

**ELEVENTH ANNUAL WILLEM C. VIS  
INTERNATIONAL COMMERCIAL ARBITRATION MOOT  
2003–2004**

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Equapack, Inc. v. Medi-Machines S.A.

Memorandum for Medi-Machines, S.A.

(Respondent)

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**Table of Contents**

**LIST OF ABBREVIATIONS ..... iv**

**TABLE OF AUTHORITIES ..... vi**

**Articles and Treatises ..... vi**

**Treaties and Rules..... xiii**

**Cases..... xiv**

**Arbitral Awards.....xx**

**STATEMENT OF FACTS.....1**

**SUMMARY OF ARGUMENT .....2**

**I. THE MODEL 14 MACHINES CONFORMED TO THE CONTRACT.....3**

**A. The machines were of the description required by the contract. ....3**

        1. The contract called for machines capable of processing only non-corrosive dry bulk commodities.....3

        2. Both the CISG and UNIDROIT support RESPONDENT’s position.....5

        3. RESPONDENT adequately informed CLAIMANT about the machines’ capabilities. ....6

        4. No particular purpose of packaging salt was made known to RESPONDENT at the conclusion of the contract. ....6

        5. The original contract was never modified to require machines with the ability to process salt.....7

**B. The machines conformed with the contract because their packing speeds reflected the speed of machines of the same kind. ....8**

        1. The machines were of the quality required by the contract.....8

            a) The adequacy of the Model 14 machines’ processing speed must be judged by comparison to machines of a similar design.....9

            b) CLAIMANT erroneously states the quality standard that applies under the CISG. ....10

            c) Even if 180 bags per minute is the average industry rate for fine products, the rate for the Model 14 machines falls within an acceptable range of deviation.....10

        2. RESPONDENT did not make any warranties regarding the machines’ processing speed. ....11

<b>II. EVEN IF THE MODEL 14 MACHINES DID NOT CONFORM TO THE CONTRACT, CLAIMANT IS NOT ENTITLED TO RELY ON THE LACK OF CONFORMITY.</b>	<b>12</b>
<b>A. CLAIMANT failed to properly inspect the machines.</b>	<b>12</b>
1. CLAIMANT did not conduct an appropriately diligent examination of the machines.	12
a) CLAIMANT failed to conduct a test run.	12
b) CLAIMANT failed to examine the machine diligently for compatibility with highly corrosive products.	13
2. Even if CLAIMANT did conduct an appropriately diligent examination, the length of the examination period was unreasonably long.	14
<b>B. CLAIMANT failed to mitigate damages.</b>	<b>15</b>
<b>III. EVEN IF THE TRIBUNAL FINDS THAT RESPONDENT COMMITTED A BREACH OF CONTRACT, THE BREACH WAS NOT A FUNDAMENTAL ONE.</b>	<b>16</b>
<b>A. RESPONDENT did not substantially deprive CLAIMANT of what it was entitled to expect.</b>	<b>16</b>
1. RESPONDENT’s delivery of allegedly nonconforming machines did not substantially deprive CLAIMANT of what it was entitled to expect.	17
2. RESPONDENT was not responsible for any harm suffered by CLAIMANT after delivery.	18
<b>B. No “substantial detriment” to CLAIMANT was foreseeable to RESPONDENT.</b>	<b>19</b>
<b>IV. REGARDLESS OF WHETHER RESPONDENT COMMITTED A FUNDAMENTAL BREACH, CLAIMANT DID NOT MAKE AN EFFECTIVE AVOIDANCE.</b>	<b>21</b>
<b>A. CLAIMANT lost the right to avoid because it was unable to return the goods in substantially the condition in which they were received.</b>	<b>21</b>
<b>B. CLAIMANT did not avoid the contract.</b>	<b>22</b>
1. CLAIMANT’s failed to give effective notice of its intent to avoid.	22
2. CLAIMANT’s purported declaration of avoidance was not timely.	23
<b>V. THE TRIBUNAL SHOULD ORDER CLAIMANT TO POST SECURITY FOR COSTS.</b>	<b>24</b>
<b>A. The Tribunal has jurisdiction to issue an order of security.</b>	<b>24</b>
<b>B. Ordering security for costs is a widely accepted practice in dispute settlement.</b>	<b>24</b>

<b>C. An order of security for costs is necessary to protect RESPONDENT’s interests. ....</b>	<b>25</b>
1. CLAIMANT’s questionable financial position weighs heavily in favor of an order of security. ....	25
2. Concerns over enforcement weigh in favor of ordering CLAIMANT to post security for costs. ....	26
3. The merits and good faith of CLAIMANT’s action are not a significant factor in this request for security for costs. ....	27
4. RESPONDENT’s request for an order of security for costs is based on the reasonable concerns explained above, not in strategic or evasive tactics. ....	28
<b>VI. THE TRIBUNAL SHOULD ORDER CLAIMANT TO REFRAIN FROM DIVULGING INFORMATION RELATED TO THE ARBITRATION. ....</b>	<b>28</b>
<b>A. Claimant is not entitled to derogate from its obligation of confidentiality. ....</b>	<b>29</b>
1. Exception (d) to SIAC Rule 34.6 does not release CLAIMANT from its duty of confidentiality in this arbitration. ....	29
a) CLAIMANT has not established the requirements enumerated in SIAC Rule 34.6 (d). ....	29
b) CLAIMANT is obligated to refrain from divulging all details of the arbitration. ....	31
c) CLAIMANT is obligated to refrain from divulging the existence of the arbitration. ....	31
d) Requiring confidentiality of a third party does not improve the case for disclosure. ....	32
2. Allowing CLAIMANT to disclose information would be neither legitimate nor reasonable. ....	32
<b>B. The Tribunal has authority to rule on all matters of confidentiality. ....</b>	<b>33</b>
<b>C. Unauthorized disclosure would warrant consequences for Claimant. ....</b>	<b>34</b>
<b>CONCLUSION .....</b>	<b>35</b>

## LIST OF ABBREVIATIONS

¶	Paragraph
¶¶	Paragraphs
AAA	American Arbitration Association
AG	Amtsgericht
A.L.R.	Australian Law Reports
Apr.	April
Art.	Article
Arts.	Articles
Aug.	August
BG	Bundesgericht
BGH	Bundesgerichtshof
CISG	United Nations Convention on the International Sale of Goods
Co.	Company
Dec.	December
E.g.	Exempli gratia (for example)
Ex.	Exhibit
Feb.	February
Id.	Idem (previously cited item)
ICC	International Chamber of Commerce
Inc.	Incorporated
Jan.	January
LCIA	London Court of International Arbitration
LG	Landgericht
Lloyd's Rep.	Lloyd's Reporter
Mar.	March
Model Law	UNCITRAL Model Law on International Commercial Arbitration

No.	Number
Nov.	November
NSWLR	New South Wales Law Reports
Oct.	October
OG	Obergericht
OGH	Oberster Gerichtshof
OLG	Oberlandesgericht
Proc. Order	Procedural Order
P.	Page
Q.B.D.	Queen's Bench Division
QCA	Queensland Court of Appeal
Sept.	September
SIAC	Singapore International Arbitration Centre
Supra	Above
UCC	Uniform Commercial Code
UNCITRAL	United Nations Commission on International Trade Law
U.K.	United Kingdom
U.S.	United States
U.S.A.	United States of America
V.	Versus
Vol.	Volume

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available at: <http://www.cisg.law.pace.edu/cases/970108s1.html>  
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### ***United Kingdom***

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### ***United States of America***

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Chateau Des Charmes Wines Ltd. v. Sabate, 328 F.3d 528, 9th Circuit Court of Appeals (2003)

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cited as *Ladd v. Honda Motor (U.S.A.)*

Shuttle Packaging Systems, L.L.C. v. Jacob Tsonakis, INA S.A, case no. 1:01-CV-691, District Court, Michigan (2001)

available at: <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/011217u1.html>

cited as *Shuttle v. Tsonakis (U.S.A.)*

Supermicro Computer, Inc. v. Digitechnic, case no.C-00-02214-CAL, District Court, California (2001)

available at: <http://www.cisg.law.pace.edu/cases/010130u1.html>

cited as *Supermicro Computer v. Digitechnic (U.S.A.)*

## Arbitral Awards

Netherlands Arbitration Institute, case no. 2319 (15 Oct. 2002)

available at: <http://cisgw3.law.pace.edu/cases/021015n1.html>

cited as *Netherlands Arbitration Institute, 15 Oct. 2002*

Arbitration Institute of the Stockholm Chamber of Commerce, Beijing Light Automobile Co., Ltd. v. Connell L.P. (5 June 1998)

available at: <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/980605s5.html>

cited as *Beijing Light Automobile v. Connell (Sweden)*

## STATEMENT OF FACTS

1. The parties to this arbitration are the CLAIMANT, Equapack, Inc., and the RESPONDENT, Medi-Machines, S.A. The present dispute arises out of a contract in which RESPONDENT agreed to sell, and CLAIMANT agreed to buy, six dry food packing machines.
2. On 24 June 2002, CLAIMANT's works manager, Donald Swan, contacted RESPONDENT seeking to purchase machines that could be "used over a wide range of products, both fine goods, such as ground coffee or flour, and coarser goods such as beans or rice." [*Claimant's Ex. 1*]. He indicated that "[b]oth price and prompt delivery would be essential elements of our purchasing decision." [*Id.*]. Notably, Mr. Swan made no mention of any intention to use the machines with salt or other corrosive products. RESPONDENT's salesman, Stefan Drake, responded by offering two auger-feeder machines—the Model 14 and Model 16—that met the needs identified by CLAIMANT. [*Claimant's Ex. 2*]. On 12 July 2002, CLAIMANT accepted the offer for six Model 14 machines. [*Claimant's Ex. 3*].
3. After the conclusion of the contract, on 23 July 2002, Mr. Swan telephoned Mr. Drake to inquire into the progress of the order. During the conversation, Mr. Swan spoke casually about other matters, including a brief comment mentioning salt: "A2Z wants us to get going on packaging their stuff. They have everything in mind from large beans to salt to fine powder and we are going to have to do it all. Some of this is stuff we've never handled before, but I am sure we'll do fine with your machines to help us." [*Statement of Defense ¶ 6*].
4. The machines were delivered on 21 August 2002. Despite explicit warnings in the product manual against using the machines to package corrosive products, [*Proc. Order 3, Clarification 25*], CLAIMANT used the machines to package salt, damaging them severely. [*Claimant's Ex. 6; Proc. Order 3, Clarification 29*]. Notwithstanding its misuse of the machines, CLAIMANT now argues that RESPONDENT should have supplied machines that could process corrosive products—even though such products are considerably more expensive than the Model 14 machines purchased by CLAIMANT. CLAIMANT also alleges that the machines were slower than it expected, even though it had not requested specific performance standards during the contract negotiations. According to tests by engineer Eur. Ing. Heath-Robinson, the machines operated at rates between 130 and 180 bags per minute, depending on the substance being packed. [*Engineer's Report*].

5. Mr. Swan contacted Mr. Drake on 18 and 19 October 2002 regarding the problems with the machines. *[Claimant's Ex. 6]*. Mr. Swan demanded reimbursement for the purchase price and other expenses. Since RESPONDENT was not to blame for the misuse of the machines, Mr. Drake declined to offer reimbursement, but he did offer to make a substantial concession on the purchase of Model 17 packaging machines. *[Claimant's Ex. 7]*.
6. CLAIMANT initiated this arbitration on 10 February 2003. *[Notice of Arbitration]*. In light of recent reports in the financial press about CLAIMANT's questionable financial position, RESPONDENT subsequently requested that the Tribunal order CLAIMANT to post \$20,000 as security for RESPONDENT's legal costs. *[Letter of Horace Fasttrack, 1 Sept. 2003]*.
7. CLAIMANT is currently in the process of being acquired by Equatoriana Investors. *[Letter of Joseph Langweiler, 9 Sept. 2003]*. The due diligence for that transaction is currently in progress. *[Id.]*. After learning of the potential acquisition, RESPONDENT requested an order prohibiting CLAIMANT from disclosing any information about the existence or nature of this arbitration during the due diligence process. *[Letter of Horace Fasttrack, 17 Sept. 2003]*.

## **SUMMARY OF ARGUMENT**

8. Based on the arguments set forth below, RESPONDENT respectfully submits the following:
  - (1) That the Model 14 machines delivered by RESPONDENT conformed to the contract **(I.)**;
  - (2) That CLAIMANT is not entitled to rely on any nonconformity **(II.)**;
  - (3) That RESPONDENT did not commit a fundamental breach of contract **(III.)**;
  - (4) That CLAIMANT did not make a valid avoidance of contract **(IV.)**;
  - (5) That CLAIMANT should be required to post security for costs **(V.)**; and
  - (6) That CLAIMANT should be ordered to refrain from disclosing the existence or the details of the arbitration **(VI.)**.

## **I. THE MODEL 14 MACHINES CONFORMED TO THE CONTRACT.**

9. CLAIMANT's assertion that RESPONDENT breached the contract, [*Memorandum for Claimant* ¶ 17], must be rejected. The machines conformed to the contract in all respects: they were capable of processing non-corrosive fine and coarse dry bulk commodities (A.), and their packing speeds reflected the speed of machines of the same kind (B.).

### **A. The machines were of the description required by the contract.**

1. *The contract called for machines capable of processing only non-corrosive dry bulk commodities.*

10. CLAIMANT's letter of 24 June 2002, [*Claimant's Ex. 1*], constituted an invitation to make an offer since it was not addressed to a specific person and did not indicate the goods and expressly or implicitly fix or make a provision for determining the price. [*Art. 14(3) CISG*]. The letter (hereinafter referred to as "the Invitation") stated that CLAIMANT expected to use the machines "over a wide range of products, both fine goods, such as ground coffee or flour, and coarser goods such as beans or rice." [*Id.*]. Ground coffee, flour, beans, and rice are all examples of *non-corrosive* dry bulk commodities.

11. RESPONDENT's letter of 3 July 2002 was an offer because it was sufficiently definite—stating the goods, quantity, and price—and indicated an intent to be bound in case of acceptance. [*See Art. 14(1) CISG*]. This letter ("the Offer") reflected CLAIMANT's request, proposing a machine that could be used over a wide range of non-corrosive dry bulk commodities. [*Claimant's Ex. 2*]. CLAIMANT's letter of 12 July 2002 amounted to an acceptance since it indicated assent to RESPONDENT's offer as required under Article 19(1) CISG and did not contain additional or different terms which materially altered the terms of the Offer as required under Article 19(2) CISG. Notably, that letter ("the Acceptance") did not mention any requirements for the machines to handle corrosive products, such as salt.

12. Under Article 35(1) CISG, "[t]he seller must deliver goods that are of the quantity, quality and description required by the contract." The contract thus formed was for six machines that could handle a wide range of non-corrosive fine and coarse dry bulk commodities such as ground coffee, beans, flour, and rice. RESPONDENT delivered six such machines.

13. RESPONDENT's Offer mentioned machines that were capable of handling a wide range of products. [*Claimant's Ex. 2*]. CLAIMANT argues that this means all products, corrosive and

non-corrosive, including salt. [*Memorandum for Claimant* ¶ 19]. However, as CLAIMANT acknowledges, Article 8(3) CISG “provides that consideration is to be given to all relevant circumstances of the case, including the negotiations.” [*Memorandum for Claimant* ¶ 20 (quoting Art. 8(3) CISG)]. CLAIMANT’s Invitation must therefore be taken into account when interpreting the Offer and the resulting terms of the contract.

**14.** RESPONDENT agrees with CLAIMANT that “the mention of ‘a wide range of products’ followed by some examples of goods both fine and coarse is a clear indication of CLAIMANT’s will to pack a number of otherwise unspecified goods of the *same* nature.” [*Memorandum for Claimant* ¶ 21 (emphasis added)]. The Invitation specifically referred to “fine goods, such as ground coffee or flour, and coarser goods such as beans or rice.” [*Claimant’s Ex. 1*]. Although CLAIMANT is correct that the phrase “such as” is an introduction to a non-exhaustive list of products, it means “like” or “for example.” [*Black’s Law Dictionary*]. Although CLAIMANT argues that the Invitation was so broad as to include everything, CLAIMANT’s own requirements were much more specific. The common denominator for the items listed—their same nature—is that they are all dry *non-corrosive* commodities. In accordance with Article 8(3) CISG, a reasonable person in the same position as RESPONDENT would not have understood these examples to include dry *corrosive* commodities such as salt. Such interpretation is further strengthened by industry practice, since the vast majority of firms that pack dry bulk products do not pack salt. [*Proc. Order 3, Clarification 27*]. Therefore, it would be unreasonable for RESPONDENT to assume that by providing examples of only non-corrosive products CLAIMANT also meant to include salt. This conclusion is consistent with *Schmidt v. Textil-Werke*, where the Supreme Court of Switzerland held that the seller was entitled to believe that the buyer also supposed that the machine was not equipped for a certain rapport length.

**15.** RESPONDENT submitted its offer for six machines capable of handling dry non-corrosive products, exactly as CLAIMANT specified in its Invitation. The Offer incorporated CLAIMANT’s own description—from the Invitation—by reference, using the term “as you have stated.” [*Claimant’s Ex. 2*]. This description was not changed by the Acceptance, which specified “six Model 14 dry stuff packaging machines.” [*Claimant’s Ex. 3*]. Thus, the machines delivered conformed to the description required by the contract.

2. Both the CISG and UNIDROIT support RESPONDENT's position.

16. CLAIMANT argues that the Tribunal should follow the French Civil Code and construe ambiguous terms against RESPONDENT. [*Memorandum for Claimant* ¶ 33]. Honnold warns of the “natural tendency to read the international text through the lens of domestic law.” [*Honnold (1) 208*]. If the CISG is viewed through a domestic lens, then the image produced will be distorted. [*Murray 366*]. Furthermore, “since Article 7(1) asserts that the international character and need for uniformity in application should be taken into account ... A domestic law resolution of an issue would not promote [such ends].” [*Darkey 139-40*]. Even assuming, arguendo, that the product description was ambiguous, the CISG does not follow the French Civil Code's rule of construction. Instead, the CISG adopts a reasonable person standard of interpretation. [*Art. 8(2) CISG*]. The analysis above, [*see supra* ¶ 12], demonstrates that applying a reasonable person standard of interpretation leads to a product description that does not include corrosive commodities, such as salt.

17. Looking to the UNIDROIT for guidance helps further strengthen RESPONDENT's interpretation. In addition to a reasonable person standard of interpretation [*Art. 4.1 UNIDROIT*], the UNIDROIT also incorporates a *contra proferentem* rule by which “if contract terms supplied by one party are unclear, an interpretation against that party is preferred.” [*Art. 4.6 UNIDROIT*]. In the instant case, CLAIMANT supplied the product description in the Invitation, which was subsequently incorporated in the Offer and Acceptance as explained above. [*See supra* ¶ 10]. CLAIMANT qualified the term “wide range of products” with examples of non-corrosive dry fine and coarse bulk products. CLAIMANT now argues that the term “wide range of products” also includes corrosive products, and specifically salt. However, since CLAIMANT supplied the description, it had the burden of providing at least one example that encompassed a corrosive product, such as salt. If the machines were to have specific characteristics, CLAIMANT should have informed RESPONDENT. [*LG Regensburg, 24 Sept. 1998 (Germany); OLG Koblenz, 11 Sept. 1998 (Germany)*]. CLAIMANT did not do so. Under the *contra proferentem* rule, CLAIMANT's failure to specify corrosive products preclude it from now claiming that the description included machines capable of handling corrosive items, such as salt.

3. *RESPONDENT adequately informed CLAIMANT about the machines' capabilities.*

**18.** RESPONDENT agrees in principle with CLAIMANT's conclusion that "an introduction of a non-exhaustive list of products ... should have led a responsible seller to specify the type of products within the category of fine and coarse dry bulk goods for retail packaging incompatible with their machines or not to recommend unfit machines." [*Memorandum for Claimant ¶ 20*]. However, the machines are able to process non-corrosive dry bulk commodities similar to those specified by CLAIMANT. Within this range, there were no limitations for RESPONDENT to disclose. Outside this range there were many limitations. For instance, the machines were not suitable for packaging raw meat, footballs, furniture, or nuclear materials. These materials fall outside the types of items described by CLAIMANT, but at its most broad interpretation they fall within the phrase "wide range of products." The CISG was drafted with the needs and requirements of international business in mind. [*Secretariat Commentary to Draft Art. 6 (counterpart to Art. 7 CISG)*]. RESPONDENT could not reasonably be expected to clarify every possible phrase used and was entitled to rely on clarifications made by CLAIMANT. [*See, e.g., Schmidt v. Textil-Werke (Switzerland); OLG Koblenz, 11 Sept. 1998 (Germany) (seller not liable for buyer's failure to inform seller of fact that the dryblend chemical was not suitable for producing plastic tubes in the buyer's manufacturing facilities)*].

4. *No particular purpose of packaging salt was made known to RESPONDENT at the conclusion of the contract.*

**19.** The CISG states that goods must be "fit for a particular purpose expressly or impliedly made known to the seller at the time of the conclusion of the contract." [*Art. 35(2)(b) CISG*]. "A contract is concluded at the moment when an acceptance of an offer becomes effective." [*Art. 23 CISG*]. "An acceptance of an offer becomes effective at the moment the indication of assent reaches the offeror." [*Art. 18(2) CISG*]. CLAIMANT's Acceptance, dated 12 July 2002, thus concluded the contract. [*Claimant's Ex. 3*]. CLAIMANT admits that no mention of salt was made until the telephone call of 23 July 2002, [*Notice of Arbitration ¶ 7*], which was well after the conclusion of the contract. As a result, the contract contained no requirement that the Model 14 machines conform to a particular purpose of processing salt.

5. *The original contract was never modified to require machines with the ability to process salt.*

**20.** “A contract may be modified or terminated by the mere agreement of the parties.” [*Art. 29(1) CISG*]. “Modification or termination of the contract is governed by CISG rules on formation of contract (Arts. 14 and seq. CISG).” [*T. S.A. v. R. Établissement (Switzerland)*]. However, a party must have sufficient notice of a proposal to modify in order for that proposal to be valid. [*Supermicro Computer v. Digitechnic (U.S.A.)* (applying CISG)]. In the instant case, RESPONDENT did not have sufficient notice of any intention by CLAIMANT to modify the contract to require the machines to process salt. The purpose of CLAIMANT’s call on 23 July 2002 was to check on the status of the order, not to propose a modification. [*Notice of Arbitration ¶ 6*]. As the transcript of the telephone call shows, CLAIMANT embedded the word “salt” between the words “large beans” and “fine products.” [*Statement of Defense ¶ 6*]. Taken together, and especially considering that in a typical telephone call it is common to not “hear” every word that is spoken, it is understandable how RESPONDENT’s Mr. Drake may not have actually heard the word “salt”.

**21.** Even if CLAIMANT’s actions were held to be adequate notice of a proposal to modify, the proposal was not sufficiently definite. Under the CISG, “a proposal is sufficiently definite if it indicates the goods and expressly or implicitly fixes or makes provision for determining the quantity and the price.” [*Art. 14(1) CISG*]. CLAIMANT never stated that it planned to use RESPONDENT’s machines to package salt. CLAIMANT simply said that it would be using our machines to “help” in the fulfillment of a customer order. [*Statement of Defense ¶ 6* (emphasis added)]. CLAIMANT never gave RESPONDENT reason to assume that it was largely inexperienced in the industry, nor did it give RESPONDENT reason to assume specifically that it had never packaged salt. CLAIMANT mentioned three products that encompassed the range of products that it was to pack in the fulfillment of a customer order. Within this range, CLAIMANT mentioned that “some of this is stuff we’ve never handled before.” [*Id.*]. Since the range mentioned in the 23 July 2002 call was so broad, it was understandable that CLAIMANT may not have had experience with all the products within the range. As this range was entirely different from the range CLAIMANT specified in the Invitation, it was reasonable for RESPONDENT to conclude that CLAIMANT knew of the inherently corrosive qualities of salt and that CLAIMANT would not intend to use machines for that purpose unless they were specifically designed and ordered for such purpose.

22. Finally, even if the Tribunal were to find that there was a valid proposal to modify under Article 14(1), RESPONDENT never agreed to the modification. Under the CISG, “an oral offer must be accepted immediately unless the circumstances indicate otherwise.” [Art. 18(2) CISG]. In the instant case, CLAIMANT’s statement about salt was made orally by telephone. “Most acceptances are in the form of a statement by the offeree indicating assent to an offer.” [Secretariat Commentary to Draft Art. 16 (counterpart to Art. 18 CISG)]. RESPONDENT did not make such a statement, and did not in fact reply to the statement about salt during the 23 July telephone conversation. [Proc. Order 3, Clarification 22].

23. The CISG establishes that “silence or inactivity does not in itself amount to acceptance.” [Art. 18(1) CISG]. The CISG allows for acceptance by performing an act, such as shipping the goods *in response to* an offer. [Art. 18(3) CISG (emphasis added)]. In the instant case, it is true that RESPONDENT shipped the machines after CLAIMANT’s phone call. However, it is not true that RESPONDENT shipped the machines *in response to* CLAIMANT’s phone call. Although Article 29 CISG “is intended to override the rule applied in many common law jurisdictions, that a modification agreement is not binding as a contract unless the promise for whose benefit the agreement is made furnishes new consideration,” [Bianca/Bonnell 240], a party’s pre-existing contractual obligation cannot be interpreted as an acceptance of the proposal to modify without further indications of assent. [Chateau Des Charmes Wines v. Sabate (U.S.A.) (applying CISG); OG Basel, 5 Oct. 1999 (Switzerland); HG Zürich, 10 July 1996 (Switzerland)]. In the instant case, RESPONDENT shipped the machines because it was obligated to do so under its original contract. Performing an act that would happen regardless of an offer or proposal to modify cannot constitute valid assent. [Id.]. “The offeree also must manifest an intent to accept it.” [The Law of Contracts § 2.13]. For example, it is well settled that if an offer specifies that if you breathe you assent, then continuing to breathe is not a manifestation of the intent to accept the offer since breathing is not an *intentional* act. [Towle 98 (emphasis added)].

**B. The machines conformed with the contract because their packing speeds reflected the speed of machines of the same kind.**

1. *The machines were of the quality required by the contract.*

24. In the instant case, the contract was formed for six Model 14 dry bulk packaging machines. The Model 14 machines contain an unpolished product path. The price paid by CLAIMANT

reflects this characteristic. CLAIMANT did not request, nor was the contract formed, for machines with a different product path. CLAIMANT only mentioned price and delivery as “essential elements” of its purchasing decision. [*Claimant’s Ex. 1*]. The Model 14 machines were the least expensive machines RESPONDENT could offer at the time of CLAIMANT’s Invitation, [*Proc. Order 3, Clarification 33*], were available for immediate shipment, [*Claimant’s Ex. 2*], and were capable of packaging all of the goods within the range stated by CLAIMANT [*see supra § I.A.1*].

a) The adequacy of the Model 14 machines’ processing speed must be judged by comparison to machines of a similar design.

**25.** The processing speeds of the Model 14 machines should be compared to the processing speeds of similar machines and not to machines having polished product paths. Under the CISG, the seller has a duty to deliver goods of the quality required by the contract. [*Art. 35(1) CISG*]. Sellers have an obligation to deliver goods at least of average fitness. [*Enderlein/Maskow 144*]. The CISG permits variations in quality, as long as they do not fall substantially below the standard that can reasonably be expected according to the price and other circumstances. [*Netherlands Arbitration Institute, 15 Oct. 2002; BG, 28 Oct. 1998 (Switzerland); Enderlein/Maskow 144*].

**26.** Based on the report of the expert appointed by the Tribunal, CLAIMANT argues that RESPONDENT delivered auger-feeder machines that were below industry average for processing speeds. [*Memorandum for Claimant ¶¶ 39-43*]. Although RESPONDENT is not challenging the data contained in the expert’s report, RESPONDENT would like to point out that the expert’s report incorrectly compared the processing speeds of the Model 14 machines, which have an *unpolished* product path, with auger-feeders containing a *polished* product path. [*Engineer’s Report*]. Auger-feeders with a *polished* product path have average processing speeds of 180 bags per minute for both fine and coarse products. [*Engineer’s Report*]. According to the expert, the reason the Model 14 machines did not reach such average processing rates during testing is “due to the fact that the metal parts of the product paths within the machine are not highly polished” and “similar machines are available with highly polished and chromium plated product paths.” [*Engineer’s Report*]. However, machines with highly polished and chromium plated product paths are not similar to the Model 14 machines. The

appropriate comparison should have been between processing speeds of Model 14 machines and other similar machines with *unpolished* product paths. Certainly the Tribunal can appreciate that it would be incorrect for a buyer to pay for an old workhorse and then demand the performance of a champion racehorse. As a result, the Engineer's Report does not support CLAIMANT's assertion that the Model 14 machines performed below the industry standard for auger-feeder machines.

b) CLAIMANT erroneously states the quality standard that applies under the CISG.

27. CLAIMANT argues that the Model 14 machines did not comply with contractual requirements because they seemed slower than *one* other auger-feeder machine previously owned by CLAIMANT. [*Memorandum for Claimant* ¶ 44 (emphasis added)]. Nowhere in the CISG is there support for the proposition that, absent an express contractual provision, sellers have a implied duty to provide goods of the same or faster speeds as any other goods previously owned by the buyer. Also, in the instant case CLAIMANT repeatedly now emphasizes its lack of experience, [*see Memorandum for Claimant* ¶¶ 29, 31, 44], which calls into question the reasonableness of CLAIMANT's expectations regarding the machines.

c) Even if 180 bags per minute is the average industry rate for fine products, the rate for the Model 14 machines falls within an acceptable range of deviation.

28. CLAIMANT further argues that “the Model 14 machines were ‘noticeably below the average industry rate of 180 bags per minute for both coarse and fine products’ according to the opinion of the expert appointed by the Tribunal.” [*Memorandum for Claimant* ¶ 39]. CLAIMANT misstates the expert's report, since the report expressly mentioned that processing speeds for coffee beans—a coarse product—met average industry rates. [*Engineer's Report*].

29. Even assuming, arguendo, that the Engineer's Report was accurate, the Model 14 processing speeds for coarse products were acceptable. For coffee beans, the Engineer found that the processing speed met average industry rates. [*Engineer's Report*]. For polished rice, there was a 2.8 to 5.6% deviation from the average industry rates. Deviations are acceptable since quality levels may be somewhat higher or lower, as long as they do not fall substantially below the standard that can reasonably be expected according to the price and other circumstances. [*Netherlands Arbitration Institute, 15 Oct. 2002; BG, 28 Oct. 1998 (Switzerland); Enderlein/Maskow 144*]. In the instant case, CLAIMANT paid a special discount price for a

discontinued machine with immediate shipment. [*Claimant's Ex. 2*]. In light of these circumstances, a deviation of 2.8 to 5.6% for one type of product is not unreasonable. This is supported by existing case law. The German Supreme Court held that a seller who delivered mussels containing a cadmium concentration exceeding the limit recommended by the German health authority was not in breach of contract since the buyer did not inform seller of the limits and the product was still edible. [*BGH, 8 Mar. 1995 (Germany)*]. In another case, considering that the buyer had not provided the seller with information regarding the manner in which the fabrics had to be cut in order to be economical and that the fabrics were suitable for the production of skirts and dresses, the court found that the fabrics conformed to the contract. [*LG Regensburg, 24 Sept. 1998 (Germany)*]. Finally, another court found that the buyer did not prove that the sheep were nonconforming since the buyer failed to prove that it made seller aware that the sheep needed to be ready for slaughter upon delivery. [*OLG Schleswig, 22 Aug. 2002 (Germany)*].

2. *RESPONDENT did not make any warranties regarding the machines' processing speed.*

**30.** CLAIMANT relies on Uniform Commercial Code 2-313(1)(a) to support its contention that RESPONDENT created an express warranty regarding processing speed by the use of the words “top products” and “complete satisfaction.” [*Memorandum for Claimant* ¶¶ 42-43]. The CISG has abandoned traditional notions of warranty found in various domestic laws and has replaced it with a unitary notion of conformity. [*Supermicro Computer v. Digitechnic (U.S.A.); G. & C. v. I (Switzerland)*]. If the UCC is taken into consideration, however, it actually supports RESPONDENT’s position. UCC 2-313(2) provides that “an affirmation merely of the value of the goods or a statement purporting to be merely the seller’s opinion or commendation of the goods does not create a warranty.” UCC 2-313 Official Comment 8 further clarifies that some statements or predictions cannot fairly be viewed as entering into the bargain.

**31.** The law recognizes that reasonable consumers would not take RESPONDENT’s sales “puffing” literally. Puffing refers to “loose general statements made by sellers in commending their products. These statements embody exaggerations, the truth or falsity of which cannot be determined easily, that amount to no more than an expression of the seller’s opinion about the character or quality of the product.” [*Ladd v. Honda Motor (U.S.A.)*]. For example, one court recognized that the statement “you meet the nicest people on a Honda” was puffing and rejected

a warranty claim by a consumer. [*Baughn v. Honda Motor (U.S.A.)*]. Thus, under the UCC, buyers can rely on affirmations of facts about seller's goods but buyers do not have a right to rely on seller's opinion or commendation regarding its product. [*Ladd v. Honda Motor (U.S.A.)*; *Baughn v. Honda Motor (U.S.A.)*]. In the instant case, RESPONDENT's statements—that the machines were “top products” and would deliver “complete satisfaction”—were not affirmations of fact, but rather RESPONDENT's commendation regarding its machines. Therefore, CLAIMANT was not entitled to rely on such statements.

## **II. EVEN IF THE MODEL 14 MACHINES DID NOT CONFORM TO THE CONTRACT, CLAIMANT IS NOT ENTITLED TO RELY ON THE LACK OF CONFORMITY.**

**32.** CLAIMANT is not entitled to rely on the alleged lack of conformity because it failed its duty to inspect (A.) and its duty to mitigate (B.).

### **A. CLAIMANT failed to properly inspect the machines.**

1. CLAIMANT did not conduct an appropriately diligent examination of the machines.

#### a) CLAIMANT failed to conduct a test run.

**33.** The CISG imposes on the buyer a duty to “examine the goods, or cause them to be examined, within as short a period as is practicable in the circumstances.” [*Art. 38(1) CISG*]. RESPONDENT agreed that it would not raise any questions under Article 39 CISG regarding notice of non-conformity [*Proc. Order 2, ¶ 2*]. However, it is well settled that a buyer's duty to inspect under Article 38 CISG is distinct from a buyer's duty to notify. [*Provincial Court of Pontevedra, 3 Oct. 2002 (Spain)*; *OGH, 14 Jan. 2002 (Austria)*; *Shuttle v. Tsonakis (U.S.A.)*; *OLG Koblenz, 18 Nov. 1999 (Germany)*; *Beijing Light Automobile v. Connell (Sweden)*; *Wonderfil v. Depraetere (Belgium)*; *OG Luzern, 8 Jan. 1997 (Switzerland)*; *OLG Saarbrücken, 13 Jan. 1993 (Germany)*].

**34.** “Article 38 does not define the intensity of the examination required.” [*Kuoppala 96*]. The examination must be such as to disclose recognizable defects in light of all the circumstances. [*Kuoppala 97*]. The examination must be “appropriately diligent, even in the case of goods' features that are hard to examine; if necessary, the buyer must call in experts.” [*OGH 27 Aug. 1999 (Austria)*]. In the case of complicated machinery, as is the case in the instant dispute, the

buyer must conduct a test run in order to confirm that the machine functions properly. [*OGH*, 27 Aug. 1999 (Austria); *OLG Oldenburg*, 5 Dec. 2000 (Germany)].

**35.** CLAIMANT acknowledges that the machines “worked reasonably well in the beginning.” [*Notice of Arbitration* ¶ 8]. It was not until CLAIMANT received the Engineer’s Report that CLAIMANT contended that the processing speeds of the machines were *noticeably* below industry average. [*Memorandum for Claimant* ¶ 39]. Thus, it can be inferred that CLAIMANT did not conduct a test run to prior to receiving the Engineer’s Report. Since CLAIMANT failed to properly examine the machines by conducting a test run and used the machines until they were so corroded that they could not be repaired or replaced, [*see Proc. Order 3, Clarifications 28-29*], the Tribunal should find that CLAIMANT was “no longer in a position to complain ... Otherwise, its behaviour would be contradictory and would constitute a violation of the principle of good faith” under Article 7(1) CISG. [*LG Saarbrücken*, 26 Mar. 1996 (Germany)].

b) CLAIMANT failed to examine the machine diligently for compatibility with highly corrosive products.

**36.** CLAIMANT argues that it did not know that salt is “so corrosive that it would require special equipment to handle it” and that if it had known, it “would certainly not have used the Model 14 machines for packing salt without first making sure that they were appropriate for that purpose.” [*Proc. Order 3, Clarification 14*]. However, CLAIMANT could not have been unaware that the machines were very likely to be inappropriate for such use.

**37.** Several factors would have alerted a reasonable person in CLAIMANT’s position that salt was likely to corrode the machines. First, CLAIMANT’s own admissions indicate that it knew that salt was corrosive, but erroneously thought it was not so corrosive as to damage the machines. [*Claimant’s Ex. 5; Proc. Order 3, Clarification 14*]. Second, the operations manual that was shipped with the machines stated that the machines were “not intended for use with highly corrosive products.” [*Proc. Order 3, Clarification 25*]. Of the spectrum of products that CLAIMANT processed, salt was the most corrosive. Certainly when compared to other dry foodstuffs, salt is highly corrosive. Although the manual was not expressly included in the contract, technical instructions contained in a manual are implicitly included since without them a buyer is unable to make a proper examination of the goods. [*Pelliculest v. Morton (France); Kuoppala 115*]. Third, there was no mention of salt or any corrosive products in the Invitation,

Offer, or Acceptance. Lastly, although the buyer is entitled to a good bargain, the price paid per machine was highly inconsistent with CLAIMANT's assumption that the machines could process salt.

**38.** In light of these factors, a reasonable person in CLAIMANT's position would have been alerted about the machine's potential inability to handle salt and would be under a duty to inspect the machines before using them to process salt. Since corrosion is a gradual process [*Proc. Order 3, Clarification 28*], a test run would not be adequate. Since different metals may have similar appearances, a visual inspection may not detect whether the machine's product path is able to process salt. As CLAIMANT itself admits, such duty to inspect would at least require CLAIMANT to call RESPONDENT to inquire about processing salt with the machines [*Proc. Order 3, Clarification 14*].

**39.** Alternatively, since CLAIMANT did not have the apparent expertise to examine the machines for incompatibility with highly corrosive products, CLAIMANT should have hired someone who did. This result is consistent with the Austrian Supreme Court's opinion of 27 August 1999. "[T]he buyer must, in the case of large quantity purchase ... call in experts in the broadest sense ... in order to comply with its obligation to examine" the goods. [*OGH, 27 Aug. 1999 (Austria)*]. It is also consistent with a German case in which the court held that "with characteristics of the goods that are difficult to inspect (such as technically complicated functions), the buyer may have to bring in experts." [*OLG Oldenburg, 5 Dec. 2000 (Germany)*]. CLAIMANT's failure to examine the machines would be irrelevant "only if the defect could only have been determined by an expert." [*OLG Jena, 26 May 1998 (Germany)*]. In the instant case, an expert or a simple call to RESPONDENT would have revealed the machine's inability to process salt.

*2. Even if CLAIMANT did conduct an appropriately diligent examination, the length of the examination period was unreasonably long.*

**40.** Article 38 CISG requires examination within as short a period as is practicable in the circumstances. [*LG Aachen, 3 Apr. 1990 (Germany); Kuoppala 105*]. The inspection period begins the moment the goods are made available to the buyer at the place of delivery. [*OGH, 14 Jan. 2002 (Austria); OLG Oldenburg, 5 Dec. 2000 (Germany); Kuoppala 115-16*]. The duration of the examination period depends on the objective conditions of the individual case, "especially

regarding the type of goods and defect, as well as the necessities and time expenditure required, as for instance with technical test procedures, test runs, etc.” [OGH, 14 Jan. 2002 (Austria)]. Courts have found that the buyer is obligated to conduct a test run or other diligent inspection within one to two weeks of delivery. [Id.; OLG Koblenz, 11 Sept. 1998 (Germany); OLG Oldenburg, 5 Dec. 2000 (Germany) (tiller machine)]. Moreover, “disorganisation on the part of the buyer was not an aspect to be considered in determining the period practicable in the circumstances” under Article 38(1) CISG. [OLG Koblenz, 11 Sept. 1998 (Germany)].

**41.** In the instant case, the machines were delivered on 21 August 2002. [Notice of Arbitration ¶ 8]. CLAIMANT admits that the machines were not installed until 30 August 2002. [Id.]. This implies that CLAIMANT could not have conducted a test run until after 30 August 2002, nine days after delivery—a period that has been held to be too late. [OLG Koblenz, 11 Sept. 1998 (Germany)]. Nor is there evidence that CLAIMANT performed a diligent inspection, [see supra ¶¶ 33-36], within the two week window provided by OLG Oldenburg, 5 Dec. 2000 (Germany). Thus, under existing case law, CLAIMANT did not comply with the examination requirements of Article 38 CISG. As a result, CLAIMANT is not entitled to rely on any alleged lack of conformity.

#### **B. CLAIMANT failed to mitigate damages.**

**42.** The CISG states that “a party who relies on a breach of contract must take such measures as are reasonable in the circumstances to mitigate the loss.” [Art. 77 CISG]. The UNIDROIT also imposes a duty to mitigate damages, establishing that “the non-conforming party not liable for harm suffered by the aggrieved party to the extent that the harm could have been reduced by the latter party’s taking reasonable steps.” [Art. 7.4.8 UNIDROIT].

**43.** Here, The machines were placed in service by the end of August. [Notice of Arbitration ¶ 8]. CLAIMANT states that by the end of September the machines were so seriously corroded that they could no longer be used. [Id.]. It can be inferred that mild corrosion must have been present long before the end of September. This is further strengthened by CLAIMANT’s own statement that, before the corrosion had reached its most serious stage, “the corrosion made it impossible to clean the feeding surfaces properly.” [Claimant’s Ex. 6]. In spite of the progressive corrosion, CLAIMANT continued to use the machines until the product paths were so damaged that they could no longer be repaired or replaced. [Proc. Order 3, Clarification 29].

If CLAIMANT had taken reasonable steps to mitigate damages, as required by Article 77 CISG and Article 7.4.8 UNIDROIT, it would have refrained from further using the machines as soon as it noticed that they were being damaged. CLAIMANT's failure to act reasonably significantly increased the damages now claimed. As a result, CLAIMANT should not be entitled to recover the damages directly caused by its own unreasonable actions. *[BGH, 24 Mar. 1999 (Germany)]*.

### **III. EVEN IF THE TRIBUNAL FINDS THAT RESPONDENT COMMITTED A BREACH OF CONTRACT, THE BREACH WAS NOT A FUNDAMENTAL ONE.**

44. As discussed above, *[see supra § I]*, RESPONDENT did not breach its contract with CLAIMANT. However, even if the Tribunal were to determine that there was a breach of contract, that breach was not fundamental. A breach is only considered fundamental if it "results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract" and if that result would have been foreseeable to a reasonable party in the breaching party's position. *[Article 25 CISG]*. The CISG has a general policy in favor of the preservation of contracts; hence, it disfavors findings of fundamental breach. *[Duncan 1379,1410; Perillo 303; Pauly 225; Hillman 30; Piche 531; Jacobs 408]*.

45. Applying these basic principles, it is clear that no fundamental breach occurred in the present case. First, CLAIMANT was not substantially deprived of what it was entitled to expect under the contract (A.). Second, the possibility that CLAIMANT would suffer substantial deprivation was not reasonably foreseeable to RESPONDENT (B.).

#### **A. RESPONDENT did not substantially deprive CLAIMANT of what it was entitled to expect.**

46. The party alleging a fundamental breach has the burden of proving that it suffered substantial deprivation. *[Honnold (2) 209; Kazimierska 109; Will 216]*. The focus of Article 25 is not merely on the extent of the harm by itself, but on the objective importance of the interest to the contracting party. *[Piche 530; Schlechtriem 177; Romito/Sant'Elia 198]*. To prevail, CLAIMANT would have to show that the deprivation caused by RESPONDENT's breach was so substantial that its contracting purpose was foiled. *[Enderlein/Maskow 112, 115; Fagan 338; Piche 529; Schlechtriem 177; BG, 15 Sept. 2000 (Switzerland)]*. CLAIMANT has failed to do so.

1. *RESPONDENT's delivery of allegedly nonconforming machines did not substantially deprive CLAIMANT of what it was entitled to expect.*

47. CLAIMANT alleges that RESPONDENT substantially deprived it of what it expected under the contract by supplying machines that were not designed to process salt and that were slightly below the average industry processing speed. [*Memorandum for Claimant ¶48*]. These alleged nonconformities were in no way substantial. The opposite is true; the machines did nearly everything that CLAIMANT expected them to do.

48. CLAIMANT specified only “price and prompt delivery” as the “essential elements” of the contract. [*Claimant's Ex. 1, 5*]. The Model 14 machines delivered by RESPONDENT fully complied with both of these “essential elements.” Importantly, neither ability to process salt nor the processing speed of the machines was ever mentioned by CLAIMANT during the contract negotiations. If these features had been crucial to CLAIMANT's contracting purpose, it should have made inquiries about them, particularly in light of RESPONDENT's disclosure that the Model 14 was a discontinued model. [*Claimant's Ex. 2*]. Accordingly, the Tribunal should reject CLAIMANT's arguments that the machines' processing capabilities substantially foiled its original contracting purpose.

49. Looking specifically at the issue of salt-processing capability, it must be stressed that CLAIMANT was not seeking to purchase machines for the sole purpose (or even for the primary purpose) of packing salt. CLAIMANT stated only that its purpose in contracting was to purchase machines that could “be used over a wide range of products.” [*Claimant's Ex. 1*]. Salt was simply one of a multitude of products being packaged by CLAIMANT. [*Notice of Arbitration ¶ 8*]. Since the machines were perfectly capable of packing a wide variety of other products, such as coffee, beans, and rice, CLAIMANT's contracting purpose was not frustrated. Where the machines are substantially in conformity with the contract and are usable for most of the buyer's purposes, there is no fundamental breach of contract. [*Enderlein/Maskow 115; Piche 535*].

50. With regard to the speed of the machines at the time of delivery, it is difficult to ascertain what detriment CLAIMANT has suffered except to the extent that slower machines are not worth quite so much as faster ones. As discussed above, the Engineer's Report failed to compare the Model 14 machines with truly similar machines. [*See supra § I.B.1.a*]. However, even accepting CLAIMANT's highly questionable assertion that the contract called for machines with

a processing speed of 180 bags per minute, RESPONDENT's delivery of machines that performed at or moderately below that standard when packing certain products can hardly be considered a substantial deprivation of CLAIMANT's expectation. The performance of the Model 14 met the purported standard for coffee beans. [*Id.*]. For polished rice and ground coffee, the Engineer's Report showed that the machines achieved rates between 130 to 175 bags per minute. Since the industry average rate is less than 180 bags per minute, the maximum amount of the machines' deviation amounts to 28% (130 bags per minute versus 180 bags per minute). The Supreme Court of Switzerland found that a 26% deviation did not amount to a substantial deprivation of the CLAIMANT's expectancy. [*BG, 28 Oct. 1998 (Switzerland)*]. Similarly, in this case, CLAIMANT has not presented any evidence whatsoever that the packing speed of the machines caused it *any* actual harm, much less substantial detriment.

**51.** In any event, damages could fully compensate CLAIMANT for either of the alleged contract breaches. As CLAIMANT itself admits, both courts and scholars have found that there is no fundamental breach when the goods are "reasonably resalable." [*Memorandum for Claimant ¶ 49; OLG Stuttgart, 12 Mar. 2001 (Germany); BGH, 3 Apr. 1996 (Germany); Romito/Sant'Elia 198*]. Even where damage is not reparable, courts and commentators refuse to characterize detriment as "substantial" where damages would be an appropriate remedy. [*BGH, 3 Apr. 1996 (Germany); Piche 531; Schlechtriem 183; West/Ohnesorge 82*]. The machines were fully functional and thus had substantial market value at the time they were delivered. Any difference between that value and the value of the machines that CLAIMANT was supposedly entitled to could easily be made up by monetary damages.

2. *RESPONDENT was not responsible for any harm suffered by CLAIMANT after delivery.*

**52.** CLAIMANT also asserts that it suffered substantial economic loss because the machines were completely destroyed by the salt it processed. [*Memorandum for Claimant ¶ 49*]. It further argues that its contracting purpose was frustrated because it was unable to satisfy its contract with A2Z Corp. [*Memorandum for Claimant ¶ 48*]. Neither of these claims stands up to scrutiny.

**53.** The damage caused to the machines was a direct result of CLAIMANT's negligent actions, namely its packaging of a corrosive material in clear violation of the machines' specifications, [*Engineer's Report; Proc. Order 3, Clarification 25*], and its failure to make an adequate

inspection, *[see supra § II.A]*. Even though CLAIMANT had evidence of the corrosion of the machines long before it reached the current extent, *[Claimant's Ex. 6]*, there is no evidence that CLAIMANT attempted to contact RESPONDENT or any other experts until the machines were seriously damaged. Thus it was not RESPONDENT's actions, but rather CLAIMANT's, that are to blame for the damage.

**54.** Moreover, even if RESPONDENT were to blame for the current state of the Model 14 machines, damages would be sufficient to compensate CLAIMANT for any harm suffered. CLAIMANT incorrectly states that it is now impossible for the machines to be put to any "reasonable use." *[Memorandum for Claimant ¶49]*. In fact, at least two Model 14 machines are currently usable for production line packaging. *[Engineer's Report]*. Moreover, even if the other four machines are not presently usable, damages could easily compensate any of CLAIMANT's losses. Avoidance is not appropriate in such a situation.

**55.** CLAIMANT also alleges that the purpose of its contract with RESPONDENT was "frustrated since CLAIMANT was unable to satisfy the main contract with A2Z." *[Memorandum for Claimant ¶48]*. However, CLAIMANT presents no evidence for this proposition beyond than the bare assertion of its counsel. *[See Letter of Joseph Langweiler, 24 Sept. 2003]*. Furthermore, even if it is true that CLAIMANT was unable to satisfy its contract, it has only itself to blame; as explained above, the damage to the machines was a result of CLAIMANT's misuse of the machines and failure to conduct a proper inspection. *[See supra ¶ 53]*.

**B. No "substantial detriment" to CLAIMANT was foreseeable to RESPONDENT.**

**56.** Even if CLAIMANT were able to persuade the Tribunal that RESPONDENT caused it substantial detriment, CLAIMANT could not prove its claim of fundamental breach unless the detriment was foreseeable to a reasonable person in RESPONDENT's circumstances. *[Art. 25 CISG; Duncan 1379; Koch 265]*. Since none of the harm of which CLAIMANT complains was objectively or subjectively foreseeable, its claim must fail.

**57.** Article 25 CISG does not explicitly state the relevant time for applying the foreseeability inquiry. *[Gabriel 295]*. The majority of commentators agree that the relevant question is whether the harm could reasonably have been foreseen at the *formation* of the contract. *[Enderlein/Maskow 116; Koch 266; Piche 530; Schlechtriem 180; Speidel 440-442; Will 220]*.

In the discussions leading up to the formation of the contract, CLAIMANT made no mention of any need for salt-packaging or processing-speed capabilities. Hence, RESPONDENT had no reason to foresee that CLAIMANT might suffer substantial detriment if the machines did not meet its expectations in these areas. While CLAIMANT did state that it needed machines that could process “a wide range of products,” [*Claimant’s Ex. 1*], the examples given by Mr. Swan were noncorrosive products. A reasonable person in RESPONDENT’s position would not have expected CLAIMANT to package highly corrosive products like salt unless specifically mentioned.

**58.** CLAIMANT relies heavily on a single statement made by Mr. Swan that its customer had “everything in mind from large beans to salt to fine powder and we are going to have to do it all.” [*Statement of Defense ¶6*]. Applying the majority rule above, it is clear that this statement is irrelevant to the foreseeability inquiry. A few commentators do suggest that statements made after the conclusion of the contract can be taken into consideration, [*see Honnold (2) 208-209; Koch 265, 231*], but this is viewed as undesirable because it can lead to unpredictable changes in risks and obligations. [*Schlechtriem 180-181; Speidel 440-442*]. Nevertheless, even applying the minority rule, Mr. Swan’s statement was insufficient to convey to RESPONDENT that CLAIMANT would be using the Model 14 machines to package salt. Mr. Swan merely stated that RESPONDENT’s machines would “help us” with the packaging of various products. Given that specialized salt-packaging equipment is available, the most reasonable conclusion for RESPONDENT to draw was that its machines would be used in combination with *other* machines to “help” CLAIMANT complete the order.

**59.** Even if it had been foreseeable that CLAIMANT would use the machines to package salt, the extent of the damage caused here was not reasonably foreseeable. If CLAIMANT had acted in accordance with its duty to mitigate damages, [*Art. 77 CISG*], it would taken action when it noticed that the machines were becoming corroded. [*See Notice of Arbitration ¶8*]. Instead, CLAIMANT simply ignored the problem and continued to use the machines, thereby exacerbating the problem until the machines were unusable for packaging food. [*Claimant’s Ex 6*]. This unreasonable behavior can hardly be considered foreseeable.

#### **IV. REGARDLESS OF WHETHER RESPONDENT COMMITTED A FUNDAMENTAL BREACH, CLAIMANT DID NOT MAKE AN EFFECTIVE AVOIDANCE.**

**60.** CLAIMANT purports to have avoided the contract under Article 49(1) CISG. [*Memorandum for Claimant 59-60*]. This is not the case, even assuming for the sake of argument that RESPONDENT committed a fundamental breach. First, CLAIMANT lost the right to avoid the contract because it was unable to return the goods to RESPONDENT in the condition in which they were received (A.). Second, it did not make an adequate valid declaration of avoidance (B.).

##### **A. CLAIMANT lost the right to avoid because it was unable to return the goods in substantially the condition in which they were received.**

**61.** A buyer loses the right to declare the contract avoided if “it is impossible for him to make restitution of the goods substantially in the condition in which he received them.” [*Art. 82(1) CISG*]. Both parties recognize that the machines are now severely corroded and not in the condition in which they were received. [*Claimant’s Ex. 6; Statement of Case ¶8*].

**62.** CLAIMANT nonetheless suggests that it retains the right to avoid under Article 82(2)(c), [*see Memorandum for Claimant ¶63*], because the change in the condition of the goods occurred “in the course of normal use before he discovered or ought to have discovered the lack of conformity.” [*Art. 82(2)(c) CISG*]. CLAIMANT makes no argument that its action in using the machines to process salt constituted “the course of normal use.” Hence, CLAIMANT has failed to meet its burden of proof. [*OLG Stuttgart, 12 Mar. 2001 (Germany)*].

**63.** Furthermore, CLAIMANT fails to address the fact that it continued to use the machines (whether or not in the course of normal use) after it had reason to discover any nonconformity. The processing limitations of the Model 14 machines should have been clear to CLAIMANT at the time of delivery. CLAIMANT admits that it noticed “at the beginning” that the machines “were slower for most products than had been [its] previous experience with similar machines.” [*Notice of Arbitration ¶8*]. Yet it continued to use machines for over a month after the machines were placed into service, thereby altering their condition. [*Id.*]. Hence, CLAIMANT lost any right to rely on the processing speed of the machines as a ground for avoidance.

**64.** With regard to the salt, first, the fact that the Model 14 machines were not made of stainless steel should have been apparent to CLAIMANT through the inspection that CLAIMANT was

obligated to perform. [*Art. 38 CISG; OLG Stuttgart, 12 Mar. 2001 (Germany)*]. Second, the warning labels on the machines were sufficient to alert the buyer that these machines were not suitable for processing salt. [*Proc. Ord. 3 ¶25*]. Third, before corrosion reached the current levels CLAIMANT observed that the machines it was using to process salt were becoming corroded [*Claimant's Ex. 6*] which was a further warning sign of any lack of conformity. Any one of these factors standing alone should have alerted CLAIMANT to the fact that the Model 14 machines were not capable of handling salt. However, well after it should have discovered this fact, CLAIMANT continued to use the machines. [*Claimant's Ex. 6*]. In doing so, it lost the protection of Article 82(2)(c) CISG and with it any right to avoid the contract. [*OLG Stuttgart, 12 Mar. 2001 (Germany)*].

#### **B. CLAIMANT did not avoid the contract.**

**65.** Even if CLAIMANT had the right to avoid, it did not make a valid exercise of that right. First, its purported declaration of avoidance was inadequate (1.); second, its declaration was untimely (2.).

##### *1. CLAIMANT's failed to give effective notice of its intent to avoid.*

**66.** A buyer who wishes to avoid the contract must communicate a declaration of that avoidance to the other contracting party. [*Art. 26 CISG; Huber 424-425; Jacobs 407-408*]. The burden of proving that an adequate declaration of avoidance was made falls upon the party making the declaration. [*Huber 425*]. The notice “must satisfy a high standard of clarity and precision.” [*Leser 189; see also Jacobs 410*]. Especially where the goods have already been delivered, indirect notice of avoidance, such as the return of the goods to the seller, fails to satisfy the requirements of Article 26 CISG. [*Date-Bah 224; Enderlein/Maskow 117; Leser 189*]. Notice of avoidance is generally inadequate when the buyer fails to specifically state that it is avoiding the contract. [*LG Frankfurt, 16 Sept. 1991 (Germany)*]. Such a case presents itself here.

**67.** CLAIMANT incorrectly suggests that “[e]ven though some very isolated case law holds that according to Art. 26 CISG the buyer’s notice of declaration of avoidance must represent ... a clear intention to avoid the contract, the majority of case law confirms the absence of a requirement for a fixed form.” [*Memorandum for Claimant ¶56*]. In fact, virtually all courts and commentators have required at a minimum that a clear intention to avoid be displayed in the

declaration of avoidance. [*Date-Bah* 223-225; *Enderlein/Maskow* 116-117; *Jacobs* 409, 428; *Huber* 425; *Leser* 188-189; *Romito/Sant'Elia* 200]. The German case to which CLAIMANT refers, [*see Memorandum for Claimant ¶56*], is in fact an application of the general rule that indirect notice of avoidance is inadequate. [*AG Zweibrücken, 14 Oct. 1992 (Germany)*]; *see also LG Frankfurt, 16 Sept. 1991 (Germany)*]. Exceptions to this rule have only been made in extreme circumstances, which are not present here. [*See, e.g., Roder v. Rosedown Park (Australia)*]; *OLG Hamburg, 28 Feb. 1997 (Germany)*].

**68.** Indeed, the case to which CLAIMANT refers presents a factual situation indistinguishable in material respects from the current case. The German court specifically held that a complaint about the goods coupled with a suggestion that the buyer take back the goods was inadequate notice of avoidance. [*AG Zweibrücken, 14 Oct. 1992 (Germany)*]. Similarly, CLAIMANT bases its claim of avoidance on Mr. Swan's written statement that CLAIMANT no longer wanted the machines and that RESPONDENT could dispose of them at will. [*Claimant's Ex. 6; Memorandum for Claimant ¶59*]. Following the reasoning of the German case, there is no question that the purported notice of avoidance given by CLAIMANT was inadequate.

2. *CLAIMANT's purported declaration of avoidance was not timely.*

**69.** If a valid declaration of avoidance is not made within a reasonable time after the buyer knew or ought to have known of the breach, right to avoid lapses. [*Art. 49(2)(b)(i) CISG; Leser* 189]. Where the defect is hidden, courts limit the concept of a "reasonable time" to a few days after the breach did or ought to have become apparent. [*LG Ellwangen, 21 Aug. 1995 (Germany)*]. If the buyer delays for longer, its declaration will be untimely and therefore ineffective. [*HG Zürich, 26 Apr. 1995 (Switzerland)*]. Even if the Tribunal determines that RESPONDENT knew of a defect in the product, CLAIMANT is still required to make a declaration of avoidance within "reasonable time" in order to retain the right to avoid. [*Honnold (2) 333*].

**70.** Here, CLAIMANT's purported declaration of avoidance was not made within a reasonable time. Where defects should have been immediately apparent or were discernible from a simple inspection, the "reasonable time" will begin to run from the time that the buyer is obligated to carry out a reasonable inspection. [*Art. 39 CISG; Honnold (2) 331*]. As discussed above, [*see supra ¶¶ 63-64*], any defects in the Model 14 machines should have been immediately obvious to CLAIMANT upon undertaking the required inspection. Even CLAIMANT admits that it

realized the supposed defects before the end of September, *[Notice of Arbitration ¶8]*, at least three weeks before its purported avoidance on 19 October. Since CLAIMANT failed to comply with the timeliness requirement of Article 49, its avoidance was ineffective.

## **V. THE TRIBUNAL SHOULD ORDER CLAIMANT TO POST SECURITY FOR COSTS.**

### **A. The Tribunal has jurisdiction to issue an order of security.**

71. As CLAIMANT correctly notes, the Tribunal has the power to decide the matter of security for costs. *[Memorandum for Claimant ¶¶ 64-67]*. The question of arbitral power to order such interim measures may have been controversial in the past, but the current view among commentators is that the jurisdictional issue is settled. *[Rubins 317-327; Werbicki 62-69; Wagoner 68-73]*.

72. Furthermore, the SIAC rules to which both CLAIMANT and RESPONDENT agreed to be bound specifically empower the Tribunal to order security for costs and require parties to waive rights to appeal such orders to another jurisdiction. *[SIAC Rules 27, 26.4]*. Security may be ordered in any “manner the Tribunal thinks fit.” *[SIAC Rule 27.3]*. Further, SIAC Rule 26.3 gives the Tribunal the discretion to “determine any question of law arising in the arbitration ... [and may consider] such written or oral evidence as it shall determine to be relevant, whether or not strictly admissible in law.” Therefore, the SIAC rules allow for the Tribunal’s consideration of both general international practice and equitable consideration when determining awards of security for costs.

### **B. Ordering security for costs is a widely accepted practice in dispute settlement.**

73. Notwithstanding CLAIMANT’s assertions to the contrary, security for costs is not considered “inappropriate in arbitration.” *[Memorandum for Claimant ¶ 68]*. On the contrary, virtually all major international arbitral tribunals are empowered to decide on the appropriateness of security for costs. *[Marchac 129; see SIAC Art. 27.3; Model Law Art.17; ICC Art. 23; AAA Art. 22; LCIA Art. 25.2]*. Many national laws also provide for security for costs to be ordered in arbitration *[Werbicki 69]*. The number of tribunals in international and national arbitration organizations allowing security for costs is also increasing. *[Rubins 313-316]*. This trend of

widespread power to order security for costs suggests that this is an appropriate practice in international arbitration.

**74.** CLAIMANT cites an ICC case indicating a less favorable attitude toward security for costs. *[See Memorandum for Claimant ¶ 68]*. While it is true that certain organizations, including the ICC and the AAA, award security for costs less frequently than others, *[Rubins 337-339]*, the practices of those institutions are based on their particular legal histories and should not be taken as evidence of a general international rule. AAA practice is grounded in the American legal culture, which incorporates the principle that each party generally pays its own costs. *[Rubins 329-330]*. Therefore there has been little reason to order security for costs that are unlikely to be awarded. The ICC's reluctance to order security for costs is also rooted in legal culture; until recent reforms, interim measures in Europe were granted through national courts, not arbitral tribunals, *[Rubins 341; Schwartz 54]*, and the ICC has approached the use of this new jurisdictional power cautiously. However, even these institutions now approach security for costs more favorably. In the U.S., arbitrators and courts are empowered to order interim measures such as security for costs as courts order the losing party to pay costs in some cases. *[Rubins 330]*. Article 28 of the 1998 Rules of the ICC secures arbitrators' jurisdictional authority to order interim measures, and the ICC is increasingly willing to order security for costs in many situations. *[Rubins 340]*.

**75.** The LCIA presents a better model for the SIAC to follow. The legal system of England, from which LCIA developed, has centuries of legal experience awarding costs and is the historical place of origin for the practice of ordering security for costs. *[Altaras 81-84]*. When jurisdictional power over interim awards in arbitration passed from the courts to arbitral tribunals, the legal culture in England influenced arbitrators' willingness to award security for costs in dispute settlement. *[See Rubins 323-327, 342-343]*. Just as the SIAC rules follow the language of the LCIA in empowering the Tribunal to order security for costs, the Tribunal would be well-advised to follow the LCIA's practice by issuing such an order in this case.

**C. An order of security for costs is necessary to protect RESPONDENT's interests.**

*1. CLAIMANT's questionable financial position weighs heavily in favor of an order of security.*

**76.** The practice of awarding the winning party the reasonable expenses of presenting its case is widespread in international arbitration. *[Rubins 312]*. In this case, the financial press has raised

serious concerns about CLAIMANT's financial position which call into question its ability to pay any award of costs ordered by the Tribunal. CLAIMANT's financial difficulties apparently include cash flow problems, delinquency in paying creditors, and apparent unsuccessful attempts to secure financing from banks. [*Letter of Horace Fasttrack, 1 Sept. 2003*]. If RESPONDENT prevails in this dispute and is awarded costs by the Tribunal, that victory will be hollow if it cannot enforce the award due to CLAIMANT's lack of funds.

**77.** Contrary to CLAIMANT's assertions, the financial condition of the parties is a legitimate consideration in determining awards of security for costs. In fact, commentators on the 1997 Guidelines drafted by the Chartered Institute of Arbitrators suggest that the financial condition of the claimant might be the most important factor to consider. [*Rubins 326; see also Schockman v. Hogg ¶¶ 9-12*]. In practice, the ability of a party to fulfill an award of costs against it is a significant consideration in awards for security for costs. [*Redfern/Hunter 7-32*].

**78.** CLAIMANT offers no evidence to deny the reports of financial difficulties beyond the mere assertion that it "would have no difficulty" in paying an award of costs. [*Letter of Joseph Langweiler, 9 Sept. 2003*]. Given that several media sources have raised the issue of CLAIMANT's financial problems, the burden is now on CLAIMANT to show that it is sufficiently solvent.

**79.** Though equitable considerations may discourage arbitrators from security for costs awards that would bar legitimate claims for economic reasons, CLAIMANT has not alleged that security for costs would unjustly bar them from making their claim. [*See Memorandum for Claimant ¶ 83*]. CLAIMANT has made no assertion that it would be unable to pursue this dispute if an order for security for costs is awarded by the Tribunal.

**80.** As the above argument demonstrates, [*see supra § I*] CLAIMANT's financial difficulties are a result of its own conduct, not that of RESPONDENT. However, it is for the Tribunal to decide the merits of this case at its conclusion, not pre-judge whether RESPONDENT's "unsavory" activities caused CLAIMANT's financial hardships, [*Memorandum for Claimant ¶86*], by deciding whether or not to award security for costs.

*2. Concerns over enforcement weigh in favor of ordering CLAIMANT to post security for costs.*

**81.** A security for costs order would circumvent any problems with enforcement that might arise. Despite the fact that Equatoriana is a party to the New York Convention, courts in

Equatoriana have not been rigorous in enforcing awards in cases where the company is in financial difficulties. [*Letter of Horace Fasttrack, 1 Sept. 2003*]. A better solution for enforcement of awards is to remove the responsibility for enforcement from the hands of the national courts altogether. [*Craig 23-26*]. Guaranteeing enforcement through the tool of ordering security for costs would avoid potential political tension between the home nations of the parties. If Equatoriana failed to enforce an award, Mediterreneo could then refuse to enforce arbitral awards to Equatorianan parties, [*see New York Convention art. XIV*], increasing tension between the nations. By contrast, when enforcement is secured through security for costs, future contracting parties in both nations can confidently place their trust in the arbitration process (leading to an increase of cross-border dealings that can benefit both nations).

**82.** The request for security for costs is not, as CLAIMANT suggests, based solely on nationality. [*See Memorandum for Claimant ¶¶ 79-80*]. It is true that basing a request for security solely on the ground of nationality would offend the principle of equal treatment. However, RESPONDENT's request is based not on the fact that CLAIMANT is based in Equatoriana but rather upon reasonable concerns about the feasibility of enforcement.

*3. The merits and good faith of CLAIMANT's action are not a significant factor in this request for security for costs.*

**83.** RESPONDENT is not required to prove that CLAIMANT's assertions are not "*bona fides ... [or] scandalous or oppressive or ... unlikely to find a proper cause of action*" as suggested by CLAIMANT. [*See Memorandum for Claimant ¶ 70*]. The test for an order of security for costs in this international arbitration is likelihood of recovery.

**84.** It is true that an order for security for costs can potentially deter spurious claims. If a claimant company is insolvent, there is potential misuse of the arbitration system to injure the respondent with little risk of injury to itself and final arbitration awards for costs may not be able to be collected from an insolvent claimant. [*Rubins 373*]. However, RESPONDENT is not basing its request on any allegation of spurious claims by CLAIMANT.

**85.** Though CLAIMANT argues it must already advance a substantial amount of money for its half of the SIAC arbitration fees, [*see Memorandum for Claimant ¶ 71*], this does not replace the need for security for costs. The ability and willingness to pay advance arbitration fees does not necessarily guarantee the ability or willingness to pay costs at the end of the arbitration process.

The presence of separate rules in the SIAC for advance costs, [*SIAC Rule 27.1*], and security for costs, [*SIAC Rule 27.3*], suggests that payment of advance arbitration costs does not eliminate the need to order security for costs where appropriate.

**86.** CLAIMANT's assertions of good faith are not particularly relevant in this case. CLAIMANT's good faith has no bearing on its ability to pay or on Equatoriana's willingness to enforce an award of costs. Security for costs orders are designed not only to prevent claimants from misusing the arbitration system, but also to ensure that sincere but misguided claimants cannot avoid paying costs due to financial difficulties. In cases where security for costs is granted, tribunals focus not only on potential abuse of the arbitration process by the non-movant, but also on concerns about subsequent enforcement of awards. [*Werbicki 65; Rubins 364*].

*4. RESPONDENT's request for an order of security for costs is based on the reasonable concerns explained above, not in strategic or evasive tactics.*

**87.** RESPONDENT's goal in requesting security for costs is simply to assure that CLAIMANT can and will comply with any order for payment of costs the Tribunal may make in its final determination of this dispute. As explained above, security for costs is a widespread, accepted practice and is particularly warranted in this dispute. It is not, as CLAIMANT suggests, a tool to evade its claims. [*Memorandum for Claimant ¶ 82*].

**88.** CLAIMANT seems to base its allegation of bad faith on RESPONDENT's late payment of advance fees to the SIAC. [*See Memorandum for Claimant ¶ 85*]. The brief delay by RESPONDENT in paying its share of the advance fees has no bearing on a determination of good faith in these proceedings. The fees have in fact been paid, indicating that RESPONDENT has not been unwilling to pay. In any case, the matter of payment is a transaction between RESPONDENT and the arbitration institution, not between RESPONDENT and CLAIMANT, and is therefore not indicative of any lack of good faith toward CLAIMANT.

## **VI. THE TRIBUNAL SHOULD ORDER CLAIMANT TO REFRAIN FROM DIVULGING INFORMATION RELATED TO THE ARBITRATION.**

**89.** CLAIMANT has threatened to reveal information about this arbitration in the course of due diligence proceedings. [*Letter of Joseph Langweiler, 24 Sept. 2003*]. However, CLAIMANT is bound to a duty of confidentiality under the SIAC Rules (A.). The Tribunal has the authority to

rule on this matter (B.), and CLAIMANT’S refusal to follow such an order would warrant serious consequences (C.).

**A. Claimant is not entitled to derogate from its obligation of confidentiality.**

90. SIAC Rule 34.6 provides that both “the parties and the Tribunal shall at all times treat all matters relating to the proceedings (including the existence of the proceedings) and the award as confidential.” RESPONDENT respectfully submits that no exception to this rule, enumerated or reasonably implied, applies to CLAIMANT’S release of any information in this case.

*1. Exception (d) to SIAC Rule 34.6 does not release CLAIMANT from its duty of confidentiality in this arbitration.*

91. CLAIMANT argues that Rule 34.6(d) permits it to derogate from the general confidentiality requirement. [*Memorandum for Claimant ¶ 96*]. In fact, however, this exception simply does not apply, neither with regard to disclosing the existence of the arbitration, nor to any details related to the arbitration. Moreover, the fact that third parties may be bound to a duty of confidentiality does not justify divulging information to those third parties.

a) CLAIMANT has not established the requirements enumerated in SIAC Rule 34.6 (d).

92. SIAC Rule 34.6 (d) allows for an exception to the duty of confidentiality when a disclosure to a third party is “in compliance with the provisions of the laws of any State which is binding on the party making the disclosure.” CLAIMANT has failed to establish either of the two key requirements of Rule 34.6(d). First, disclosure in this case would not amount to *compliance* with the law of Equatoriana. Second, CLAIMANT has not established that it is *bound* by the laws of Equatoriana to disclose in this situation.

93. With regard to whether or not disclosure is necessary to comply with Equatoriana law, CLAIMANT has left several questions unanswered. The courts of Equatoriana consider each case individually in order to see if the matter to be disclosed would “materially affect” the financial status of the company to be purchased. [*Proc. Order 3, Clarification 38*]. To assume that the result of the arbitration will materially affect CLAIMANT’S financial status is presumptuous insofar as it assumes that the claim is valid. Even more importantly, CLAIMANT has failed to prove the extent to which its claim, if valid, would affect its financial status.

Because each case would be considered individually, it will also be difficult to determine how the courts of Equatoriana will rule in CLAIMANT'S case without more information about what they consider "material."

**94.** There is no indication that CLAIMANT'S situation is analogous to those cases where Equatoriana Courts apply a strict disclosure requirement. One likely difference is that CLAIMANT is seeking to disclose information that it is prohibited from disclosing by virtue of its own agreement to arbitrate under SIAC rules. The fact that this disclosure relates to an arbitration, which is internationally recognized as a private affair, coupled with the possibility that CLAIMANT agreed to a duty of confidentiality, could very well alter the Equatorianan Courts' analysis of the case.

**95.** In short, between the indeterminate questions concerning both compliance and the binding effect of Equatoriana Law, it is at the least uncertain whether or not the exception under SIAC Rule 34.6 (d) applies. In the case of *Esso v. Plowman*, the court cited uncertainty as to the effect of disclosure as one reason to deny disclosure, even as it held that there was no implied duty of confidentiality in the case before it. [*Esso v. Plowman (Australia) 37*]. Given such treatment of confidentiality by a court that did not particularly favor the concept, permitting disclosure by CLAIMANT would constitute a mistake.

**96.** Even if this type of case was of the type previously ruled on in Equatoriana, the notion that the ruling binds CLAIMANT is clearly flawed. CLAIMANT had the legal right to enter into the present arbitration agreement. Before it did so, it also had a legal right to sell its assets to a third party and make necessary disclosures in doing so. However, once CLAIMANT chose the former option, it gave up its right to sell itself along with its ability to comply to with all of the requirements of due diligence that accompany such a purchase. [*See Devolvé 380*]. It legally obligated itself to perform A, which prevented it from performing B. This is a common scenario in the world of contract, and it would undermine the freedom of contract to not allow this type of agreement; it would likewise undermine the sanctity of contract to allow the same agreement to be violated once it is allowed.

b) CLAIMANT is obligated to refrain from divulging all details of the arbitration.

**97.** The principle of confidentiality is a fundamental component of arbitration, even if it is subject to qualifications. [*Bond 273*]. However, the type of information to be disclosed is a pivotal factor in deciding whether an exception applies. [*Neill 288*]. The line of separation between different types of information to be disclosed is customarily drawn between the details of the arbitration (proceedings, documents, evidence, etc.) on one hand and the existence of the arbitration on the other. [*Devolvé 382; Neill 288*]. Greater sensitivity is applied to the details of the arbitration than to its existence. [*Neill 288*]. This distinction derives from the fact that the most dangerous material in an arbitration is usually found in the details—often involving highly sensitive financial data, trade secrets, and other matters that are perhaps necessary to settle a dispute, but which can also be volatile or potentially lethal in the wrong hands.

**98.** Thus, the strictest of care must be taken in deciding whether CLAIMANT is exempted from its duty of confidentiality in regard to any and all details of this arbitration. The exceptions listed under SIAC Rule 34.6 (d) should be strictly construed in light of all that is at stake and the precedential value afforded to the details of an arbitration by past decisions.

c) CLAIMANT is obligated to refrain from divulging the existence of the arbitration.

**99.** The prohibition against notifying a third party of the existence of this arbitration is expressly prohibited in the language of SIAC Rule 34.6 (d). Per its agreement to arbitrate any and all disputes arising out of the contract for the sale of goods under the SIAC Rules, CLAIMANT is obligated to follow the terms of its contract as expressed through the SIAC Rules.

**100.** CLAIMANT has had more than adequate opportunity to review the terms of the SIAC Rules, the set of rules that it originally incorporated into the contract. The fact that CLAIMANT agreed from the outset that SIAC Rules govern any possible arbitration firmly emphasizes the importance of taking the clauses within the SIAC rules to mean what they say. Without meeting any of the explicit exceptions provided for under Rule 34.6, CLAIMANT is specifically obligated to refrain from divulging the existence of the arbitration. [*Neill 290, 295*].

d) Requiring confidentiality of a third party does not improve the case for disclosure.

**101.** Equatoriana Investors would have a duty to CLAIMANT to not disclose any information divulged to them in the course of due diligence. [*Proc. Order 3, Clarification 39*]. CLAIMANT argues that this fact preserves the confidential nature of these proceedings. [*Memorandum for Claimant ¶ 99*]. This is not the case, however.

**102.** First, SIAC Rule 34.6 specifically prohibits disclosure to third parties without first meeting one of the enumerated exceptions to the duty. There is no exception allowing disclosure to others who are themselves under a duty of nondisclosure. As no exceptions to this duty have been met, CLAIMANT is under an obligation to refrain from divulging to any third party, including Equatoriana Investors.

**103.** Second, as CLAIMANT is not permitted to divulge information about this arbitration to a third party pursuant to its contractual agreement, neither is CLAIMANT permitted to do so in principle. While Equatoriana Investors would incur its own duty of confidentiality by accepting information concerning this arbitration in the course of due diligence, its only obligation would be to CLAIMANT. [*Id.*]. This raises questions of both liability and integrity. The Tribunal cannot expect RESPONDENT to gain comfort from a third party's obligation to confidentiality when that obligation not to disclose does not extend to RESPONDENT. Moreover, there would be a strong possibility that RESPONDENT would have no recourse against the third party if it were to wrongfully disclose information.

2. *Allowing CLAIMANT to disclose information would be neither legitimate nor reasonable.*

**104.** The legitimacy of protecting of a party's own interest in disclosure is determined by whether the disclosure is necessary. [*Neill 295*]. Necessity in this case is defined in accordance with legality. In other words, if the vindication of a party's rights could only be achieved by disclosure, then it (the disclosure) is deemed necessary. [*Insurance Co. v. Lloyd's Syndicate (U.K.)*].

**105.** Moreover, the term "necessity" cannot be used in the loose sense of the word. The mere fact that a disclosure would be helpful or persuasive in achieving the vindication of the claimed right could not justify breaching confidence. [*Neill 295*]. Disclosure must be the *only* means available to vindicating such a right.

**106.** The reasonableness of disclosing information is determined by several factors. One must consider the legitimacy of the disclosure, the motivation behind the disclosure, and the nature of confidentiality's relationship to the arbitration process itself before determining how reasonable it would be to disclose. Given these notions of legitimacy and reasonableness, RESPONDENT respectfully suggests that the Tribunal should recognize self-interest (and not the desire to act on a legal right) as a principle motivator behind CLAIMANT'S desire to disclose. Furthermore, disclosure would undermine the dignity of the arbitration process.

**107.** The companies, individuals, and governments who choose arbitration as a form of dispute resolution highly value confidentiality as a fundamental characterization of international commercial arbitration. [*Bond 273*]. In fact, it is not an overstatement to claim that a presumption of confidentiality attaches itself to the international commercial arbitration process. [*Devolvé 1; Fouchard/Gaillard/Goldman 153; Boyd 303*]. In Europe the prevailing view is that arbitral proceedings are subject to strict confidentiality. [*Gaillard 153; Boyd 270-272; Neill 288*]. As these observations show, parties have come to expect confidentiality in the international commercial arbitration process.

**108.** Even recent decisions that seem to have called confidentiality into question can be distinguished by both their facts and their place of origin. The majority opinion in *Esso v. Plowman* limits its rejection of an implied notion of confidentiality to Australia. [*Esso v. Plowman (Australia) 401*]. The decision in another Australian case, *Australia v. Cockatoo* does not have general bearing on other cases because a large part of its decision was based on the fact that the case involved the government and the government had a duty to act in the public interest. The present case does not involve the government acting in the public interest, and the arbitration certainly is not taking place in Australia. Confidentiality is fundamental to the principal of arbitration. [*Devolvé*]. To import the arguments used in either of the two Australian decisions to other jurisdictions would not only disturb accepted principles of arbitration, it would drive the arbitration process out of those jurisdictions entirely. [*Neill 316-317; Pryles 267*].

**B. The Tribunal has authority to rule on all matters of confidentiality.**

**109.** CLAIMANT asserts that the Tribunal does not have the requisite authority to order it to refrain from disclosure. [*Letter of Joseph Langweiler, 24 Sept. 2003*]. This stance is in direct contravention of the parties' agreement. Paragraph 15 of the contract incorporates the SIAC

Rules to govern any disputes arising out of or in connection with the contract. *[Notice of Arbitration ¶ 5]*. SIAC Rule 25(j) affords the Tribunal power to issue orders, interim injunctions, or other measures. Not only does the Tribunal have authority to rule on matters for which it has jurisdiction under the “Competence-Competence” principle, *[Gotwald 66-67; Berger 6, 29]*, but SIAC Rule 26 gives the Tribunal’s power to exercise powers defined elsewhere in the rules, and to determine any issue of law arising in the course of the arbitration. *[SIAC Rules 26.1, 26.3]*.

**110.** SIAC Rule 34.6 extends a duty of confidentiality to “all matters relating to the proceeding (including the existence of the proceedings) and the award.” By virtue of their inclusion in the SIAC rules, matters discussed in Rule 34 fall under the jurisdiction of the Tribunal. *[SIAC Rule 26.1]*. Thus the Tribunal clearly has authority to rule on matters of confidentiality.

**111.** CLAIMANT argues that only the relevant court in Danubia can decide this issue. *[Letter of Joseph Langweiler, 24 Sept. 2003]*. However, this argument is flawed for at least two reasons. First, CLAIMANT contracted to arbitrate under the SIAC Rules, a set of rules which gives the Tribunal to jurisdiction to decide this issue. *[SIAC Rule 26.1]*. Second, because of the contractual nature of the duty, a relevant court would enforce both the clause and the jurisdiction of the Tribunal insofar as it is enumerated in the SIAC Rules.

### **C. Unauthorized disclosure would warrant consequences for Claimant.**

**112.** CLAIMANT would be liable for breach of contract if it were to violate the Tribunal’s order not to divulge information to Equatoriana Investors. *[Brown 1015]*. Considering that a breach of contract is a matter of law, the Tribunal would have jurisdiction to rule on the matter and issue damages and/or an injunction against further disclosures. *[SIAC Rule 26.3; Brown 1016]*. The damages in such a case would correspond to the amount which could be proven to have been caused by CLAIMANT’S breach of confidentiality.

**113.** There is also the possibility that a court of law could issue damages in the form of contract damages, penalties, or even the invalidation of the arbitration agreement, as the Stockholm City Court did in one recent case. *[Trade Finance v. Bulgarian Foreign Trade Bank (Sweden); see also Nakamura 25]*. Thus, if CLAIMANT decided to breach its duty after the final award had been issued by the Tribunal, it would still find itself responsible for paying damages, paying a penalty fee, or losing the amount of any award it received. *[Aita v. Ojeh (France)]*;

*Paulsson/Rawding 312]*. Some of these measures may seem harsh; however, the duty of confidentiality would be meaningless if CLAIMANT could violate it without consequence. *[Brown 1017]*.

## **CONCLUSION**

**114.** Based on the foregoing arguments, RESPONDENT respectfully requests that the Tribunal find that the Model 14 machines delivered by RESPONDENT fully conformed to the contract. If the Tribunal nonetheless finds a breach of contract to have occurred, RESPONDENT recommends that the Tribunal find that such breach was not fundamental, and that CLAIMANT did not make a valid avoidance of the contract.

**115.** RESPONDENT also requests that the Tribunal order CLAIMANT to post security for RESPONDENT's arbitration costs and order CLAIMANT to refrain from disclosing the existence or the details of the arbitration.