whole dispute. There is no valid arbitration agreement in the first contract (I.2.2). The second agreement incorporates the Arbitration Clause in the contract and extends to the first contract (I.2.3). In the alternative, the two orders constitute one contract which has been modified by the second agreement incorporating the Arbitration Clause (I.2.4).

I.2.1 The CISG determines whether there is a valid arbitration agreement between the parties

As previously established in (I.1.1.), the parties have agreed that the CISG is applicable to the merits of the dispute in accordance with Article 17 ICCRA.⁴¹ Accordingly, the CISG should also determine whether there was an agreement between the parties as regards the incorporation of the Arbitration Clause into the contract as the CISG specifically deals with the formation of contracts and the consent of parties.

In international arbitral practice, the *lex contractus*, generally, also governs the substantive validity of the arbitration clause.⁴² This rule has, generally, only been sidestepped in cases where the parties omitted to make an explicit choice of the law applicable to the main contract.⁴³ Derogation from this rule must be considered to be exceptional.⁴⁴ In addition, the NYC states that an award may be denied enforcement if "the said agreement is not valid under the law to which the parties have subjected it" and thus further supports this view.⁴⁵

In *Filanto v. Chilewich*, the Court held that in examining whether there was an agreement between the parties it would make that assessment "in light of, and with reference to, the substantive international law of contracts embodied in the Sale of Goods Convention."⁴⁶

Hence, CISG is applicable to the substantial validity of the Arbitration Clause.

I.2.2 There is no valid arbitration agreement between the parties in the first contract

I.2.2.1 The Effective offer was made by Claimant on 5 April 1999

According to Article 14(1) CISG, "[a] proposal for concluding a contract addressed to one or more specific persons constitutes an offer if it is sufficiently definite and indicates the intention of the offeror to be bound in case of acceptance". Accordingly, the key components in an offer are specificity, definiteness and an indication to be bound.⁴⁷

⁴¹ See Request for Arbitration, paragraph 22, and Answers to Request for Arbitration, paragraph 19.

⁴² *ICC Award in Case No. 2626 and Oberlandesgericht Hamburg* September 22, (1978), *Rass. Arb.* 1979, at 271 (No.94) in *Rubino-Sammartano* (1990), at page 141.

⁴³ See for instance *ICC award No. 5066*, 1986.

⁴⁴ *Rubino-Sammartano* (1990), at page 142.

⁴⁵ Article V (a) NYC and *Berger* (1993), at 157.

⁴⁶ *Filanto S.p.A., v. Chilewich International Corp.*

⁴⁷ *Bernstein, Herbert and Joseph Lookofsky* (1997), 'Understanding the CISG in Europe: A compact Guide to the 1980 United Nations Convention on Contracts for the International Sale of Goods', page 33.

All three key components for an offer are met in Claimant's purchase order of 5 April.⁴⁸ This offer was aimed specifically at Respondent and not to the public. Thus, it fulfills the specificity requirement.

Secondly, it has to be assessed whether the offer was sufficiently definite by indicating the goods and expressly or implicitly fixing the price.⁴⁹ Accordingly, the Purchase Order No. 6839 specified the ordered goods and it is stated in the e-mail that the total sum of the purchase is \$ 100 000. This communication explicitly sets both the quantity and the price. In contrast, the previous e-mail sent by Respondent,⁵⁰ cannot be considered as an offer, since the price list only sets the price per item and does not determine the total price or the quantity of each item.⁵¹ Price lists, even in the case when they are directed to a specific group of customers, are only considered to be invitations to treat.⁵²

Thirdly, it is clear that Claimant intended to be bound by an acceptance following the Purchase Order. This conclusion follows from the fact that Claimant asks explicitly in the e-mail for the shipping costs *only* for the purpose of performing the contract.⁵³

Hence, Claimant made the effective offer on 5 April 1999.

1.2.2.2 The Contract was formed when Claimant opened its letter of credit and neither of the Parties' General Conditions prevail

The CISG applies the mirror-image rule or the "battle of forms".⁵⁴ This "last shot" principle is expressed in Article 19 (1) CISG stating that a "reply to an offer which purports to be an acceptance but contains additions, limitations or other modifications is a rejection of the offer and constitutes a counteroffer".

However, in cases when the parties make reference to contradictory terms, the CISG's "last-shot principle" does not provide an acceptable solution, since a party may use Article 19 (3) to use divergent terms in order to escape a performed contract which has become disadvantageous.⁵⁵ In such cases, it must be concluded that the parties place less weight to their General Conditions than the part of the contract which has *actually* been performed. It follows that the *essentialia negotii* should first be established between the parties, e.g. the performed part of the contract. Secondly, it must be presumed that the parties have waived the application of their conflicting terms through the non-application of Article 19, in accordance with the autonomy of the parties under Article 6 CISG.⁵⁶

Claimant contends that this rule must be applied in the case at hand. As stated previously in (I.2.2.1), the effective offer was made in Claimant's e-mail of 5 April 1999. Respondent rejected this offer through the e-mail of 6 April 1999.⁵⁷ As conditions regarding dispute

⁴⁸ Claimant's e-mail of 5 April 1999, Exhibit no. 3.

⁴⁹ *Bernstein/Lookofsky* (1997), page 33.

⁵⁰ Respondent's e-mail of 2 April 1999, Exhibit no. 2.

⁵¹ *Schlechtriem* (1998), Article 14, paragraph 2-3, at pp. 105-106 and 108-110.

⁵² *Schlechtriem* (1998), Article 14, paragraph 4, at page 111.

⁵³ Claimant's e-mail of 5 April 1999, Exhibit no. 3.

⁵⁴ *Bernstein/Lookofsky* (1997), page 41, and *Schlechtriem* (1998), Article 19, paragraph 20, at page 144.

⁵⁵ *Schlechtriem* (1998), Article 19, paragraph 20, at pp. 144-145.

⁵⁶ Decision 6 October 1995, *AG Kehl* and *Schlechtriem* (1998), Article 19, paragraph 20, at 145.

⁵⁷ Respondent's e-mail of 6 April 1999, Exhibit no. 4.

settlement constitute a material part of a contract according to Article 19 (3) CISG, the inclusion of Respondent's jurisdiction clause through Respondent's General Conditions of Sales makes the e-mail a rejection of Claimant's offer and thus constitutes a counter-offer under Article 19 (1).

Claimant did not respond to this counter-offer. According to Article 18 (1) CISG, silence or inactivity does not constitute acceptance. The first activity by the parties after the e-mail of 6 April occurs when Claimant opens its letter of credit and thus commenced performance. As Claimant explicitly had referred to its General Conditions of Purchase, it cannot be argued that this amounted to an implied acceptance of Respondent's Conditions of Sales. Both parties indicated their will of including their own General Conditions. It follows that the last-shot principle does not give an acceptable solution to the problem. Thus, the only reasonable solution would be to conclude that the parties have waived the application of Article 19 in relation to the general terms under Article 6 CISG.

Hence, neither Respondent's nor Claimant's General Conditions form part of the agreement. There is no arbitration agreement for this contract.

I.2.3 The Arbitration Clause constitutes a valid arbitration agreement in the second contract which extends to the first contract

A second contract was concluded by the parties the 28 May 1999. Moreover, as the second contract or the modification is governed by the Arbitration Clause, this valid arbitration agreement also extends to the first contract.

As previously stated in **I.2.2.1**, the key components in an offer under Article 14 CISG are specificity, definiteness and an indication to be bound.⁵⁸

In the e-mail of 27 May, Claimant sent a purchase order specifying goods of a value of \$500,000 to Respondent.⁵⁹ In addition, Claimant stated that "[s]ince you *already have a copy* of our General Conditions of Purchase, I need not *attach them to this order*" [emphasis added].⁶⁰ As previously concluded, this statement unambiguously indicates Claimant's intention to include its General Conditions of Purchase in this second contract. Moreover, as this order specifies the goods, quantity and price, it meets the requirements for an offer under Article 14 CISG and, in addition, incorporates the Arbitration Clause contained in the General Conditions of Purchase into the contract.

Respondent accepted this offer in its e-mail of 28 May 1999. A thorough analysis of that e-mail clearly indicates an acceptance by Respondent. First, Respondent acknowledges the second order. Secondly, Respondent makes a calculation of the total costs, including the shipping costs, so that Claimant may establish a letter of credit. Finally, Respondent concludes by stating that "[y]ou can expect the goods to be shipped by 20 June 1999."⁶¹

All these factors taken into consideration together express Respondent's intention to accept the offer. Especially the setting of date of delivery indicates that Respondent saw its response as concluding a final contract. Accordingly, Respondent has indicated its intention to be

⁵⁸ *Bernstein/ Lookofsky* (1997), at page 33.

⁵⁹ E-mail of Claimant of 27 May 1999, Exhibit no. 5.

⁶⁰ E-mail of Claimant of 27 May 1999, Exhibit no. 5.

⁶¹ E-mail of Respondent of 28 May 1999, Exhibit no. 6.

bound and given an explicit assent to Claimant's purchase order of 27 May 1999 according to Article 18 (1) CISG. As the General Conditions of Purchase were incorporated through reference in the offer which Respondent accepted, the Arbitration Clause forms an arbitration agreement between the parties.

As no valid arbitration clause governs the first contract (see **I.2.2**), the valid arbitration agreement between the parties in the second contract extends to the first contract. In an Award by the Bulgarian Arbitral Tribunal, it was held that a contract was so connected to another contract containing an arbitration clause, that the latter was applicable to both contracts.⁶²

Similarly, in this case the dispute concerns connected contracts. The claims regarding both contracts arise from the same factual and legal basis as they concern the two purchase orders⁶³ and Respondent's fundamental breach. Furthermore, Respondent, apparently, agrees in respect of this conclusion when seeking relief by basing its calculation on both orders.⁶⁴ Thus, the contracts are so connected that it would be unreasonable to exclude the first contract from the dispute over the second contract. Moreover, it would be uneconomical for both parties to have two concurrent litigation proceedings before two different courts.

Accordingly, the Arbitration Clause incorporated in the second agreement extends to the first agreement. On these grounds, the Arbitration Clause constitutes a valid arbitration agreement between the parties and the Tribunal has jurisdiction.

I.2.4 In the alternative the second agreement modifies the first contract and incorporates a valid arbitration agreement between the parties

Nevertheless, should the Tribunal hold that only one contract exists between the parties, the second agreement between the parties constitutes a separate agreement of modification of the first contract incorporating the Arbitration Clause.

According to Article 29 (1) CISG "[a] contract may be modified or terminated by the mere agreement of the parties". Thus, the modification constitutes a *separate* agreement to modify the contract which is governed by the provisions regarding offer and acceptance in CISG.⁶⁵

Claimant modified the contract by the additional order contained in the e-mail of 27 May 1999. The e-mail explicitly states that "we [Claimant] would like to make our *initial* purchase larger than anticipated".⁶⁶ Consequently, Claimant expressed its will to modify the quantity and price of the first order by an additional order of a value of \$ 500 000. In addition, Claimant also included a reference to its General Conditions of Purchase, which formed part of the modification offer. Accordingly, as Claimant has previously established that the offer meets all the requirements of Article 14 CISG,⁶⁷ the offer constitutes a valid offer of modification under Article 29 CISG.

Respondent has confirmed this conclusion in its acceptance by stating in the following e-mail

⁶² Award October 1, 1980, in proceedings No. 60/1980, YCA 1987, vol. XXI, at page 84 in *Rubino-Sammartano* (1990), at page 181.

⁶³ Clarification Answers, Procedural Order No. 1, Question No. 45.

⁶⁴ Answer to Request for Arbitration, paragraphs 8-11.

⁶⁵ *Schlechtriem* (1998), Article 19, paragraph 20, at 211.

⁶⁶ See Exhibit no.5.

⁶⁷ As set out above under **I.5.1.1**.

that "we have treated your purchase *orders* as *one* purchase [emphasis added].⁶⁸ In addition, Respondent gave an 8% discount on the total quantity of goods comprised by both orders. Hence, it is clear that Respondent saw the two purchase orders as one. In addition, Respondent, in its Answer to Request for Arbitration, also acknowledged that "[b]oth parties treated the two shipments as a single contract...".⁶⁹ As stated in **(I.2.3.)**, Respondent's reply amounted to an acceptance to this offer of modification.⁷⁰

In addition, Respondent's acceptance extends to the reference to Claimant's General Conditions of Purchase, which were included in the offer of modification. Respondent's argument that their General Conditions of Sales would apply to the second purchase order lacks legal ground in CISG.⁷¹ Respondent did not reject Claimant's offer of modification or attempt to include their General Conditions of Sale in a counter-offer according to Article 19 (1) and (3) CISG. Moreover, an argument based on waiver by the parties of the application of Article 19 CISG is futile, since there are no contradictory terms in the modification contract. The terms referred to previously have no effect, since they were pertinent to the first contract. If Respondent wanted to include its terms in the modification, it would have included those in the reply to Claimant's modification offer. Consequently, Respondent accepted the offer of modification as proposed in the e-mail of 27 May as prescribed in Article 18 (1) CISG.

Consequently, Respondent is making contradictory statements. On the one hand Respondent accepted the offer of modification and benefited from it, while on the other hand it disputes that an arbitration agreement was concluded between the parties. In *Filanto v. Chilewich*, the attempt of a party to rely on the benefits of the same agreement, which it later disputed, indicated the party's possible assent to the agreement.⁷² Thus, Respondent's behavior must be seen as a dishonest attempt to stall and evade the current proceedings, which are *per se* a result of Respondent's breach of contract.

In conclusion, the Arbitration Clause constitutes a valid arbitration agreement between the parties and the Tribunal has jurisdiction.

II Claimant had the right to avoid the contract

Claimant submits that Respondent committed a breach of contract under Article 42 CISG **(II.1.)**. This breach amounted to a fundamental breach **(II.2.)**. Thus, Claimant declared the contract avoided **(II.3.)**.

II.1 Respondent committed a breach of contract per Article 42 (1) CISG

Claimant will demonstrate that Respondent failed to deliver goods free from the claim of a third party based on intellectual property, which constitutes a breach of contract per Article 42 (1) CISG **(II.1.1.)**. Claimant gave notice to Respondent within reasonable time after becoming aware of the claim of the third party (Vis Fish Company) **(II.1.2.)**.

⁶⁸ See Exhibit no. 6.

⁶⁹ Answer to Request for Arbitration, paragraph 15.

⁷⁰ As set out above under **I.5.1.1.**

⁷¹ Answer to Request for Arbitration, paragraph 15.

⁷² See *Filanto S.p.A., v. Chilewich International Corp.*

II.1.1 Conditions establishing Respondent's liability are fulfilled

Article 42 (1) CISG provides the duty of the seller to deliver goods, which are free from any right or claim of a third party based on industrial property or other intellectual property. Notwithstanding Respondent's contrary allegations⁷³ Claimant submits, that Respondent breached the contract by failing to perform its obligation stipulated in Article 42 CISG (II.1.1.1.). Moreover, Respondent could not have been unaware of the third party claim (II.1.1.2.). Respondent is not exempted under Article 42 (2) CISG (II.1.1.3.).

II.1.1.1 Respondent did not deliver goods which were free from a third party claim

It is undisputed that trademarks are protected as an intellectual property right and accordingly fall under the scope of Article 42 CISG.⁷⁴ It is also widely accepted that Article 42 CISG does not require the claim of the third party to be founded.⁷⁵ This follows from the aim of this provision, which is to protect the buyer against having to face a third party's claim, since such litigation would be costly and time-consuming. The literal interpretation supports the view that unfounded claims are also covered by the liability under Article 42 CISG, otherwise the word "rights" would be superfluous.

However, Claimant acknowledges that a minimum level of seriousness is required⁷⁶. The seriousness of the third party claim was established in the legal opinion of Howard & Heward ascertaining the fact that Vis Fish trademark was registered for all water related goods⁷⁷ and that this broad scope registration of the trademark was possible under Danubian law. Furthermore, a start of litigation by the third party is not required to establish a breach of Article 42.⁷⁸ Thus, Respondent failed to deliver goods that were free from a third party claim.

II.1.1.2 Respondent could not have been unaware of the third party claim

Respondent could not have been unaware of the third party claim since it had the obligation to inquire about the legal situation concerning registered trademarks before concluding an international sales contract⁷⁹. If such an obligation did not exist, the protection for the buyer would be surely diminished since the seller could always defend himself with the claim that he had no knowledge of the trademark. The liability of the seller would be restricted to cases dealing with well-known trademarks only. Furthermore, it is reasonable for the seller to assess the legal situation before entering a new market.

⁷³ Answer to the Request for arbitration, II.4.

⁷⁴ cf. art. 2 (viii) of the Convention Establishing the World Intellectual Property Organization (1967); *Achilles, Wilhelm-Albrecht*, Kommentar zum UN-Kaufrechtsuebereinkommen (CISG), 2000, Art. 42, No. 2.

⁷⁵ *Schlechtriem-Schwenzer* (1998) Art. 42, No. 6 *Enderlein-Maskow-Strohbach*, Internationales Kaufrecht, Berlin 1991, Art. 42, No. 2; *Magnus in: von Staudinger*, Kommentar zum Buergerlichen Gesetzbuch mit Einfuehrungsgesetzen und Nebengesetzen, Wiener UN-Kaufrecht (CISG), Berlin 1999, Art. 42, No. 13; *Vida*, RTD com. (1994), p. 32.; *Honnold*, Uniform Law for International Sales, Deventer 1991, Art. 42, § 270 referring to Art. 41 § 266: "...should protect the normal expectation of a buyer that he is not purchasing a lawsuit".

⁷⁶ Secretariat Commentary 1978, Art. 39 (now Art. 41), No. 10; *Heilmann*, Maengelgewaehrleistung im UN-Kaufrecht, Berlin 1994, p. 660; *Herber/Czerwenka*, Internationales Kaufrecht, Muenchen 1991 Art. 41, No. 6.

⁷⁷ See Procedural Order No.I. Q.7, The Vis Fish trademark is registered for class 28 which includes sports fishing equipment.

⁷⁸ *Rauda/Etier*, Warranty for Intellectual Property Rights in the International Sale of Goods in: *Vindobona Journal* (2000), pp. 30-61, p. 36; *Achilles* (2000) Art. 42, No 3 referring to Art. 41, No. 3; *Magnus*, Art. 42, No. 7 in: *Honsell*, Kommentar zum UN-Kaufrecht, Berlin, Heidelberg 1997.

⁷⁹ *Rauda/Etier* (2000), p. 44; *Schlechtriem*, Einheitliches UN-Kaufrecht, Tuebingen 1996, p. 65; *Staudinger-Magnus* (1999) Art. 42, No. 22; *Piltz* Internationales Kaufrecht, Das UN-Kaufrecht (Wiener Uebereinkommen von 1980) in praxisorientierter Darstellung, Muenchen 1993, § 5 No. 109; *Herber/Czerwenka* (1991) Art.42. 5.

Moreover, the Secretariat's Commentary confirms that the seller is always liable under Article 42 CISG if the intellectual property right in question has been published.⁸⁰ However, the seller's duty to perform such a search is restricted to specific territories, in this case Danubia, as provided by Article 42 (1) (a) and (b) CISG. It is obvious from the facts of the present case that Respondent's liability cannot be restricted since the parties had agreed that the goods would be resold in Danubia. Furthermore, Respondent had the intention to enter the Danubian market even before the contract was concluded. This interest is reflected by the fact that it was Respondent who initiated the negotiations by referring to its web site in an announcement. Therefore, even if one disagreed with the existence of a general duty to search, in this situation the seller had the obligation to make the legal inquiries concerning trademark infringement.⁸¹ Respondent also raised Claimant's confidence in its knowledge about the market situation when it offered an exclusive dealership for its goods⁸².

Accordingly, Respondent had the obligation to investigate whether there was a conflicting trademark in the Danubian market. Respondent did not perform this obligation. If it had, the registration of Vis Fish would easily have been found.⁸³ To conclude, Respondent's failure to perform its obligation under Article 42 was a breach of the contract.

II.1.1.3 Respondent is not exempted under Article 42 (2) CISG

Article 42 (2)(a) CISG exempts the seller from its liability only when the buyer knew or could not have been unaware of the right or claim. Clearly, Article 42 (1) CISG provides an obligation for the seller to inquire the legal situation concerning published rights therefore it follows that the buyer does not have the same duty⁸⁴. Otherwise the seller would never be liable pursuant to Article 42 CISG. Moreover, the seller is in a better position to assess whether an infringement could arise, as it has a more thorough knowledge of its own products than the buyer. It is appropriate therefore, to burden the seller and not the buyer with the duty of search. The buyer only loses its right to rely on Article 42 (1) CISG if it has clear indications for a right of the third party, e.g. concerning well-known trademarks.⁸⁵

In the present case, Claimant was aware of the existence of Vis Fish Company, but it did not have knowledge about the existence and the extent of Vis Fish's trademark registration. Therefore, Claimant could not have been reasonably expected to know that a trademark infringement might be possible. The sport goods ordered from Respondent and the food products sold by Vis Fish are *prima facie* distinct enough to lead Claimant to believe that no infringement of the trademark of Vis Fish was involved. Furthermore, as Claimant had no duty to perform a trademark search, it was not in the position to find the registration of Vis Fish. Thus, Claimant meets the requirements laid down in Article 42 (2) CISG as it was and reasonably could have been unaware of the third party claim at the time of the conclusion of the contract.

⁸⁰ Secretariat Commentary 1978, No. 6; *Langenecker* (1994), p. 181.

⁸¹ Cf. *Heuzé*, *La vente internationale de marchandises-Droit uniforme*, No. 316, Paris: Joly (1992), who differentiates which party has taken the first step. This party has the duty to investigate the legal position.

⁸² Claimant's exhibit No. 2.

⁸³ Clarification No. 21.

⁸⁴ *Schlechtriem-Schwenzer* (1998) Art. 42, No. 17; *Enderlein/Maskow/Strohbach* (1991) Art. 42, No. 9; *Staudinger-Magnus* (1999) Art. 42, No. 26; *Herber/Czerwenka* (1991) Art. 42, No. 6.

⁸⁵ *Rauda/Etier* (2000) p. 56; *Achilles* (2000) Art. 42, No. 11; *Staudinger-Magnus* (1999) Art. 42, No. 26.

II.1.2 Claimant gave notice within a reasonable time

Claimant can rely on his right under Article 42 CISG since it gave notice to Respondent within a reasonable time as stipulated in Article 43 (1) CISG (II.1.2.1.). However, should this Tribunal find the notice untimely, Respondent cannot invoke Article 43 CISG as it has waived and forfeited its right to object that the notice was not given timely (II.1.2.2.).

II.1.2.1 Claimant's notice was given timely

Claimant's notice was in compliance with the requirements laid down in Article 43 (1) CISG, which provides that the buyer loses the right to rely on Article 42 if the notice was not given within a reasonable time after the buyer has become aware or ought to have become aware of the right or claim. Claimant stipulates that it became aware of the third party claim on 28 October 1999 after Howard & Heward gave its legal opinion. Although Claimant was first contacted by the third party on 20 September 1999⁸⁶, this date did not mark the beginning of the time limit as defined by Article 43 (1) CISG. As demonstrated in II.1.1.1., the third party claim has to have a certain level of seriousness to establish a breach under Article 42 CISG. According to Claimant's evaluation after the first letter of Vis Fish, the claim was frivolous. Thus, Claimant acted in the light of its assessment when it contacted the third party to rebut the claim⁸⁷. However, after receiving third party's response repeating its claim, Claimant sought legal advice to establish the frivolous nature of that claim. Bearing in mind the different nature of the products in dispute, Claimant's assessment as to the frivolity of the third party claim was reasonable. Consequently, due to its lack of legal expertise, Claimant was not aware and could not have been aware that there was a sufficiently serious claim as required by Article 42 CISG,. Therefore, Claimant became aware of a third party claim as required by Article 42 CISG for the first time after receiving the legal opinion on 28 October 1999⁸⁸. The time period stipulated in Article 43 (1) CISG began on that date⁸⁹. On 3 November 1999, 6 days after becoming aware of the claim, Claimant gave notice to Respondent. In the light of court decisions concerning Article 39 CISG, which also operates with the criterion of "reasonable time", Claimant concludes that its notice must be considered to be within this time limit, even in comparison with the most stringent standards.⁹⁰

Nevertheless, should this Tribunal arrive to the conclusion that the time period began on 20 September 1999, Claimant argues in the alternative that the notice was given within a reasonable time (6 weeks). The criteria of measurement of "reasonable time" have been established in the case law dealing with Article 39 CISG. The trend in case law points to the development of a general time limit of 1 month⁹¹ notwithstanding the fact that "reasonableness" depends on the circumstances of the specific case⁹². Claimant contends that the time limit associated with Articles 38 and 39 CISG should be longer than the time limit stipulated in connection with Article 43 CISG. This is based on the fact that assessing third

⁸⁶ Exhibit No. 7.

⁸⁷ This assessment is clearly reflected in Claimant's letter on 4 October 1999, Exhibit No. 8.

⁸⁸ Exhibit No. 10.

⁸⁹ The beginning of the time limit after establishing the seriousness of the claim is confirmed in:

Enderlein/Maskow/Strohbach (1991) Art. 43, No. 2; *Soergel/Luederitz* (1991), *Buergerliches Gesetzbuch mit Einfuehrungsgesetzen und Nebengesetzen*, 12edition, Art. 43, No. 2.

⁹⁰ *LG Stuttgart* RIW 1989 pp. 984 ; *OLG Düsseldorf*RIW 1993 pp. 325;

⁹¹ *BGHZ* 129, 85f.; *OG Luzern*, SJZ 1998, 515, 518; *Cour d'Appel Grenoble*, J.D.I. 1996, 948ff.; *OLG Stuttgart* RIW 1995 pp. 943; *OLG Köln*, OLGR Köln 1998 pp.2.

⁹² *Hungarian Chamber of Commerce and Industry, Court of Arbitration*, Award of 5 December 1995, cf. [Pace CISG Database], *Andersen, Camilla Baasch*, Reasonable Time in Article 39 (1) of the CISG - Is Article 39 (1) Truly a Uniform Provision?, p. 36ff. cf. [Pace CISG Database] 1999; *Achilles*, Art. 43, No. 5.

party claims is a lengthier procedure than examining the conformity of goods, since the former lies outside the buyers' expertise to evaluate the seriousness of such claims. Therefore, it is widely accepted that an appropriate reaction is to investigate the legal situation by consulting for legal advice⁹³. Thus, the time limit of Article 43 is longer than the accumulated time limits of Article 38 (examination of conformity of goods) and Article 39 (notice of non-conformity). Furthermore, in the present case there was no reason to act immediately since Respondent was not threatened to lose any rights.⁹⁴ Consequently, even after 6 weeks the notice was given within a reasonable time and therefore Claimant can rely on Respondent's liability under Article 42 CISG.

II.1.2.2 Waiver and forfeiture by Respondent

Should the Tribunal find that the notice was not given within a reasonable time, Claimant submits that Respondent lost its right to invoke Article 43 CISG on two legal grounds.

According to case law, a party may implicitly waive its right to object the timeliness of a notice.⁹⁵ The implied waiver of the right to rely on Article 43 must be concluded from Respondent's conduct. It is clear from Respondent's answer to the notice that it did not contest that there was a breach of contract, as it only contested whether it purported to fundamental breach. Respondent's offer to reimburse all reasonable costs of a possible litigation supports the conclusion that Respondent has admitted its failure to fulfill the obligations prescribed by Article 42 CISG. Respondent thereby accepted its liability under Article 42 CISG unconditionally, even in the case that notice was not given within a reasonable time.

Secondly, Respondent forfeited its right to object to the reasonableness of the time within which the notice was given⁹⁶. Respondent received the notice of Claimant on 5 November 1999. However it only objected to its timeliness in its Answer to the Request for Arbitration, on 10 July 2000. Bearing in mind that Respondent had already accepted its liability under Article 42 CISG, the objection first raised more than 8 months after receiving Claimant's notice is clearly contradictory. Thus, Respondent has forfeited its right under Article 43 CISG.

II.2 The requirements for avoidance under Article 49 (1)(a) CISG are met due to a fundamental breach by Respondent

Claimant had the right to avoid the contract under Article 49 (1)(a) CISG, since the breach of Article 42 CISG by Respondent amounts to a fundamental breach according to Article 25 CISG. Accordingly, Respondent will demonstrate in the following that the conditions under Article 25 CISG are met. First, there was such a detriment caused by Respondent's breach as to substantially deprive Claimant of what it was entitled to expect under the contract (**II.2.1**).

⁹³ Piltz (1993) § 5, No. 116; *Staudinger-Magnus* (1999), Art. 43, No. 26; *Achilles* (2000) Art. 43, No.5; *Schlechtriem/Schwenzer* (1998) Art. 43, No. 3;

⁹⁴ *Staudinger-Magnus* (1999) Art. 43, No. 21; *Vida*, RTD com 1994, 32; *Piltz* (1993) § 5 No. 116;

⁹⁵ *BGH* RIW 1997, 1037, 1038; *BGH* IPRax 1999, 377, 378f.; *Schlechtriem/Schwenzer* (1998) Art. 39, No. 33.

⁹⁶ The possibility of a forfeiture was accepted by the *Arbitral Tribunal - Vienna, 15 June 1994*, RIW 1995, 590ff.: "A given legal position (e.g. a right, a defense, etc.) can not only be intentionally waived but can also be objectively forfeited. This follows from the general principle of good faith and the closely related principle of estoppel (prohibition of *venire contra factum proprium*). Thus, a legal position of a party must be regarded as having been forfeited whenever that party's conduct could be construed as meaning that it no longer wished to exercise its right or its defense, (...)".

Secondly, there was no possibility of cure by neither Claimant nor Respondent (II.2.2). Thirdly, the effects of the breach of contract were foreseeable to Respondent (II.2.3).

II.2.1 The third-party claim by the Vis Fish Co. is a substantial detriment which deprives Claimant of what it was entitled to expect under the contract

It has been established by case law that a breach of contract amounts to a substantial detriment when the purpose of the contract is endangered so seriously that, for the concerned party, the interest in the fulfillment of the contract ceases to exist as a consequence of the breach.⁹⁷ Thus, one must first consider the importance of the interest, which the contract and its individual obligations actually create for the parties. Accordingly, also the breach of an obligation, which is not a primary obligation of the contract, but, rather, a secondary obligation may be, without anything further, fundamental. In the following Claimant will first determine the aim of the contract between the parties (II.2.1.1), and secondly, it will establish that this aim was frustrated through Respondent's breach of contract (II.2.1.2).

II.2.1.1 The Aim of the contract was to sell Respondent's goods in Danubia

Claimant submits that the aim of the contract was to resell Respondent's goods in Danubia at a profit. As established in the facts of the case, Respondent's goods had yet not been sold in Danubia at the time the parties initiated their negotiations. Therefore, Claimant had a clear interest in reselling and promoting them as a novelty in the Danubian market. Claimant is always looking for new brands to promote in order to strengthen its position in the Danubian market.⁹⁸ Furthermore, Claimant had an interest in Respondent's products due to its reputation among retailers of water sports goods.⁹⁹ Importantly, this underlying premise was also explicitly communicated to Respondent, which therefore must have been aware of it.¹⁰⁰ Not only was Respondent aware of this essential aim, but in fact, Respondent was itself pursuing this aim through actively inviting trading partners to resell the goods in Danubia.¹⁰¹ Respondent explicitly stated that "we have long desired to enter that market [the Danubian market]".¹⁰² In addition, Respondent's offer of an exclusive dealership to Claimant confirms the aforementioned aim. Consequently, the parties had clearly defined the aim of the contract. Following from this aim, Respondent had the obligation to deliver goods that were fit for resale in Danubia.

II.2.1.2 The aim underlying the contract was substantially frustrated through Respondent's breach

Claimant contends that the aim underlying the contract was substantially frustrated through Respondent's breach under Article 42 CISG. As a consequence of the breach, Claimant was forced to withdraw the contested goods from the Danubian market for the following reasons. The trademark right of Vis Fish company may either be founded or unfounded. However, Claimant contends that in either situation, it is substantially deprived of what it had expected under the present contract.

⁹⁷ *OLG Frankfurt*, EuZW 1992, p. 352; *BGH RJW* 1997, 1037, 1038.

⁹⁸ Claimant's e-mail of 31 March 1999, Exhibit no. 1.

⁹⁹ This reputation has been established in the Clarification Answers, Procedural Order no. 1, Question no. 25.

¹⁰⁰ Claimant's e-mail of 31 March 1999, Exhibit no. 1.

¹⁰¹ Clarification Answers, Procedural Order no. 1, Question No. 43.

¹⁰² E-mail of 2 April 1999, Exhibit no. 2.

It is clear that a founded trademark claim by Vis Fish Company frustrates the aim of the contract between the parties. The selling of goods burdened by a third party trademark right violates the law. Once Claimant is held to infringe intellectual property rights, it will be ordered by a Court to stop selling the goods. Moreover, Claimant may also face confiscation of the infringing goods, or paying damages to the third party as envisaged in the GATT TRIPs Agreement¹⁰³ to which both Danubia and Equatoriana are parties.¹⁰⁴

Thus, the selling of Respondent's goods in Danubia is impossible which means that the aim of the contract is frustrated.

However, not only the existence of a founded trademark can lead to such consequences that the avoidance of the contract is the only option. As whether the trademark right of the third party is founded can only be decided as a result of a litigation. Thus, Claimant had to assess the likelihood and the possible consequences of that litigation. Following this assessment, Claimant had to arrive to the conclusion, that this uncertain legal situation, in itself constitutes a substantial detriment to Claimant in the light of the aim of the contract.

The likelihood of the litigation was ascertained in the legal opinion of Howard & Heward.¹⁰⁵ The underlying reasons for this conclusion were based on the fact that the Vis Fish Company has aggressively defended its trade mark rights in the past.¹⁰⁶ In two previous cases, the threat of litigation has proven to be so overwhelming for the involved companies that they chose to settle the dispute prior to court proceedings. Notably, in one of these cases the disputed goods was playground equipment, which is not only comparable to the goods in the present case but also falls within the same trademark class as Respondent's goods.¹⁰⁷ Considering these facts, Claimant could only arrive to the conclusion that the threat was substantive and the litigation was the most likely outcome. After establishing that litigation was almost inevitable in the given situation, Claimant had to consider the possible consequences of those proceedings.

First, the use of interim measures is always a possibility at the beginning of such litigation. Whether interim measures are often used in Danubia is not relevant, since it is a decision taken by the judge, and therefore cannot be predicted by Claimant. As a consequence of the measures, Claimant would be deprived of the possibility of selling the goods and suffer substantial economic loss.

Secondly, once involved in a time consuming trademark litigation Claimant has to face all the adverse effects of the legal proceedings. As the most prominent market player of the Danubian sporting equipment market, Claimant cannot afford to sell goods that are alleged to be burdened with third-party rights. Accordingly, a claim that Claimant is selling goods infringing registered intellectual property rights seriously jeopardizes not only Claimant's reputation but also the everyday flow of business. These allegations would have a significant impact on sales and thus also undermine Claimant's market position. As a retailer, Claimant is highly dependent on its reputation among the consumers and trading partners, who are easily influenced by bad publicity of an alleged involvement in trademark infringement. Hence, Claimant cannot be expected to sell goods, which may destroy its goodwill and reputation.

Thirdly, the uncertainty of the length of the litigation would constitute a detriment to

¹⁰³ Article 50 § 1(a), § 2 and Article 46 of TRIPs agreement

¹⁰⁴ See Procedural Order No. 1. , at Question 4.

¹⁰⁵ Exhibit No. 10.

¹⁰⁶ Letter of Howard & Heward of 28 October, Exhibit no. 10.

¹⁰⁷ Clarifications Answers, Procedural Order no. 1, Question 7 and 14.

Claimant, for example, when planning the future sales orders. Furthermore, though the quality of the goods would not deteriorate as a consequence of storage, they could lose their appeal to the consumers, being out-fashioned.

Eventually, once the litigation is over, Claimant still would have to face further problems. The consequence of a decision which establishes that the trademark was founded has already been demonstrated. Nevertheless, even if the claim were to be judged unfounded, Claimant would not be relieved. In this case, Claimant bears the risk of not being able to recover his full costs (including the lawyer's fees) of the legal proceedings. Such costs, as harm to goodwill and temporary decrease in turnover caused by the litigation, cannot be recovered by Claimant, since the value of such costs is difficult to determine and enforce in legal proceedings. In addition, Claimant would also bear the risk of third-party insolvency when recovering the legal costs for litigation. Clearly, it cannot be expected from Claimant to get involved in a time-consuming and expensive litigation to defend Respondent's products. This would be a serious disruption of Claimant's business.

In conclusion, the gravity of the possible consequences affirms the *rationale* behind Article 42 CISG to protect buyers from third party litigation.¹⁰⁸ Thus, it is widely accepted that a breach of Article 42 CISG almost always amounts to a fundamental breach.¹⁰⁹ Furthermore, there are strong efficiency arguments for deciding not to get involved in a litigation first to defend Respondent's goods, and then in a second proceeding trying to recover the costs of the former litigation. With this in mind, an avoidance of the contract provides the only reasonable way to solve the situation.¹¹⁰ The restitution would allow Claimant to buy substitute goods and Respondent could sell the goods to another party. Accordingly, the breach constitutes a substantial detriment and the avoidance provides the only viable solution to Claimant.

II.2.1.3 There was no possibility to cure

Claimant submits that Respondent's breach of contract amounts to a fundamental breach since there was no possibility to cure the detriment caused by it.¹¹¹ Two criteria have been set to establish fundamental breach in case law relating to the delivery of non-conforming goods. The first criterion is the impossibility to repair the goods or to make a substitute delivery of conforming goods. The second condition is whether the buyer can be expected to realize the value of the defective goods and thus can use them in a reasonable way.¹¹² The present case is comparable to the delivery of non-conforming goods, since in both cases defective goods are delivered. In the first case, the defects have material character, in the second situation the defects have a legal nature. Thus, in both cases the buyer cannot enjoy the full use of the purchased goods. Claimant submits that both criteria are fulfilled in the present case.

¹⁰⁸ See *Schwerha, Joseph J.* (1995), 'Warranties against infringement in the sale of goods: A Comparison of the UCC @ 2-312(3) and Article 42 of the U.N. Convention on Contracts for the International Sales of Goods', *Michigan Journal of International Law*, at 441., 458.

¹⁰⁹ *Schlechtriem* (1998), Art. 25, No. 20; *Langenecker* (1993), p. 268, 269.

¹¹⁰ Mitigation of the losses is a general principle of the CISG, *Beraudo, Jean-Paul*: The UN Convention on Contracts for International Sale of Goods and Arbitration, ICC Bull. Vol.5.No.1, May 1994, p.61

¹¹¹ This standard as a requirement to establish fundamental breach is also reflected in the legal literature. See *inter alia Schlechtriem* (1998) Art 25. No. 20. , *Bianca- Bonnell* (1987), *Commentary on the International Saales Law*, Milan 1987, Art. 25 notes 2.111.

¹¹² *Cour de Cassation IPRax* (1996) pp. 126. , *OLG Frankfurt NJW* (1994) pp. 1013, *Hanseatisches Oberlandesgericht*, 1. Zivilsenat, 26 November 1999, [1 U 31/99] (www.uni-freiburg.de), also see *Schlechtriem/ Huber* (1998) Article 49, No. 12, *Honnold* (1999) No. 184.

As concerning the first condition, there was no possibility of either repair or substitute delivery. Removing the marks from the infringing goods is comparable to repair in case of non-conformity. Although it is possible in theory, in the present situation, it was neither a practicable, nor a reasonable measure since it would have damaged the goods.¹¹³

Substitute delivery in this situation is also impossible, since all goods of Respondent would be equally infringing the trademark right. On the other hand, if Respondent delivered goods without the infringing trademark Claimant would lose its interest in the contract, since the aim of the contract was to sell Respondent's goods, which can only be identified by the consumers if the brand name is used.

Regarding the second condition it has been established previously, that the goods had to be withdrawn from the market. It was not possible to use them in any other reasonable way than resale. Furthermore, the goods could not have been resold in Danubia by any other person either. As Claimant had no connections to any other market than the Danubian, it could not have been reasonably expected from it to attempt to enter a new market for the sole reason of disposing the goods that have no value in Danubia.

Furthermore, Claimant contends that Respondent's conduct after the avoidance confirms that there was no effective remedy to cure the detriment suffered by Claimant as a consequence of the breach and the uncertain legal situation caused by it. Respondent's offer to compensate the reasonable costs of litigation cannot be viewed as a sufficient remedy, especially since Claimant already established, that even the possibility of such litigation amounts to a fundamental breach.

It has to be concluded that there was no possibility to cure the detriment, and avoidance of the contract was the only possible solution for Claimant. The impossibility of cure therefore establishes the fundamental breach of Respondent.

II.2.1.4 The result of the breach of contract was foreseeable by Respondent

Claimant submits that the consequences of the breach of the contract were foreseeable on two grounds. First, Respondent knew the aim of the contract. Secondly, Respondent could not have been unaware that this aim would be frustrated by the breach of its obligations under Article 42 CISG. Respondent has to be measured against the high standards of a merchant ("a reasonable person of the same kind in the same circumstances"),¹¹⁴ since it has exported its goods since 1995. Therefore he should be familiar with these consequences, which are common for these types of infringement. In conclusion, Respondent was clearly in a position to foresee the result of its breach.

II.3 Claimant declared the contract avoided

Claimant has declared the contract avoided in the letter of 3 November 1999 addressed to Respondent in compliance with Article 26 CISG. Claimant submits that this avoidance was given in a notice that was clear (**II.3.1.**) and within reasonable time in accordance with Article 49 (2)(b)(i) CISG (**II.3.2.**). Thus, all conditions required by Article 49(1)(a) CISG for an effective avoidance have been fulfilled.

¹¹³ Procedural order No. I. #23

¹¹⁴ Article 25 of CISG.

II.3.1 The letter of 3 November was a declaration of avoidance

According to Article 26 CISG, "[a] declaration of avoidance of the contract is effective only if made by notice to the other party." The courts have interpreted this provision so that the will to avoid the contract must be clearly expressed to the other party.¹¹⁵ In compliance with this rule, Claimant explicitly declared the contract avoided. In its letter of 3 November 1999, it is stated that "Sports and More Sports, Inc., is hereby avoiding the contract...". In addition, Claimant refers to Article 49 and Article 82-84 CISG, which governs the effects of avoidance, the mutual restitution. It follows that the declaration made by Claimant is clear and unambiguous.

II.3.2 The notice of avoidance was given within a reasonable time

Claimant's notice was in compliance with the requirements laid down in Art. 49 (2) (b) (i) CISG, which provides that the buyer can only declare the contract avoided within a reasonable time after it knew or ought to have known of the breach. Claimant will demonstrate that the avoidance was declared within a reasonable time.

Claimant contends that "reasonable time" within the meaning of Article 49 CISG is at least as long¹¹⁶, but rather longer¹¹⁷ than in Article 43 CISG (II.1.2.1). Claimant is of the latter opinion, notably that the time limit under Article 49 CISG is longer for the following reason. Avoidance under Article 49 CISG should be used as a last resort due to a fundamental breach. It follows from the function of the provision that a party should have sufficient time to contemplate this last resort, while the purpose of Article 43 CISG is simply to notify the seller of the breach.¹¹⁸ Thus, the time limit under Article 49 CISG extends beyond the time limit of Article 43 CISG.

As the reasonable time requirement under Article 43 was fulfilled in present case, the Tribunal should find that the avoidance was also given within the reasonable time, as the two notices were contained in the same document.¹¹⁹ It must be noted here, that there is no provision in CISG which precludes Claimant from giving notice at the same time of avoidance. This possibility has also been recognized in case law.¹²⁰ As Claimant avoided the contract within one week after receiving the letter from Howard and Heward, this avoidance was declared within reasonable time in compliance with Article 49 CISG.

III Claimant has right to restitution under Article 81-84 CISG and damages under Article 74 of CISG

Claimant is entitled to both restitution and damages after the avoidance of the contract. This follows from the remedy system of the Convention according to which damages and restitution are used complementarily.¹²¹ Restitution (Article 81 CISG) arises from the

¹¹⁵ *LG Frankfurt* RIW (1991) p. 952

¹¹⁶ *LG Oldenburg* NJW -RR. (1995), pp. 438; *OLG Köln* RIW (1994) pp. 972; *Bianca/ Bonnell/ Will* Article 49 No. 2.2.2.1 arguing that the time limits of Articles 39/43 and 49 are identical.

¹¹⁷ *Staudinger/ Magnus* Art. 49. No.38, *Schlechtriem/ Huber* (1998) Art. 49 No.46. *Achilles*, Art. 49 No. 11

¹¹⁸ *Soergel/Luederitz* (1991), 'Bürgerliches Gesetzbuch mit Einführungsgesetzen und Nebengesetzen', 12ed, Article 49, no. 13; *Staudinger/Magnus* (1999), Article 49, no.38

¹¹⁹ Exhibit No. 12.

¹²⁰ *LG Oldenburg* NJW -RR. (1995), pp. 438; *OLG Köln* RIW (1994) pp. 972; also accepted by *Bianca/ Bonnell/ Will* Article 49 No. 2.2.2.1

¹²¹ *Honnold*, 443

avoidance of the contract. The effect of the avoidance is that it "releases both parties from their obligations". This is accompanied by the parties' mutual restitution of whatever has been supplied by the other party. However, restitution alone is not sufficient to compensate the parties for their expenses following from their expectation of the contract being duly performed. Article 74 CISG provides remedy for these losses through damages. This distinction is also recognized in the case law: "Damages under Article 74 CISG do not include the restitution of the contract price already paid by [buyer] to [seller]."¹²²

According to this practice, Claimant has an overall claim, based on two grounds. First, Claimant asks for the restitution of the purchase price as provided for under Article 81 CISG with interest (**III.1.**). Secondly, he is entitled to compensation for all additional losses suffered as a consequence of the breach based on Article 74 CISG (**III.2.**). Finally, Claimant stipulates that respondent should bear all legal costs of Arbitration (**III.3.**).

III.1 Restitution

As stipulated in Article 81 CISG, Claimant is entitled to restitution for the goods that are unsold after the avoidance of the contract (**III.1.1.**). Under Article 84(1) CISG Respondent is bound to refund the price of the goods purchased and pay interest on this sum from the day on which the price was paid (**III.1.2.**). Claimant has the right to return all unsold goods. However, Claimant is not under obligation to account for the benefits that it had derived from the unsold goods as there were no such benefits. Therefore, Article 84(2) CISG is not applicable in the present case, contrary to Respondent's allegations (**III.1.3.**).

III.1.1 After the avoidance of the contract Claimant has the right to mutual restitution in respect of the unsold goods

As demonstrated above, the contract between Claimant and Respondent has been avoided on the basis of the fundamental breach. By this date, one third of the goods were sold, for which the contract has been fulfilled, thus the avoidance and the restitution only affects the goods that were still unsold at that time. Under these circumstances partial restitution is explicitly provided for by the Convention.¹²³ This principle was reaffirmed in a German court decision, where the non-conformity of the goods was discovered only some time after they were released to sale.¹²⁴ Accordingly, the claim for restitution consists of the unsold goods (two thirds of the original purchase), and two thirds of the price paid, respectively.

III.1.2 Respondent is bound to refund the price and pay interest on this sum

III.1.2.1 Quantum of restitution

Article 81 (2) CISG obliges Respondent to refund the price of the goods and Article 84 (1) CISG states that it has to pay interest on that sum from the date when it was paid.

Claimant paid for both orders separately. Both payments included the shipping costs. These are claimed under damages, and thus have to be deducted from the amounts paid according to

¹²² ICC Award 7660 (1994), ICC International Court of Arbitration Bulletin (November 1995) 69-72.

¹²³ Honsell-Weber, Vorbem. Art. 81-84, No.13

¹²⁴ See *LG Ellwangen*, 21 August 1995, 1 KfH O32/95 (at www.uni-freiburg.de)

the practice in previous ICC cases.¹²⁵ The first payment made on 10 May 1999 was \$102,000 made up of \$95,000 purchase price and \$7,000 shipping costs.¹²⁶ The second payment (\$483,000 total) was made on 25 June 1999; it consisted of \$457,000 of purchase price and \$26,000 of shipping costs.¹²⁷ One third of the goods had been sold prior to the avoidance of the contract on 3 November 1999. These goods had a total value of \$200,000 and the net purchase price paid after the 8% reduction was \$184,000.¹²⁸ One fourth of the sold goods were from the first shipment, three fourth from the second shipment.¹²⁹ Accordingly, \$46,000 should be deducted from the purchase price of the first shipment and \$138,000 (3x 46,000) should be deducted from the purchase price of the second shipment. Consequently, the partial refund of the price of the goods is calculated as following:

- From the first shipment:
\$95,000 (total paid)- \$46,000 (goods sold from first shipment) = **\$49,000**.
Interest due from the date of payment: 10 May 1999.
- From the second shipment:
\$457,000 (total paid)- \$138,000 (goods sold from second shipment) = **\$319,000**
Interest due from date of payment: 25 June 1999.

III.1.2.2 Applicable interest rate

According to Article 84 (1) CISG, Claimant is entitled to interest on the purchase price. However, the applicable interest rate is not defined in that provision. The purchase price was paid by letter of credit in Equatoriana. According to the *travaux preparatoire* of the Convention, Article 84 (1) CISG was formed to protect against parties purposely delaying payment as to take advantage of the availability of either high interest rates or cheap credit.¹³⁰ Thus, the applied interest rate must be based on market realities, and the amount should reflect the actual gain of Respondent.¹³¹ The applicable interest rate should be the short-term commercial lending rate of Equatoriana, which is 7%. Since there is a disparity¹³² between the Danubian and the Equatorianan interest rates, any other solution would result in the unjust enrichment of Respondent.

III.1.3 Claimant has a right to return all unsold goods.

Claimant has a right to return the unsold goods after avoidance of the contract. According to Article 84(2) CISG, Claimant must account for the benefits deriving from the goods that are returned. Respondent claims the average markup price of the goods sold before the avoidance. Claimant contests the merits of Respondent's claim on two grounds. First, the sold goods on which the profit was made do not form part of the restitution (**III.1.3.1**). Secondly, the profits

¹²⁵ ICC Award 7660 (1994)

¹²⁶ Claimant's Exhibit No. 4.; Procedural Order No. I. 48.

¹²⁷ Claimant's Exhibit No. 6.; Procedural Order No. I. 48.

¹²⁸ Request for Arbitration No. 13.

¹²⁹ Procedural Order No. I. No. 45.

¹³⁰ Article 84 sets forth a general principle protecting against the "unjust enrichment" of one of the parties. Thus, the seller has to account for the interest he could have earned on the refund price. Since the obligation to pay interest is a restitutionary concern, the rate of interest payable should be calculated based on the current rate at the seller's place of business. For further analysis see: *Alan F. Zoccolillo Jnr*, Determination of the Interest Rate under the 1980 United Nations Convention on Contracts for the International Sale of Goods: General Principles vs. National Law

¹³¹ *OLG München* [7 U 1720/94], *Bezirksgericht der Saane Zivilgericht*, 20 February 1997 (CLOUT 261) (Pace CISG website), also applies interest rate of the seller's place of business.

¹³² Procedural Order No. I. No. 54.

do not *derive* from the goods, but rather they are a result of Claimant's business itself, therefore they are not covered by the "benefit" required by Article 84(2) CISG (III.1.3.2.).

III.1.3.1 *The restitution is partial in respect of the unsold goods*

As previously established, the aim of the contract was fulfilled until the point of avoidance and by that date, one third of the goods had been sold. Claimant never denied that the aim of the contract (i.e. to sell the goods in Danubia at a profit) was fulfilled in respect of those goods.¹³³ Therefore, Claimant did not claim the price and the interest of the sold goods. The restitution is partial, it covers only the yet unsold goods and the purchase price and interest of those goods, which thus form the material scope of the restitution.

Article 84(2) CISG states that the buyer has to account the seller for all benefits which he has derived from the goods or part of them: if he must make a restitution of the good or part of them.¹³⁴ "Where the buyer must return the goods, it is less obvious that he has benefited from having had possession of the goods"¹³⁵. Therefore, paragraph (2) specifies that the buyer is liable to the seller for all benefits which he has derived from the goods only if (1) he is under an obligation to return them."¹³⁶ Accordingly, Claimant must only account for the benefits deriving from those goods that are *returned*. As previously stated, Respondent only refunds part of the purchase price, in respect for the unsold goods. Thus, he does not have to account for the benefits (=interest) deriving from the purchase price of the sold goods. Therefore, Article 84(2) CISG should not be construed to include the benefits deriving from the goods that are not to be returned, since the obligation of the parties would then be in disparity.¹³⁷

Respondent may *only* demand the benefits deriving from the goods that Claimant is intending to return. However, it is impossible to discover such benefits deriving from the unsold goods. It has been affirmed in case law that the mere possession of the goods that remain unsold as a consequence of the breach is not a benefit.¹³⁸ Therefore, Article 84 (2) cannot be applied in the present situation to support Respondent's clearly unfounded claim.

III.1.3.2 *The profit does not "derive" from the goods but it is gained through Claimant's business activity*

Even if the restitution covered the goods that were sold before the avoidance of the contract, Claimant submits that the profits are not covered by the scope of Article 84(2), as the benefits do not derive from the goods, but from Claimant's business activity. The benefits covered by Article 84 (2) CISG usually would include fruits of the goods (both *fructes naturales* and indirect fruits) and benefits of use.¹³⁹ However, the profit is attached to Claimant's business and is achieved through activity and investment: the infrastructure of shops, the marketing,

¹³³ In *LG Ellwangen* (21 August 1995), ICC Award No. 7660.

¹³⁴ Article 84(2)(a)

¹³⁵ see decision: *OLG Oldenburg* 1 February 1995 (Pace CISG database)

¹³⁶ Secretariat's Commentary, p. 58.

¹³⁷ "Article 84 reflects the principle that a party who is required to refund the price or return the goods because the contract has been avoided or because of a request for the delivery of substitute goods must account for any benefit which he has received by virtue of having had possession of the money or goods. Where the obligation arises because of the avoidance of the contract, it is irrelevant which party's failure gave rise to the avoidance of the contract or who demanded restitution." In Secretariat's Commentary, p. 58.

¹³⁸ *OLG Oldenburg* (1995), the mere possession of furniture that were later returned to the seller under restitution did not give any benefits to the buyer, therefore Article 84(2) was not applicable.

¹³⁹ See in *Schlechtriem*, Art 84. 18-19, p. 660.

advertisement, etc. Consequently, the difference between the purchase price and the retail price is a "benefit" that is clearly attached to and derives from Claimant's business activity and does not derive from the goods themselves. Thus, this profit is not covered by the scope of Article 84 (2) CISG and cannot form part of the restitution.¹⁴⁰

Consequently, Claimant submits that **total sum** of the restitution is **\$368,000**, with **7%** interest rate starting from the date of the payments, respectively. Furthermore, Claimant contends that Respondent's counterclaim should be dismissed, as it lacks any legal base.

III.2 Damages

Notwithstanding the concurrent restitution by the parties, Claimant is entitled to compensation according to Article 74 CISG, which is based on the principle of full compensation.¹⁴¹ This standard is designed to place the aggrieved party in as good a position as if the other party had properly performed the contract.¹⁴² As damages cover the whole loss resulting from the non-performance, Claimant is entitled to claim the value of its interest in the performance of the contract.¹⁴³ Accordingly, Claimant will demonstrate below the sum of loss suffered as a consequence of the breach. Furthermore, Claimant states that this amount (and elements of this amount) was or ought to have been foreseeable by Respondent as a probable consequence of the breach (**III.2.1**). Claimant claims interest for this sum. (**III.2.2**.)

III.2.1 Quantum of the damages

The amount of damages for breach of contract has to be calculated on the basis of the total profit expected from the contract.¹⁴⁴ It includes the sum of actual loss suffered by the injured party, including the loss of profit. The loss has to occur in consequence of the breach and must not exceed a sum that is foreseeable by the party in breach, at the time of the conclusion of the contract, as stipulated in Article 74 CISG. The sum of the damages that Claimant suffered as a consequence of Respondent's breach consists of the following items:

Claim #1. Shipping costs of the goods purchased.

Claimant contends that the transport costs of the goods was a foreseeable expense, which has incurred and led to no sales because of Respondent's breach. Thus, it forms a loss for Claimant. Respondent arranged the shipping of the goods and therefore he knew the amount of transport costs.¹⁴⁵ Whenever transport costs are foreseeable by the party in breach, they should be awarded as damages, as stated in *Delchi Carrier SpA v. Rotorex Corp.*¹⁴⁶ The first shipment was \$7,000 paid on 10 May 1999, the second shipment was \$ 26,000 paid on 25 June 1999. Thus the total cost of shipping was \$33,000.

Claim #2. Cost of letters of credit

The costs of the letters of credit were also foreseeable by Respondent. The cost of the letters of credit occurred by 25 June 1999. Claimant claims compensation for his loss of \$620.

¹⁴⁰ For a comparable opinion see: *Honsell- Weber*, Art 84. No. 21.

¹⁴¹ *Bianca- Bonnell*, p. 543

¹⁴² *Treitel*, Remedies (1998) p.82., *Honnold*, Uniform Sales Law, 1999, p. 445.

¹⁴³ *Hanseatisches Oberlandesgericht*, 1. Zivilsenat, 26 November 1999 [1 U 31/99], (www.uni-freiburg.de)

¹⁴⁴ *Hanseatisches Oberlandesgericht* (1999)

¹⁴⁵ Claimant's Exhibits No.2, No.4, No.6

¹⁴⁶ *Delchi Carrier SpA v. Rotorex Corp.*, US Court of Appeals Second Circuit, 71 F. 3d 1024; 1995 U.S. App. Lexis 34226

Claim #3. Advertising.

Claimant contends that its advertising costs, which were foreseeable by Respondent at the time of the conclusion of the contract should be awarded as damages in accordance with ICC case law.¹⁴⁷ Claimant expected the contract to be duly performed and thus sell Vis Water Sport goods, which previously have not been marketed and were unknown in Danubia. Therefore, Claimant invested in an advertising campaign to introduce the goods.¹⁴⁸ This investment turned into a loss, since as a consequence of the breach the expected profit did not occur. It must be noted that Respondent benefited from this campaign financed solely by Claimant, since Respondent's goods are now better known in Danubia.¹⁴⁹ The advertising cost was foreseeable by Respondent since he knew¹⁵⁰ that the goods are going to be marketed and sold in Danubia.¹⁵¹ The sum of the advertising costs is \$35,000.

Claim #4. General selling and administrative expenses allocated to goods.

Claimant is entitled to recover its general selling and administrative expenses if it is possible to demonstrate that those costs in case of performance exceeded the general costs in case of non-performance.¹⁵² Claimant's business has a general fixed cost of selling and administrative expenses, which are in connection with all the good sold and are allocated among them proportionally. Therefore each unit of goods have costs attributed only to those goods. In case the sales do not occur, this cost turns into a loss, which Respondent could foresee. It is a sum of \$ 40,000.

Claim #5. Fee of Legal Opinion.

Claimant had additional expenses of the legal fees paid to Howard & Heward for the legal opinion. This loss was a direct consequence of the breach of contract. Claimant acted in good faith and was driven by the aim of being faithful to the contract by first ascertaining the breach and asking for legal opinion on the claim.¹⁵³ These costs are therefore reasonable and presumed to be foreseeable by Respondent.¹⁵⁴ Claimant paid \$2,000 as legal fees.¹⁵⁵

Claim #6. Loss of profit.

It has been established in ICC case law¹⁵⁶ that the injured party should be able to demand compensation for any profit lost as a consequence of the breach of the other party, to the extent and under the condition that the loss was foreseeable by the other party in breach.¹⁵⁷ Respondent has expressly stated that Vis sports goods are usually sold with a 70% markup

¹⁴⁷ ICC Award 8611(1997)

¹⁴⁸ Request for Arbitration No. 5.

¹⁴⁹ Procedural Order No. I. No. 25.

¹⁵⁰ Claimant's Exhibit No. 1-3.

¹⁵¹ Advertising costs are usually awarded as damages, if the seller knew that the goods are going to be marketed and sold, and this aim is frustrated by the non-delivery of the seller, or the delivery of non-conforming goods. See in ICC Award 8611/HV/JK (1997) (www.cisg.pace.com)

¹⁵² *Hanseatisches Oberlandesgericht* (1999) (OLG Hamburg) [1 U 31/99]

¹⁵³ "Legal costs are [claims] that are usual in situations of avoidance of a contract for breach of one party. They should be therefore considered as foreseeable", ICC Award No. 7587 (1992), in: Extracts from ICC Awards n the Application of International Conventions, ICC Bull. Vol. 6./ No. 2 - November 1995, p. 63.

¹⁵⁴ *Schlechtriem*, Art. 74, no. 19.: There is a presumption of foreseeability in connection with reasonable expenses of ascertaining the damage or of avoiding or mitigating it. Also see *Handelsgericht Aargau*, Switzerland, 19 December 1997 (Pace CISG database)

¹⁵⁵ Procedural Order No. 1. #50.

¹⁵⁶ ICC Award No. 7565 (1994), ICC Award No. 7585 (1992), ICC Award No. 7531 (1994) in ICC Bull. Vol 6. No. 2 November 1995, p. 60-77, *Delchi v. Rotorex* (1995)

¹⁵⁷ *Bianca*,/ *Bonnell* p. 544.

price by retailers.¹⁵⁸ This is the profit that Claimant expected to have under this contract. It is indisputable, that if the contract was performed properly Claimant would have gained that profit. Therefore, the loss of profit is a direct consequence of Respondent's breach.

Since the basic aim of Article 74 CISG is to place the injured party in the same economic position he would have been had the contract been performed¹⁵⁹, this loss of profit should be compensated by Respondent, as fully as possible. The loss as a possible consequence of the breach was foreseeable by Respondent, especially because he knew the usual markup price at the time of the conclusion of the contract.¹⁶⁰ It was established in *Delchi v. Rotorex* that if the buyer can show his loss of profit that incurred as a foreseeable and direct result of Respondent's breach with sufficient certainty then this should be granted as damages.¹⁶¹ The sum of the expected profit is 70% of the value of the unsold goods, amounting to \$280,000. The costs normally occurring around the sales (claim #1, #2, #3) have to be deducted from this gross profit to calculate the net profit and avoid the double compensation of Claimant. Thus, should any of those claims be not allowed as direct losses by the Tribunal, they alternatively must be considered as part of the loss of profit and should be added to this net sum. The net loss of profit that Claimant claims is at minimum \$172,000.

Ad Claim #5 and #6: Claims #5 and #6 are new claims that fall within the Terms of Reference

ICC Arbitration Rules (ICCRA) Article 19 stipulates that after the Terms of Reference (**ToR**) have been signed parties may only make new claims which do not fall outside the limits of the ToR. However, the Arbitral Tribunal may authorize the party to make a new claim that falls outside the limits of the ToR.¹⁶² Although the amounts of claim #5 (legal fee) and #6 (loss of profit) are not expressly included in the ToR, Claimant stipulates that these claims fall within its limits.

The ToR is designed to enable the parties and the Arbitral Tribunal to focus on issues in the arbitration. "They are not to be understood as foreclosing the making of arguments or introduction of evidence not expressly referred to herein."¹⁶³ This requirement of flexibility should be regarded in dealing with claim #5 and #6. The broad interpretation to include all claims closely connected to the claims stipulated in the ToR has always been the main practice of ICC Tribunals.¹⁶⁴ There are some guidelines to define new claims that remain within the limits fixed by the ToR, such as the link between the new claim and the initial claim, the interest of the parties, the economic importance of the new claim and the interest of properly administered justice. It also should be considered whether there is a possible complication or delay of the proceedings because of the claim.¹⁶⁵ Having regard to these guidelines, Claimant's claims clearly are within the scope of the ToR. Both parties claim the

¹⁵⁸ Answer to the Request for Arbitration No. 10.

¹⁵⁹ *Bianca/ Bonnell* p. 543.

¹⁶⁰ "Foreseeability depends on knowledge of matters and facts which enable the party concerned to foresee the consequences of the breach." In *Bianca- Bonnell*, p. 542

¹⁶¹ United States 9 September 1994 U.S. Dist. Ct. (*Delchi Carrier S.p.A. v. Rotorex Corp.*)

¹⁶² ICC Arbitration Rules Article 19

¹⁶³ *Derain- Schwartz*, A Guide to the New ICC Arbitration Rules, Kluwer, 1998, p. 233

¹⁶⁴ "Therefore even if [Claimant's] last claims were to be considered as new claims distinct from the first one, there would exist between these claims and the initial one a tight link which by itself would justify [the inclusion of those claims]." in: *National Oil Company v. Libyan Sun Oil Company*, ICC Award No. 4462 (1985) Y.C.A. XVI (1991) p. 54-78, at pp. 71. This broad interpretation was challenged and reaffirmed by the US District Court. (*NOC v. LSOC*, US Dist. Ct. Delaware, 15 March 1990, 733 Fed Suppl. (1990) pp. 800-822)

¹⁶⁵ *Andreas Reiner*, Terms of Reference, ICC Bull. Vol 7. No.2. Dec. 1996

costs of the arbitration, including legal costs.¹⁶⁶ This statement should be understood to cover all legal costs arising from the breach of contract and all consequent legal actions. Further elaboration of claims and counterclaims are within the ToR.¹⁶⁷ Thus, the legal costs of ascertaining the fundamental breach are covered by that claim.

Claim #5, the loss of profit did not form part of the original claim. However, in its response for arbitration, Respondent claimed the benefits deriving from the sold goods. This claim forms part of the ToR.¹⁶⁸ Thus, the profits arising from the goods are partly included in the ToR. The profits arising from the goods sold before the avoidance and the profits due to arise from the goods yet unsold at that time cannot be dealt with by separately. They are so closely connected that it is impossible to include one in the material jurisdiction of the Tribunal without implicitly including the other. The two amounts represent a continuity deriving from the same legal basis, the underlying sales contract. Although, Claimant first did not raise the issue of loss of profits, Respondent's consequent claim brought it within the sphere of application of the ToR.

Furthermore, Article 19 of the new ICC Rules is more lenient as the previous rules that were mentioned above.¹⁶⁹ The claims would surely satisfy the requirements set down in the case law of the old rules, therefore qualify under the more relaxed new rules. In conclusion, the ToR should be interpreted as to include these claims indirectly, by including claims that are so closely connected that they seem to be inseparable.

Claim #7: Storage expenses deriving from the preservation of goods

Articles 86 and 87 CISG regulate preservation of goods that the buyer intends to reject. These costs are also covered by Article 74 CISG. Article 87 CISG provides for the recovery of all reasonable expenses incurred from preservation of goods (e.g. deposit in a warehouse). This claim is also accepted in case law.¹⁷⁰ Claimant has fulfilled his obligation of preserving the goods by placing them in a warehouse from 3 November 1999. The continuing cost of warehouse storage derives from Respondent's refusal to accept the non-conforming goods. The costs are approximately \$570 per month (\$4,000 between 3 November 1999 and 6 July 2000). At the time of submitting present memorandum, the cost of storage amount to \$7,430.

The **total sum of damages** at the time of submitting the memorandum is **\$390,050**.

III.2.2 Claimant has a right to interest on the damages awarded

It is established in case law that claimants prevailing on the merits are entitled to receive interest on the principal amount awarded.¹⁷¹ This can be equally derived from Article 74 (loss of profit) and Article 78¹⁷² (interest due on any sum in arrears) of the Convention.¹⁷³ However, the Convention is silent about both the starting date of the accrual of interest (**III.2.2.1.**) and the applicable interest rate (**III.2.2.2.**). Thus, these issues should be decided

¹⁶⁶ Terms of Reference, no. 16.

¹⁶⁷ *Craig/ Park/ Paulsson: An Annotated Guide to the 1998 ICC Arbitration Rules*, 1998, p. 121

¹⁶⁸ Terms of Reference, no. 13.

¹⁶⁹ ICC: Terms of Reference Under the 1998 ICC Arbitration Rules, ICC Bull. Vol 3. No. 1 May 1992, p. 24.,

¹⁷⁰ *ICC Award, No. 7531 of 1994*

¹⁷¹ *ICC Award No. 7331 (1994)*

¹⁷² *Bridge: The International Sale and Practice*, Oxford, 1999, pp. 104.

¹⁷³ *OLG München*, March 2, 1994; RIW 1994:596, *OLG Frankfurt, January 18, 1994*, RIW 1994:241; *OLG Koblenz*, September 17, 1993, RIW 1993:938, *ICC Award No. 8128, ICC Award No. 7585*, ICC Bull. November 1995.61 ff.

with the guidance of the interpretation principles laid down in Article 7 of the Convention itself. Interpretation should be made in conformity with the general principles the Convention is based on. In absence of such principles, the problem should be solved with the help of the law applicable by virtue of the rules of private international law. Furthermore, regard is to be taken to the need for uniform interpretation and therefore, to the case law of the Convention.

III.2.2.1 Damages are due on the date of avoidance

The Convention does not expressly define the date from which the interest should accrue on the principal sum of the award. However, according to Article 84 CISG the interest is due from the date when the price was paid. It may be concluded that the CISG follows the principle that damages are due from the time when they occur.¹⁷⁴ For the shipping costs (claim #1) and for the cost of the letter of credit (claim #2) this time is a firm date, the date of payment, defined in **III.2.1**. Thus, for these sums the interest is due starting from the aforesaid dates. For the rest of the claims it is impossible to determine the exact date of the loss. As an ancillary method, also used in practice, the interest should start to accrue on the date, when proper notice was given, which is also the date of the avoidance.¹⁷⁵ Therefore, the interest on all other claims is due from 3 November 1999.

III.2.2.2 Applicable interest rate

Claimant contends that the applicable interest rate to the interest on the principal sum of damages is the short-term lending rate of Equatoriana. There is a clear trend in case law to apply the *lex contractus* (the law which would be applicable to the sales contract if it were not subject to the CISG) to define the applicable interest rate.¹⁷⁶ Some courts go as far as referring to this solution as a unanimous one.¹⁷⁷ According to prevailing conflict of law rules in most countries, the *lex contractus* would be the law of the country where the party who is to perform the characteristic performance (seller) of the contract has its seat.¹⁷⁸

Although, in present case the relevant conflict rules has not been established, the former Convention makes applicable the law with which the contract has the closest connection. This approach is in conformity with Article 17 of the ICC Arbitration Rules, which allows the Arbitral Tribunal to apply the most appropriate law in absence of a choice by the parties. The closest connection presumed to be the law where the party who is to effect the characteristic performance has its habitual residence.¹⁷⁹ In sales contracts the characteristic performance is to be effected by the seller, thus it is the interest rate of the country where the seller has its place of business which generally is applicable.¹⁸⁰ In the present case, the applicable interest rate is that of Equatoriana, where Respondent has its seat. The CISG stands on the principle of

¹⁷⁴ ICC Award No. 6360 (note: this award was rendered according to the ULIS (1964), but the relevant provisions are identical.

¹⁷⁵ ICC Award 7331

¹⁷⁶ LG Hamburg IPRax 1991, 400; Fővárosi Bíróság Budapest v. 24.3.1992 cited by Vida IPRax 1993, 263 f.; OLG Frankfurt NJW 1994, 1013; OLG München RIW 1994, 595; ICC Award No. 7197 (1992) J.D.I. 1993, 1028. This opinion is also dominant in the legal literature: Schlechtriem Art. 78. No. 26; Staudinger/Magnus Art. 78. No. 12; Witz Nr. 81f; it is also the conclusion of F. Ferrari in CISG Case Law on the Rate of Interest on Sums in Arrears, R.D.A.I. (1999) no. 1. at p. 90.

¹⁷⁷ OLG Hamm, 8 February 1995 (uni.freiburg.de); HG Kanton Zürich cited by Behr, 9 September 1993, see also: Franco Ferrari, CISG Case Law on the Rate of Interest on Sums in Arrears, R.D.A.I., No.1, 1999, p.90

¹⁷⁸ Rule constructed by Schnitzer, Jan Kropholler: Internationales Privatrecht §52 III. p. 416, (1997) Tübingen

¹⁷⁹ The reason for this rule is that the obligation of the seller is more endangered to be breached.

¹⁸⁰ OLG Koblenz, January 31, 1997

full compensation.¹⁸¹ By focusing on this objective, the inquiry should be which interest rate will fully compensate the aggrieved party. Thus, Claimant should be awarded interest payments at the rate based on the actual credit costs, the short term lending rate.¹⁸²

Claimant stipulates that if this Tribunal disregards the private international law approach, and applies general principles it is still bound to arrive to the same conclusion. New cases in international arbitration affirm that such general principles as stipulated in Article 7(2) CISG are possible to find.¹⁸³ The UNIDROIT Principles, which is an unofficial "restatement"¹⁸⁴ of international commercial contracts, has been based on the same principles as the CISG and thus it is appropriate to use these principles to fill the gaps of the Convention. The UNIDROIT principles give more guidance on the applicable interest rate. "*The rate of interest shall be the average bank short-term lending rate to prime borrowers prevailing for the currency of payment at the place of the payment, [...]* Article 7.4.9 (2). According to the above stated law, the applicable rate of interest is the short term lending rate in Equatoriana, where the payment was made by letters of credit. This interest rate is also applicable to the interest on the restitution of the purchase price as indicated above in **III.1.2.2.** It is therefore desirable to use the short term lending rate of Equatoriana of 7%.

III.3 Costs of Arbitration and Legal Costs

Claimant contends that the costs of arbitration and the legal costs should be born by Respondent alone. Present arbitration proceedings are due to the fact that Respondent refused to co-operate with Claimant on the matter of mutual restitution, after the breach of contract had been discovered. Thus, Respondent did not act in good faith, contrary to CISG that governs present contract, and also contrary to the principles of *lex mercatoria*. Due to Respondent's behavior and due to the fact that Respondent is the party in breach, Respondent should bear the costs of arbitration, including the reasonable legal and other costs incurred by Claimant, as stipulated in Article 31 of the ICC Rules of Arbitration.

¹⁸¹ *Arbitral Award, Case SCH-4366, (Aus. v. F.R.G.)*, Internationales Schiedsgericht der Bundeskammer der Gewerblichen Wirtschaft (June 15, 1994) (abstract)

¹⁸² *Koneru, Phanesh, 'The International Interpretation of the UN Convention on Contracts for the International Sale of Goods: An Approach Based on General Principles'*, 6 *Minnesota Journal of Global Trade* (1997) 105-152.

¹⁸³ International Court of Arbitration of the Federal Chamber of Commerce of *Vienna, Award No. 4318 and Award No. 4366* [15 June 1994] and *ICC Award No 8128* (1995) refer to the UNIDROIT Principles when defining applicable interest rate

¹⁸⁴ *M. J. Bonnell, An International Restatement of Contract law*, 2nd ed., Transnational Publishers Inc., Irvington, New York, 1997, p. 229

Request for relief

In view of the above submissions, may it please the Tribunal

- to declare that a valid arbitration agreement has been concluded between Claimant and Respondent
- to declare that Respondent's breach of contract was fundamental breach
- to declare that Claimant had a right to avoid the contract
- to allow restitution of the purchase price of \$368,000 with interest on this sum as of the day of payment
- to dismiss Respondent's counterclaim of \$ 147,700
- to allow damages of \$390,050 and interest on this sum as of 3 November 1999
- to order Respondent to bear all costs of arbitration and all other legal costs.

For Sports and More Sports Inc.

Attorneys

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Natalia Matting

Maastricht, 1 December 2000