TWELFTH ANNUAL WILLEM C. VIS

INTERNATIONAL COMMERCIAL ARBITRATION MOOT

MEMORANDUM
for
RESPONDENT

On Behalf of:	*Against:*
Equatoriana Commodity Exporters, S.A. 325 Commodities Avenue, Port City, Equatoriana.	Mediterraneo Confectionary Associates, Inc. 121 Sweet Street, Capitol City, Mediterraneo.
RESPONDENT	**CLAIMANT**

NATIONAL UNIVERSITY *of* SINGAPORE

COUNSEL

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FADZLI HUSSEN *GITTA SATRYANI JUWITA* *CHAN LAI HING*

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A. The storm and EGCMO embargo on export of cocoa from Equatoriana were impediments beyond the Respondent's control that caused the delay in delivery of the 300 tons of cocoa. 3

B. The Respondent could not reasonably be expected to have taken the storm and EGCMO embargo on the export of cocoa into account at the time of conclusion of the Cocoa Contract. 4

C. The Respondent could not reasonably have avoided or overcome these impediments and their consequences because the Claimant contracted for Equatoriana cocoa under the Cocoa Contract. 5

1. The Claimant and the Respondent intended to contract for Equatoriana cocoa under the Cocoa Contract. 5

2. The Respondent could not reasonably have avoided or overcome the effects of the impediments because there was no other available source of Equatoriana cocoa. 7

D. The Respondent gave notice of the storm and EGCMO embargo to the Claimant within a reasonable time. 7

II. FURTHER AND IN THE ALTERNATIVE, THE COVER PURCHASE IS UNJUSTIFIED AS THE CLAIMANT IS NOT ENTITLED TO AVOID THE CONTRACT FOR THE DELAY IN DELIVERY OF THE 300 TONS OF COCOA. 8

A. Avoidance is a condition precedent for the conclusion of a substitute transaction under Art. 75 CISG 9

B. The Claimant is not entitled to avoid the contract as it failed to fix an additional period of time for the Respondent to perform the contract. 9

C. There was no fundamental breach committed by the Respondent to justify avoidance. 11

1. The Claimant did not suffer any substantial detriment within the meaning of Art. 25 CISG. 11

a. Timely performance was not an essential expectation under the contract. *11*

b. The Claimant did not suffer consequences of sufficient gravity to constitute substantial deprivation under the Cocoa Contract. *12*

2. Even if the Claimant suffered substantial detriment, it was not and could not have been foreseeable by the Respondent or a reasonable person in its position. 13

a. Foreseeability is determined at the time of conclusion of the contract. 13

b. The detriment was not foreseeable to the Respondent at the time of the conclusion of the Cocoa Contract. 14

c. A reasonable person of the same kind as the Respondent would not have foreseen the detriment. 14

D. In any event, there was no valid declaration of avoidance prior to the conclusion of the cover purchase. 14

III. CONSEQUENTLY, EVEN IF THE RESPONDENT CANNOT RELY ON ART. 79 CISG, THE CLAIMANT IS STILL NOT ENTITLED TO CLAIM ANY DAMAGES. 16

A. The Claimant is not entitled to claim USD 289,353 for the difference in price between the cover purchase and the Cocoa Contract because it has not fulfilled the requirements of Art. 75 CISG. 16

1. The Claimant is not entitled to USD 289,353 because it was not entitled to make the cover purchase before the contract was avoided. 16

2. Alternatively, the Claimant is not entitled to claim USD 289,353 because the cover purchase was not concluded reasonably. 17

B. Furthermore, the Claimant is not entitled to claim for its loss of profit as this loss was not foreseeable at the time of the conclusion of the contract within the meaning of Art. 74 CISG. 18

C. Alternatively, even if the Claimant is entitled to claim damages for the cover purchase, it is only entitled to USD 179,026. 18

1. The Claimant's damages should be reduced to USD 179,026 because it failed to mitigate its losses under Art. 77 CISG. 18

2. The sum of USD 179,026 would be the sum derived by applying Art. 76 CISG. . 19

IV. THE TRIBUNAL HAS JURISDICTION UNDER ART. 21(5) SWISS RULES TO HEAR THE CROSS-CLAIM UNDER THE SUGAR CONTRACT. 19

A. The parties have consented to the application of all the provisions of the Swiss Rules, including Art. 21(5), by its agreement to apply the Geneva Rules. 20

1. The parties did not expressly opt out of the Swiss Rules which have automatically replaced the Geneva Rules after 1 January 2004. 20

2. The Claimant has waived its right to object to Art. 21(5) Swiss Rules. 21

3. The parties intended to apply the most up-to-date arbitration rules available at the Chamber of Commerce and Industry of Geneva, which were the Swiss Rules. ... 22

B. In any event, the Swiss Rules were the prevailing rules at the time of commencement of arbitration and Art. 21(5) is a reasonable provision which is consistent with the *lex arbitri*. 23

1. The Swiss Rules were the applicable rules at the time of submission to arbitration on 5 July 2004. 23
2. The parties cannot exclude the application of Art. 21(5) Swiss Rules because it is not an unjustified and unexpected provision. 24
3. Art. 21(5) Swiss Rules is consistent with the UNCITRAL Model Law and is applicable to the present case...25

C. The Tribunal has jurisdiction to hear the cross-claim relating to the Sugar Contract because the claim falls within the scope of Art. 21(5) Swiss Rules........26

1. Art. 21(5) Swiss Rules extends the Tribunal's jurisdiction to hear the cross-claim under the Sugar Contract even though the dispute does not fall within the scope of the arbitration clause in the Cocoa Contract. 26
2. The present dispute relating to the Sugar Contract is a set-off defence within the meaning of Art. 21(5) Swiss Rules. 27
3. In any event, there is negligible difference between a set-off defence and a counterclaim in this case as Art. 21(5) Swiss Rules can be interpreted to cover both. 27

D. The Chamber of Commerce and Industry of Geneva is the appropriate forum to hear the cross-claim arising under the Sugar Contract. 28

V. EVEN IF ART. 21(5) SWISS RULES DOES NOT APPLY IN THE PRESENT CASE, THE TRIBUNAL STILL HAS JURISDICTION TO HEAR THE CROSS-CLAIM RELATING TO THE SUGAR CONTRACT AS A SET-OFF DEFENCE. 29

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B. The cross-claim under the Sugar Contract satisfies the requirements of a set-off defence...30

1. There is mutuality of claims in this case..31
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3. The main claim and the cross-claim are mature claims. 31
4. The main claim and the cross-claim are liquidated. 32
5. The set-off defence in this case is not excluded by contract and does not prejudice the Claimant's interest. 32

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B. In any case, the Respondent is still entitled to set-off the amount up to USD 289,353 that is initially claimed by the Claimant under the Cocoa Contract. 34

VIII. PRAYER FOR RELIEF...35

TERMS & ABBREVIATIONS

AG	Amtsgericht (Petty District Court, Germany)
AP	Audiencia Provincial (Appellate Court, Spain)
Am. Rev. Int’l Arb.	American Review of International Arbitration
Arb. Int’l	Arbitration International
Arb. Law Monthly	Arbitration Law Monthly
ASA	Swiss Arbitration Association
Aust. Bus. L. R.	Australian Business Law Review
BGH	Bundesgerichtshof (Federal Supreme Court, Germany)
BTPP	Bulgarska turgosko-promishlena palata (Bulgarian Chamber of Commerce and Industry)
CCRF	Constitutional Court of the Russian Federation
CIETAC	China International Economic and Trade Arbitration Commission
CISG	United Nations Convention on Contracts for the International Sale of Goods of 11 April 1980
Co.	Company
Ed.	Editor(s)
ed.	Edition(s)
EGCMO	Equatoriana Government Cocoa Marketing Organization
fn.	Footnote
Int’l A.L.R.	International Arbitration Law Review
Ipso facto	By the fact itself
ICC	International Chamber of Commerce
HG	Handelsgericht (Commercial Court, Switzerland)
Ltd.	Limited
LG	Landgericht (District Court, Germany)

J. Char. Inst. Arb.	Journal of the Chartered Institute of Arbitrators
J. Int’l Arb.	Journal of International Arbitration
J. Small & Emerging Bus. L.	Journal of Small & Emerging Business Law
Memo.	Memorandum
No.	Number
NW. J. Int’l L. & Bus.	Northwestern Journal of International Law & Business
OGH	Oberster Gerichtshof (Austria)
OLG	Oberlandesgericht (Provincial Court of Appeal, Germany)
p.	Page
pp.	Pages
RFCCI	Russian Federation Chamber of Commerce and Industry
Problem	Twelfth Annual Willem C. Vis International Commercial Arbitration Moot Problem
TA	Tribunale d’ appello (Appellate Court)
Temp. Int'l. & Comp. L. J.	Temple International and Comparative Law Journal
UNCITRAL	United Nations Commission on International Trade Law
U.K.	United Kingdom
U.S.	United States of America
v.	Versus
World Arb. & Mediation Rep.	World Arbitration & Mediation Report

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STATEMENT OF FACTS

Mediterraneo Confectionary Associates, Inc. (hereinafter the "Claimant") is a company incorporated in Mediterraneo and is a manufacturer of confectionary items. Equatoriana Commodity Exporters, S.A. (hereinafter the "Respondent") is a company incorporated in Equatoriana and largely trades commodities produced in Equatoriana. The Respondent only trades cocoa of Equatoriana origin and the parties have had prior business dealings over the years in which the Respondent has supplied the Claimant only with Equatoriana cocoa.

On 19 November 2001, the Claimant entered into the Cocoa Contract 1045 (hereinafter the "Cocoa Contract") with the Respondent to purchase 400 metric tons of cocoa beans at the price of USD 1,240.74 per metric ton. Under the Cocoa Contract, delivery was to take place between March to May 2002 with the Respondent electing a delivery date sometime between January to February 2002.

However, on 14 February 2002, a storm hit the cocoa producing areas in Equatoriana and caused extensive damage to the cocoa trees in Equatoriana. The storm was the first in 22 years that caused damage to the cocoa trees in Equatoriana and was widely reported in the cocoa industry. Consequently on 22 February 2002, the Equatoriana Government Cocoa Marketing Organization (hereinafter the "EGCMO") imposed an embargo on the export of all cocoa from Equatoriana. On 20 March 2002, the embargo was extended indefinitely and would only be lifted pending further notice by the EGCMO.

The Respondent informed the Claimant of its inability to fix a delivery date as required under the Cocoa Contract due to the storm and the embargo in Equatoriana on 24 February 2002. The Claimant informed the Respondent that it was not under immediate pressure to receive the cocoa and the cocoa could be delivered later in the year. In early May 2002, the EGCMO allowed the release of a small amount of cocoa to the Respondent, 100 tons of which were shipped immediately to the Claimant.

Between October and November 2002, there were widely reported rumours that the EGCMO was planning to release additional cocoa. However, on 24 October 2002, the Claimant had made a cover purchase of 300 tons of cocoa from Oceania Produce Ltd. at the then current market price of USD 2,205.26 per metric ton without giving prior notice to the Respondent of the cover purchase. At the time the cover purchase was made, the Claimant and the Respondent were still in a contractual relationship.

Finally on 12 November 2002, the EGMCO lifted the embargo. Immediately on 13 November 2002, the Respondent informed the Claimant that it would deliver the remaining 300 tons of cocoa to the Claimant within the next several weeks. However, on 15 November 2002, the Claimant issued a letter to the Respondent to terminate the contract and also to make a claim of USD 289,353, which was the difference between the price under the contract and the cover purchase. The Respondent maintains that it is not responsible for the Claimant's purported loss. After a year and a half of negotiation to attempt to reach a settlement, the dispute was finally submitted to arbitration at the Chamber of Commerce and Industry of Geneva (hereinafter the "CCIG") on 5 July 2004.

Pursuant to Art. 21(5) Swiss Rules, the Respondent raised a cross-claim under the Sugar Contract 2212 (hereinafter the "Sugar Contract") as a set-off defence to the main claim under the Cocoa Contract. The Sugar Contract was concluded on 23 November 2003 for the sale of 2,500 metric tons of sugar to the Claimant. However, the Claimant refused to pay the contract price after the sugar had been delivered to it as it claimed that the sugar was wet and contaminated. The Respondent claims USD 385,805 under the Sugar Contract.

In accordance with the Tribunal's Procedural Order No. 1, Counsel for the Respondent argues that:

1) The Respondent is excused from liability for damages because the EGCMO embargo constituted a valid excuse under Art. 79 CISG [Respondent Memo. at paras.1-22];
2) The Claimant's cover purchase is not justified because the Claimant is not entitled to avoid the Cocoa Contract [Respondent Memo. at paras.23-52];
3) Even if the Respondent cannot rely on Art. 79 CISG, the Claimant is still not entitled to claim damages for the sum of USD 289,353 under Arts. 74–77 CISG [Respondent Memo. paras.53-68];
4) The Tribunal has jurisdiction to hear the cross-claim arising under the Sugar Contract [Respondent Memo. at paras.69-128];
5) The Respondent is entitled to claim the damages owed to it under the Sugar Contract [Respondent Memo. paras.129-133].

I. THE RESPONDENT IS NOT LIABLE TO PAY DAMAGES TO THE CLAIMANT BECAUSE THE EMBARGO CONSTITUTED A VALID EXCUSE UNDER ART 79 CISG.

1. The Respondent is exempted from liability to pay damages under Art. 79(5) CISG because of the storm in Equatoriana and the EGCMO embargo on the export of cocoa. Under Art. 79(1) CISG, a party is not liable for damages for the failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control, and that he could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract, or to have avoided or overcome it or its consequences, subject to the requirement of notice under Art. 79(4) CISG.

2. Contrary to the Claimant's assertion [Claimant Memo. at para.3], the Respondent has fulfilled all the requirements of Art. 79 CISG. In the present case, the Respondent's non-delivery during the period of March to November 2002 was due to the damage caused to the cocoa trees by the storm in Equatoriana and the subsequent EGCMO embargo on export of cocoa from Equatoriana, which constituted impediments beyond the Respondent's control [A]. The Respondent could not reasonably have taken the impediment into account at the time of the conclusion of the contract [B] and it could not reasonably have avoided or overcome the storm, embargo and their consequences [C]. The Respondent has also given notice of the impediments to the Claimant within a reasonable time [D].

A. The storm and EGCMO embargo on export of cocoa from Equatoriana were impediments beyond the Respondent's control that caused the delay in delivery of the 300 tons of cocoa.

3. The exemption from liability to pay damages for a party's failure to perform is determined in accordance with Art. 79 CISG [Secretariat Commentary, Art. 79 at para.2; Honnold at p.472]. According to Art. 79(1) CISG, the failure to perform must be due to an impediment [Schlechtriem at p.603; Southerington at 3; Bianca/Bonell at p.283; HG St. Gallen, 3 December 2002 (Switzerland); FAC Moscow, 4 February 2002 (Russia)]. An impediment has been defined as an objective event, exterior to the party which affects the party's ability to perform [Schlechtriem at p.608; Keil at p.105; Ziegler at p.79].

4. In the present case, the Respondent's non-delivery was caused by the storm in Equatoriana on 14 February 2002 which resulted in the EGCMO embargo on the export of cocoa from Equatoriana on 22 February 2002 [Problem at p.27]. The storm and EGCMO embargo were impediments because they were objective and external circumstances that

prevented the Respondent's performance [Schlechtriem at p.608; Galston/Smit/Nicholas at p.5–14]. In fact, embargoes, also known as export bans imposed by government authorities of a country, have been widely acknowledged as one of the "classical" or most common cases of impediments [Kritzer at p.506; Heilmann at p.630; BTPP, 24 April 1996 (Bulgaria); BTPP, 12 February 1998 (Bulgaria); Czarnikow v. Centrala (U.K.)]. Thus, the Respondent's situation in the present case falls within the definition of the word "impediment" contemplated by Art. 79(1) CISG.

5. Impediments within the ambit of Art. 79 CISG must also be events beyond the party's (the Respondent's) control [Honnold at p.480; Bund at p.385; Marek at p.2015; CCRF, 27 April 2001 (Russia); TA Lugano, 29 October 2003 (Switzerland)]. The Respondent's sphere of control only includes normal business risks attributed to sellers of goods in international trade, such as an increase in prices [Enderlein/Maskow at p.322; Kranz at p.197; Gritli at p.90]. However, it would place an overly heavy burden on the Respondent to bear the risk of natural catastrophes and governmental measures affecting its domestic markets [OLG Hamburg, 4 July 1997 (Germany); Kranz at p.198] and these impediments have been held to be beyond the control of the party claiming exemption [UNCITRAL CISG Digest, Art. 79 at para.14; BTPP, 24 April 1996 (Bulgaria)]. In the present case, the storm in Equatoriana falls within the definition of natural catastrophe and the resulting EGCMO embargo is indeed a form of governmental measure [Flambouras at p.266]. These impediments were not within the sphere of risks typically attributable to sellers and were beyond the Respondent's control.

B. The Respondent could not reasonably be expected to have taken the storm and EGCMO embargo on the export of cocoa into account at the time of conclusion of the Cocoa Contract.

6. Whether the party claiming exemption could reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract is a crucial element of Art. 79(1) CISG [Galston/Smit/Nicholas at p.5–9; Lookofsky at p.133; Jenkins at p.2022]. In determining whether the possibility of a particular impediment is envisaged at the time of conclusion of the contract, the explicit or implicit terms of the contract are examined and determined on a case by case basis [Kritzer at p.506; Secretariat Commentary, Art. 79, at para.6; Liu at 20.3.3.2; Weitzman at p.276].

7. The Cocoa Contract, concluded on 23 November 2001 [Problem at p.8], did not take into account or provide for the possibility of a storm or embargo. Moreover, the storm and its consequences were unforeseeable events as the storm was the first in 22 years to cause such

extensive damage that left EGMCO no choice but to impose a strict embargo [Procedural Order No. 2 at para.8]. Hence, the Respondent could not reasonably have taken the storm and EGCMO embargo into account at the time of the conclusion of the contract.

C. The Respondent could not reasonably have avoided or overcome these impediments and their consequences because the Claimant contracted for Equatoriana cocoa under the Cocoa Contract.

8. Art. 79(1) CISG also requires the Respondent to prove that it could not reasonably have avoided or overcome the consequences of the impediments. The Respondent fulfils this requirement because the parties intended to contract for Equatoriana cocoa under the Cocoa Contract [1] and the Respondent could not reasonably have avoided or overcome the consequences of the impediments because there was no other available source of Equatoriana cocoa [2].

1. <u>The Claimant and the Respondent intended to contract for Equatoriana cocoa under the Cocoa Contract.</u>

9. Even though the Cocoa Contract did not provide expressly for Equatoriana cocoa, the contract is interpreted in accordance with the parties' intentions under Art. 8(1) CISG. In the present case, the Claimant knew or could not have been unaware that the Respondent intended to contract for cocoa of Equatoriana origin.

10. The subjective intent of the contracting parties is a matter of interpretation that is governed by Art. 8 CISG [Karollus at p.68; LG Hamburg, 26 September 1990 (Germany)]. Art. 8 CISG can be used to interpret the contract even when the contract is embodied in a single document, like the Cocoa Contract in this case [Honnold at p.116; Secretariat Commentary, Art. 8 at para.2]. Art. 8(1) CISG allows contracts to be interpreted according to one party's intention when the other party knew or could not have been unaware what that intent was [Kritzer at p.122; Eörsi/Galton/Smit at p.9]. Art. 8(3) CISG states that this intention can be determined with regards to all relevant circumstances of the case including any practices which the parties have established between themselves [Secretariat Commentary, Art. 8, at para.6]. The parties' practices can be determined implicitly [Réczei at p.182; ICC Case No. 8817 of 1997] through their prior course of dealings in accordance with Art. 9(1) CISG [Schlechtriem at p.70; §1-205 UCC; Filanto v. Chilewich (U.S.); #QFD890011, CIETAC, 1990 (China); OGH, 21 March 2000 (Austria)].

11. In the present case, the Respondent's statement can be interpreted according to its intention of providing the Claimant exclusively with Equatoriana cocoa. The Claimant knew

or could not have been unaware of the Respondent's intention to contract only for Equatoriana cocoa due to the practices which the parties have established between themselves [Art. 8(1) CISG]. Notwithstanding that the source of cocoa to be delivered under the Cocoa Contract was not expressly specified [Problem at p.8], the Claimant and the Respondent have done business together on a number of occasions [Problem at p.2] and these prior practices are relevant in determining their intentions on the source of cocoa for the Cocoa Contract [Carlsen at p.10].

12. The Claimant must have known that the Respondent intended to supply cocoa of Equatoriana origin since the Claimant knew that it had always been supplied with Equatoriana cocoa under previous contracts [Procedural Order No. 2 at para.19]. Furthermore, the Respondent's business deals primarily with the exportation of commodities from Equatoriana [Problem at p.26] and the Respondent has never traded cocoa beans from any country other than Equatoriana [Procedural Order No. 2 at para.16]. Thus, under Art. 8(1) CISG, the Claimant knew or could not have been unaware of the Respondent's intention to deliver only Equatoriana cocoa because this was implicitly established through the parties' prior practices.

13. Since it has been established under Art. 8(1) CISG that the Claimant knew or could not have been unaware of the Respondent's intention to deliver Equatoriana cocoa, it is unnecessary to consider the objective intentions of the parties under Art. 8(2) CISG as alleged by the Claimant [Claimant Memo. at paras.13-38]. Art. 8(2) CISG only applies when Art. 8(1) is not applicable [Schlechtriem at p.71].

14. Nonetheless, even if the Tribunal finds that the Respondent cannot rely on Art. 8(1) CISG, a reasonable person of the same kind as the Claimant would have known that the Respondent only intended to supply Equatoriana cocoa under the Cocoa Contract. Applying Art. 8(2) CISG, a reasonable person would have known that the Cocoa Contract was for the sale of Equatoriana cocoa since the Respondent has only traded in cocoa beans from Equatoriana and the Claimant had always been supplied with Equatoriana cocoa [Procedural Order No. 2 at paras.14, 19].

15. In light of the foregoing reasons, under both Arts. 8(1) and (2) CISG, the Cocoa Contract has to be interpreted as a contract exclusively for Equatoriana cocoa.

2. <u>The Respondent could not reasonably have avoided or overcome the effects of the impediments because there was no other available source of Equatoriana cocoa.</u>

16. Pursuant to Art. 79(1) CISG, the Respondent is only required to do what a reasonable person would do to overcome the consequences of the impediment [Schlechtriem at p.612; Rimke at p.206; Krüger at p.263]. In the present case, the EGCMO has a monopoly over the export of Equatoriana cocoa and is the only source from which the Respondent could have obtained Equatoriana cocoa [Procedural Order No. 2 at para.11]. Since the Respondent's obligation under the Cocoa Contract was limited to the delivery of Equatoriana cocoa and the EGCMO imposed an embargo on the export of all Equatoriana cocoa, there was no way for the Respondent to acquire Equatoriana cocoa to deliver to the Claimant [Procedural Order No. 2 at para.12].

17. Although the Respondent did not ask for an exemption from the EGCMO embargo, it has not violated any duty to make all reasonable efforts to overcome the impediment [Claimant Memo. at para.48]. It was not unreasonable on the Respondent's part not to ask for an exemption because the EGCMO embargo was compulsory [Roxford v. Moore (U.S.); Claimant Memo. at para.48] and no exemptions were given by the EGCMO [Procedural Order No. 2 at para.12], except for the 100 tons received by the Respondent on 7 May 2002 which was promptly delivered to the Claimant on 18 May 2002 [Problem at p.3]. Thus, the Respondent could not reasonably have overcome the consequences of the impediments.

D. The Respondent gave notice of the storm and EGCMO embargo to the Claimant within a reasonable time.

18. Art. 79(4) CISG imposes a duty on the party who fails to perform (the Respondent), to give notice to the other party (the Claimant) of the impediment and the effect on its ability to perform [Kritzer at p.509; Dubrovnik Lectures at p.256]. In addition, Art. 79(4) CISG requires that the notice of the impediment be given within a reasonable time after the party who fails to perform becomes aware of the impediment [Schlechtriem at p.624].

19. The letter on 24 February 2002 complied with Art. 79(4) CISG because the Respondent notified the Claimant of the storm and EGCMO embargo and also informed the Claimant that it would be unable to deliver the cocoa only for the period of the EGCMO embargo [Problem at p.9]. Subsequent letters were also sent to notify the Claimant that the Respondent would deliver the remaining 300 tons of cocoa once the EGCMO embargo was lifted [Problem at pp.12, 16].

20. These letters were not guarantees as alleged by the Claimant [Claimant Memo. at paras.49-52]. They were merely letters notifying the Claimant that the Respondent intended to comply with its contractual obligations once the impediments ceased to exist [Problem at pp.12, 16].

21. In addition, the notice was given by the Respondent to the Claimant within a reasonable time. The first letter of 24 February 2002 was given on the second day of the EGMCO embargo on 22 February 2002 [Procedural Order No. 2 at para.10], 10 days after the Respondent became aware of the storm on 14 February 2002.

22. Accordingly, the Respondent is exempted from liability for damages under Art. 79(5) CISG [Nicholas, Force Majeure at p.235; HG Zürich, 10 February 1999 (Switzerland); RFCCI, 22 January 1997 (Russia); Schlechtriem, Uniform Sales Law in Germany at p.26] because the storm and EGCMO embargo qualified as impediments within the meaning of Art. 79(1) CISG and the Respondent has complied with the notice requirement in Art. 79(4) CISG [AG Charlottenburg, 4 May 1994 (Germany)].

II. FURTHER AND IN THE ALTERNATIVE, THE COVER PURCHASE IS UNJUSTIFIED AS THE CLAIMANT IS NOT ENTITLED TO AVOID THE CONTRACT FOR THE DELAY IN DELIVERY OF THE 300 TONS OF COCOA.

23. The Respondent acknowledges that Art. 79(5) CISG only precludes the Claimant from claiming damages and preserves its right to exercise other remedies, if any. Nevertheless, the Claimant's exercise of its purported right to make a substitute transaction [Problem at p.4] remains unjustified because avoidance is a condition precedent to the conclusion of a substitute transaction which the Claimant is not entitled to in this case [A]. Avoidance in the present situation is governed by Art. 49 CISG, which applies to both installment and entire contracts. The Claimant has not fulfilled either limbs of Art. 49(1) CISG to entitle it to avoid the contract. It failed to fix an additional period of time for the Respondent to perform as required under Art. 49(1)(b) CISG [B]. Furthermore, the late delivery does not amount to fundamental breach under Art. 49(1)(a) CISG read with Art. 25 CISG [C]. Even if the Tribunal finds that Claimant is entitled to avoid the contract, the Claimant has failed to make a valid declaration of avoidance [D], and consequently remained precluded from concluding a substitute transaction.

A. Avoidance is a condition precedent for the conclusion of a substitute transaction under Art. 75 CISG.

24. "Under Art. 75 CISG, a substitute transaction can only be made after the contract of sale has been avoided… even a substantial breach of contract by one party does not give the other party a right to free himself from the contract unless he has avoided the contract by giving notice to the other party in breach" [Schlechtriem at p.575]. As such, the Claimant's substitute purchase was unjustified as the right to avoid the contract did not arise under both Arts. 49(1)(b) [Respondent Memo. paras.27-30] and 49(1)(a) CISG [Respondent Memo. paras.31-45].

25. However, the Claimant argues that the purported substitute transaction can take place before avoidance because it has been exceptionally held that the aggrieved party can make the cover purchase before avoiding the contract when it is clear that the other party is unable to perform the contract [Claimant Memo. at para.74; OLG Hamburg, 28 February 1997 (Germany); Schlechtriem at p.575].

26. Nevertheless, the Respondent submits that the factual matrix of that case [OLG Hamburg, 28 February 1997 (Germany)] can be distinguished because the seller in that case was given a fixed period of additional time for performance and it never delivered the goods due under the contract. In the present case, the Respondent has performed part of its obligations under the contract by shipping 100 tons of cocoa on 18 May 2002 [Problem at p.12], and it was ready to perform its obligations once the EGCMO export ban was lifted [Problem at pp.12, 16]. Moreover, the Claimant did not give the Respondent an additional period of time for performance under the Cocoa Contract [Respondent Memo. at paras.26-30]. Thus, this exception does not apply to the Claimant, and it was required to avoid the contract before it could conclude its purported substitute transaction.

B. The Claimant is not entitled to avoid the contract as it failed to fix an additional period of time for the Respondent to perform the contract.

27. In order to rely on Art. 49(1)(b) CISG to avoid the unperformed part of the Cocoa Contract, the Claimant is required to fulfil the preconditions of Art. 47(1) CISG and fix an additional period of time for performance [Honnold at p.313; RFCCI, 5 March 1998 (Russia)] which is reasonable [Liu at 4.3.2.1]. The Claimant is not entitled to avoidance under this provision because it failed to fix a specific additional period of time for performance.

28. If the Claimant elects to exercise the remedy of avoidance under Art. 49(1)(b) CISG

read with Art. 47(1) CISG, the Claimant must fix a certain date or time period for delivery and make it clear that the Respondent has to perform within that time [1980 Conference Records at p.39, paras.6-7; Liu at 4.3.2.1; Kazmierska at p.112]. This notice of additional time under Art. 47(1) CISG must be unequivocal and clearly expressed in that no reasonable seller would need any further clarification to recognise that the date indicated is the final opportunity to deliver under the contract [Bianca/Bonell at p.345; Gärtner at 2B1].

29. The Claimant alleges that a period was fixed from 15 August 2002 that "covered weeks" [Claimant Memo. at para.61], and a further period was fixed from 29 September 2002 that was "in no event later than a week" [Claimant Memo. at paras.65, 67]. However, a definite period was not fixed in the letter dated 15 August 2002 since the Claimant only said that the Cocoa Contract was to be performed "soon" [Problem at p.13]. Neither was a definite period of time fixed in the telephone call made on 29 September 2002 because it merely reiterated the Claimant's concerns in the aforementioned letter [Procedural Order No. 2 at para.22]. This type of general demand that *expresses the hope to receive the goods soon* does not suffice because it does not fix an additional time for performance [Bianca/Bonell at p.345; Fagan at p.342; OLG Düsseldorf, 24 April 1997 (Germany)]. The Respondent, or any reasonable seller would require further clarification as to the definite time of performance required by the Claimant in receiving such information. It is clear that the letter and conversation only constituted general demands or reminders requiring prompt delivery without fixing a deadline for performance.

30. Even if the Tribunal finds that the Claimant did fix an additional period of time, either from 15 August 2002 [Claimant Memo. at para.61], or alternatively from 29 September 2002, as alleged by the Claimant [Claimant Memo. at paras.65, 67], the Respondent submits that this additional period of time was not reasonable. The reasonableness of an additional period of time fixed depends on the circumstances of the contract such as the nature of the delay and the seller's possibility of delivery [Bianca/Bonell at p.345; Schlechtriem at p.396]. Given the uncertain situation in Equatoriana, and the Respondent's willingness to perform [Problem at pp.9, 12], the period given by the Claimant was unreasonably short [OLG Celle, 24 May 1995 (Germany)]. Therefore, a reasonable period for delivery, which should have lasted at least until the middle of November 2002 when the EGCMO was lifted, is applicable [Procedural Order No. 2 at para.10; LG Ellwangen, 21 August 1995 (Germany); OLG Naumburg, 27 April 1999 (Germany)].

C. There was no fundamental breach committed by the Respondent to justify avoidance.

31. Art. 49(1)(a) CISG allows the Claimant to avoid the contract if the Respondent has committed a fundamental breach as defined under Art. 25 CISG. A breach is 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" [Art. 25 CISG]. The Claimant has argued that it is entitled to avoid the Cocoa Contract because the Respondent's failure to deliver 300 tons of cocoa constituted a fundamental breach of the contract [Claimant Memo. at paras.56-60]. However the Claimant is not entitled to avoid the contract for fundamental breach since the Claimant did not suffer substantial detriment within the meaning of Art. 25 CISG [1]. Even if the Claimant suffered a substantial detriment, it was not and could not have been foreseeable by the Respondent or a reasonable person in its position [2].

1. The Claimant did not suffer any substantial detriment within the meaning of Art. 25 CISG.

32. Art. 25 CISG requires the Claimant to show that it suffered a detriment that substantially deprived it of what it was entitled to expect under the contract [Kritzer at p.205, Schlechtriem p.181; Bianca/Bonell at p.216; Gärtner at B1]. The Claimant has asserted that it suffered substantial detriment because time is of essence to the contract and it suffered serious consequences arising from the delay in delivery [Claimant Memo. at para.58-59].

33. Contrary to the Claimant's assertions, it will be shown that timely performance is not an essential expectation under the contract [a] and the Claimant did not suffer consequences of sufficient gravity to constitute substantial deprivation under the contract [b].

a. Timely performance was not an essential expectation under the contract.

34. Expectation interest of the parties is ascertained objectively through the obligations and their importance as determined by the contract [Bianca/Bonell at p.209; Liu at 8.2.1]. The absence of any stipulation denoting the importance of time in the contract leads to the conclusion that time for delivery was flexible and was not critical [Enderlein/Maskow at p.114]. In the present case, there was no indication in the Cocoa Contract that delivery of the cocoa by the contractual date was critical [Problem at p.8] because the Claimant allowed the Respondent to choose the delivery dates and the installment plan [Graffi at p.341; Plate at p.65]. Furthermore, the Claimant's Mr. Sweet himself stated in his letter of 5 March 2002 that the Claimant was not under "any immediate pressure" to obtain cocoa until the later part of the year [Problem at p.10]. The Claimant was also not in shortage of cocoa as it had at

least 100 tons of cocoa in store at the time of the cover purchase; enough to last until the end of November 2002 [Procedural Order No. 2 at para.24]. Thus it can be concluded that time was not of the essence in the present contract.

35. In any event, it is for the Claimant to make clear to the Respondent what is important for each obligation and the corresponding interest [Schlechtriem, Uniform Sales Law in Germany at pp.22-23]. The undisclosed personal and subjective interest of the Claimant does not matter [Lorenz at II(A)] because it would be unreasonable to expect the Respondent to know the hidden thoughts of the Claimant [El-Saghir at (a); Vilus at p.1440]. The Claimant had ample opportunity to inform the Respondent that time was of the essence, if that was indeed the case, during the phone conversation when the contract was concluded [Problem at p.7] and again after receiving the contractual document [Problem at p.8]. However, it failed to mention time during the above instances [Problem at p.8] and failed to make the Respondent aware of the importance of timely performance. Accordingly, the Respondent should not be held liable for the Claimant's failure.

36. In addition, the importance of time is not ascertainable from the circumstances surrounding the contractual relationship of the parties in this case [Liu at 8.2.2.3; Jafarzadeh at 4.1]. Although the parties have been carrying on business relations for the past few years [Problem at p.2], the Claimant's conduct was no different in the instant contract and there was no indication of any derogation from past practices to make time of essence [Graffi at p.341; ICC Case No. 8817 of 1997]. On these facts, late delivery does not constitute fundamental breach [OLG München, 2 February 2002 (Germany)].

b. The Claimant did not suffer consequences of sufficient gravity to constitute substantial deprivation under the Cocoa Contract.

37. Substantial deprivation in Art. 25 CISG is characterised by the gravity of the consequences of the breach [Koch at p.218; Kazmierska, at p.106; BGH, 3 April 1996 (Germany)]. Where no detriment has been caused by the breach of contract, it is undisputed among scholars that there is no right of avoidance [Koch at p.218; Schlechtriem, CISG 1986 at p.60]. The absence of monetary loss denotes that a party was not substantially deprived [Koch at pp.238-245; Secretariat Commentary, Art. 25 at para.3]. In the instant case, the Claimant did not sustain any monetary loss in its confectionery production due to the delay in delivery, neither did the overall value of the contract decrease [Problem at p.16]. Hence, the Claimant's lack of monetary loss from production is indicative of its lack of detriment [Koch, Art. 25 at II(1); Babiak at p.118; Sutton at p.286].

38. Moreover, if there had been no detriment to a party at the point it purported to avoid the contract, that party could not have suffered any substantial deprivation [Koch, Art. 25 at II(1); Liu at 8.2.2.1; Gonzalez at p.86; Ziontz at p.173]. In the present case, at the time of the purported avoidance on 25 October 2002, the Claimant's business was not affected since its production was still ongoing [Problem at pp.10, 13]. This is indicative that it did not suffer any substantial deprivation [AG Ludwigsburg, 21 December].

39. Since the Claimant cannot show any consequences which would constitute substantial deprivation [UNCITRAL CISG Digest, Art. 25 at para.3; BGH, 3 April 1996 (Germany)], there cannot be a finding of fundamental breach in this case.

2. Even if the Claimant suffered substantial detriment, it was not and could not have been foreseeable by the Respondent or a reasonable person in its position.

40. In any event, even if the Tribunal finds that the Claimant has been "substantially deprived" of its essential expectation under the contract, there is still no fundamental breach under Art. 25 CISG because any substantial detriment suffered by the Claimant was not foreseeable. Foreseeability is determined at the time the contract was concluded [a]. In this case, the detriment was not foreseeable to the Respondent [b] and any reasonable person in the Respondent's position would not have foreseen such detriment [c].

a. Foreseeability is determined at the time of conclusion of the contract.

41. Art. 25 CISG does not expressly address the point in time at which foreseeability should be assessed [Secretariat Commentary, Art. 25 at para.3]. Although one might consider assessing foreseeability at the time of the breach [Soarez/Ramos at p.128, fn 83] or the period before the time of the breach [Honnold, at p.183], most scholars consider these interpretations to be too far-reaching [Koch at pp.230-231; Bianca/Bonell at Art. 25, at pp.220-221; Enderlein/Maskow at p.112; Herber/Czerwenka at Art. 25, at 9; Honsell/Karollus at Art. 25, at 27; Hoyer/Posch/Aicher at p.133; Neumayer/Ming at Art. 25, at 8]. Thus, the widely accepted view is that, the time of the conclusion of the contract is the decisive point at which foreseeability is to be ascertained [Schlechtriem at p.180; Neumayer/Ming at p.218; Heuzé at p.295; OLG Düsseldorf, 24 April 1997 (Germany)] since contractual expectations are formed at the time of contracting [Babiak at p.118; Liu at 8.2.3.3]. This position is further buttressed by the language of the said provision. The French ("était" instead of "est"), Spanish ("tenia" instead of "tiene") and Russian ("byla" instead of "yest") versions of Art. 25 CISG all use the past tense; which convey the impression that the formation of the contract is the relevant point in time to determine foreseeability [Koch at p.265; Schlechtriem, CISG 1986 at p.60].

42. This reading of Art. 25 CISG harmonises it with Art. 74 CISG, which explicitly requires damages to be foreseeable "at the conclusion of the contract", therein promoting consistency in the interpretation of the CISG remedial provisions [Kritzer at p.207; Galston/Smit/Ziegel at pp.9–2, 9–5, 9–6; Shen at p.12]. Thus, any special interests should be brought up when the bargain is struck [Schlechtriem at p.417; Enderlein/Maskow at p.114] and foreseeability of the detriment must be assessed at the time of the conclusion of the contract on 19 November 2001.

b. The detriment was not foreseeable to the Respondent at the time of the conclusion of the Cocoa Contract.

43. Under Art. 25 CISG, the Respondent would not be liable if it "did not foresee, and a reasonable person of the same kind in the same circumstances" would not have foreseen that the Claimant would suffer substantial deprivation as a result of the late delivery of cocoa [Schlechtriem at p.179].

44. This requirement of forseeability is purely subjective [Enderlein/Maskow at p.116] and depends on the Respondent's knowledge and evaluation of the relevant facts, its experience and its perception of the circumstances [Kritzer at p.217; Liu at 8.2.3.2]. The Respondent could not have foreseen the impact of a delay in delivery on the Claimant's production because it was not stipulated in the contract [Problem at p.8] and was not made known to the Respondent during the contract negotiations [Problem at p.7; Kritzer at p.217].

c. A reasonable person of the same kind as the Respondent would not have foreseen the detriment.

45. A reasonable person of the "same kind" and "in the same circumstances" as the Respondent would be a merchant engaged in the cocoa commodities trade [Schlechtriem at p.179; Vilus at p.1440; Kritzer at pp.218-219]. Taking into account the facts of the present case, a reasonable trader would not have foreseen any detriment to the Claimant's cocoa production [Koch, Art. 25 at 3b] since it would not be aware that timely delivery was of special importance to the Claimant [Respondent Memo. at paras.34-36; Schlechtriem at p.178; Koch, Art. 25 at II(1)] and it would not have foreseen any endangerment to the Claimant's business from a delay in delivery.

D. In any event, there was no valid declaration of avoidance prior to the conclusion of the cover purchase.

46. Even if the Tribunal finds that the Claimant is entitled to avoid the Cocoa Contract,

the Claimant failed to give the Respondent a proper declaration of avoidance. A contract does not end automatically upon the existence of a fundamental breach or the expiration of an additional period of time [Enderlein/Maskow at p.182]. Art. 26 CISG states that a declaration of avoidance is effective only when the requirement of notice to the other party is complied with [Babiak at p.153; LG München, 6 April 2000 (Germany)].

47. A valid declaration of avoidance must be made because the CISG does not recognise an *ipso facto* avoidance of the contract [Schlechtriem, Recent Developments at pp.309-326; Enderlein/Maskow at p.182]. Thus, the Claimant cannot argue that the Cocoa Contract has been terminated automatically [Claimant Memo. at para.67].

48. This declaration must also meet the required standard of clarity to inform a reasonable person of the intention to avoid the contract [Fletchner at p.83]. Although the word 'avoidance' need not be used, the wording of the avoidance notice must be unequivocal [UNCITRAL CISG Digest, Art. 26 at para. 5]. In the case of doubt, an imprecise letter should be interpreted as a mere 'threat' of avoidance [Enderlein/Maskow at p.243].

49. In the letter dated 15 August 2002, the Claimant merely informed the Respondent of its low stocks and the intention to purchase elsewhere if it did "not receive notification from the Respondent soon" [Problem at p.13]. This was not sufficiently clear and could not constitute a valid declaration of avoidance because it did not express a clear intention to avoid the contract [Kazmierska at p.115].

50. Furthermore, the Claimant cannot argue that the letter contained an effective notification on the basis of the CISG's "informality principle" [Bianca/Bonell at p.126]. This informality principle merely allows the notice to be oral or written and transmitted by any means [Secretariat Commentary, Art. 26 at para.4]. It does not detract from the requirement of clarity with respect to the content of the notice [Bianca/Bonell at p.126]. Accordingly, the letter of 15 August 2002 was not sufficiently definite and could not constitute a declaration of avoidance [OLG Frankfurt, 17 September 1991 (Germany)].

51. Similarly in the telephone call between the parties on 29 September 2002, the Claimant merely 'reiterated the concerns expressed in its letter of 15 August 2002 [Procedural Order No. 2 at para.22]. No further information was passed on from the Claimant which could be construed as an unequivocal expression of avoidance [Respondent Memo. at paras.48-50]. Accordingly, the telephone call cannot constitute a valid declaration of avoidance.

52. In fact, the Claimant only purported to avoid the contract on 25 October 2002 and on 15 November 2002 after it had made its cover purchase on 24 October 2002 [Problem at pp.14, 17]. Hence, the letter dated 15 August 2002 and the telephone call on 29 September 2002 did not constitute valid declarations of avoidance and the Claimant's purported substitute transaction is unjustified because Art. 75 CISG only allows a substitute transaction to be concluded after the contract has been avoided.

III. CONSEQUENTLY, EVEN IF THE RESPONDENT CANNOT RELY ON ART. 79 CISG, THE CLAIMANT IS STILL NOT ENTITLED TO CLAIM ANY DAMAGES.

53. Even if the Tribunal decides that the storm and EGCMO embargo were not valid impediments within the meaning of Art. 79(1) CISG so as to preclude the Respondent from paying damages under Art. 79(5) CISG [Respondent Memo. paras.1–22], the Claimant remains barred from claiming the sum of USD 289,353 as damages. The Claimant is not entitled to claim the said amount, being the difference between the cover purchase price and the contract price, because it has not fulfilled the requirements of Art. 75 CISG [A]. Neither can the Claimant rely on Art. 74 CISG to claim the said amount as its loss was not foreseeable at the time of conclusion of contract [B]. Even if the Tribunal finds that the Claimant is entitled to damages, it can only claim USD 179,026 as this would have been the maximum amount of losses (if any) if it had complied with its duty to mitigate losses under Art. 77 CISG or if it were to rely on Art. 76 CISG to calculate its damages [C].

A. The Claimant is not entitled to claim USD 289,353 for the difference in price between the cover purchase and the Cocoa Contract because it has not fulfilled the requirements of Art. 75 CISG.

54. In order for the Claimant to claim damages of USD 289,353 as the difference in price between the cover purchase and the Cocoa Contract, it must fulfil the requirements of Art. 75 CISG. The Claimant has not fulfilled these requirements because it was not entitled to make the cover purchase before the contract was avoided [1]. In any case, even if the Claimant was entitled to make a cover purchase, it is not entitled to claim USD 289,353 because the cover purchase was not concluded reasonably [2].

1. <u>The Claimant is not entitled to USD 289,353 because it was not entitled to make the cover purchase before the contract was avoided.</u>

55. Art. 75 CISG allows a substitute transaction to be concluded only after the contract has been avoided and failure to avoid the contract will render the claim for damages arising

from the substitute transaction inadmissible [OLG Bamberg, 13 January 1999 (Germany); DiMatteo/Dhooge/Greene/Maurer/Pagnattaro at p.417; OLG Düsseldorf, 22 July 2004 (Germany)]. A substitute transaction concluded prior to the avoidance of the contract does not fall within the operation of Art. 75 CISG [ICC Case No. 8574 of 1996].

56. In the present case, the Claimant was not entitled to conclude the purported substitute transaction and claim damages under Art. 75 CISG because it could not avoid the Cocoa Contract under Art. 49 CISG. This is because the Claimant did not give the Respondent additional time for performance [Respondent Memo. at paras.27-30] and the Respondent did not commit fundamental breach of the contract [Respondent Memo. at paras.31-45].

57. Further and in the alternative, the Claimant failed to give a proper declaration of avoidance in its letter dated 15 August 2002 and in its telephone call to the Respondent on 29 September 2002 [Respondent Memo. at paras.46-52].

58. In any case, the Claimant made its cover purchase on 24 October 2002 before it purported to avoid the contract on 25 October 2002 [Problem at p.14] and since the Claimant did not avoid the contract before concluding the substitute transaction, it is not entitled to damages for the cover purchase under Art. 75 CISG.

2. <u>Alternatively, the Claimant is not entitled to claim USD 289,353 because the cover purchase was not concluded reasonably.</u>

59. Art. 75 CISG requires the substitute transaction to be concluded in a reasonable manner and an unreasonable substitute transaction cannot be considered in measuring damages [Liu at 15.2.3]. For the substitute transaction to be concluded in a reasonable manner, the promisee must have acted as a careful and prudent businessman in the cocoa industry [Schlechtriem at p.575; ICC Case No. 8128 of 1995].

60. The Respondent submits that the Claimant's purported substitute transaction was not concluded in a reasonable manner as the Claimant failed to check with the Respondent on its ability to deliver before concluding the substitute transaction [Procedural Order No. 2 at para.22]. If the Claimant had done so, it would have known of the possibility of the termination of the EGCMO embargo [Procedural Order No. 2 at para.29; Problem at p.16].

61. The substitute transaction must also be concluded within a reasonable time after the contract has been avoided [OLG Düsseldorf, 14 January 1994 (Germany)]. The Claimant does not fulfil this requirement as it did not avoid the contract before making its cover purchase [Respondent Memo. at paras.23-52] and cannot claim damages under Art. 75 CISG.

B. Furthermore, the Claimant is not entitled to claim for its loss of profit as this loss was not foreseeable at the time of the conclusion of the contract within the meaning of Art. 74 CISG.

62. Art. 74 CISG seeks to compensate the loss of the aggrieved party. Damages under this provision are measured by expectation interests [Farnsworth at pp.247-253]. However, the calculation of damages under Art. 74 CISG is limited by the test which requires the loss to have been foreseeable by the party in breach at the time of the conclusion of the contract, in the light of the circumstances that it *knew or ought to have known* [Schlechtriem at pp.554, 567-568; Schneider at fn.45; Vékás at p.164]. This test of foreseeability is essentially both a subjective and objective test [Sutton Jeffrey at III B.1.].

63. First, the Respondent could not foresee the loss arising from the cover purchase as it did not know that time was of the essence in the Cocoa Contract. If indeed time was a critical element, it was not expressly provided for and the Claimant stated in its letter on 15 August 2002 that it would only need the cocoa "soon" [Problem at pp.8, 13]. Second, the Respondent could not have foreseen the cover purchase as it could not have known that a storm would have resulted in the EGCMO embargo [Procedural Order No. 2 at para.8]. Therefore, the claim for damages under Art. 74 CISG cannot be sustained because the loss was not foreseeable [RFCCI, 6 June 2000 (Russia); RFCCI, 24 January 2000 (Russia); OLG Bamberg, 13 January 1999 (Germany); Schlechtriem at p.571].

C. Alternatively, even if the Claimant is entitled to claim damages for the cover purchase, it is only entitled to USD 179,026.

64. Even if the Tribunal finds that the Claimant is entitled to claim damages, the amount of damages must be reduced to USD 179,026 either because it failed to mitigate its losses under Art. 77 CISG [1] or because damages are to be calculated by applying Art. 76 CISG [2].

1. <u>The Claimant's damages should be reduced to USD 179,026 because it failed to mitigate its losses under Art. 77 CISG.</u>

65. The Claimant is required to mitigate its losses under Art. 77 CISG [UNCITRAL CISG Digest, Art. 77 at para.6; RFCCI, 24 January 2000 (Russia)] by taking adequate preventive measures that are reasonably expected of a person acting in good faith in the circumstances [Bianca/Bonell at p.560; Schlechtriem at p.588; Liu at 14.5.2]. If the Claimant had checked with the Respondent prior to making its cover purchase, it would have realised that the EGCMO was going to lift the embargo which could have led to the lowering of cocoa prices in November 2002 [Problem at pp.16, 33]. Accordingly, the amount of damages that

can be claimed should be reduced by the amount that could have been avoided and the Claimant would only be entitled to claim USD 172,026 [Saidov at 4(a); Sutton at III.B.5].

2. The sum of USD 179,026 would be the sum derived by applying Art. 76 CISG.

66. The framework for calculation of damages in the CISG is found in Arts. 74-76. Thus, barring the application of Arts. 74 and 75 CISG [Respondent Memo. at paras.53-63], the Claimant can still avail itself to Art. 76 CISG when the requirements of Art. 75 CISG are not fulfilled [Sutton at III.B.3; Bianca/Bonell at pp.553-554; Kritzer at p.489].

67. Under Art. 76 CISG, damages will be calculated as the difference between the contract price and the current price at the date of avoidance [OLG Hamburg, 4 July 1997 (Germany); Zeller at 3; Enderlein/Maskow at p.306]. Despite the Claimant's assertion that the contract was validly avoided by the letter of 25 October 2002 [Claimant Memo. at para.71], the Respondent submits that this did not constitute a valid notice of avoidance as required under Art. 26 CISG because it did not state in unequivocal terms that it believed the contract to be avoided [Liu at 11.1; LG Frankfurt, 16 September 1991 (Germany)]. Therefore, the date of the purported avoidance of the contract was 15 November 2002 when the Claimant clearly stated that it considered the contract avoided [Problem at p.17].

68. Hence, the amount of damages that is recoverable by the Claimant is measured as the difference between the contract price and the price of cocoa on 15 November 2002. Given that the price of cocoa in November was at USD 1814.17 per metric ton [Problem at p.33], the damages that should be awarded for the cover purchase is USD 172,026 which is the difference between that price and the price fixed by the Cocoa Contract, and not USD 289,353 as claimed.

IV. THE TRIBUNAL HAS JURISDICTION UNDER ART. 21(5) SWISS RULES TO HEAR THE CROSS-CLAIM UNDER THE SUGAR CONTRACT.

69. The Tribunal has jurisdiction to hear the present dispute with respect to the Sugar Contract notwithstanding that it arises out of a different arbitration agreement from the Cocoa Contract. The parties, in contracting for the Geneva Rules, have consented to the subsequent application of the Swiss Rules, including Art. 21(5), in place of the Geneva Rules [A]. The Claimant cannot rely on the old Geneva Rules to avoid the effect of Art. 21(5) Swiss Rules because the Swiss Rules were the prevailing rules at the CCIG at the time of commencement of arbitration and Art. 21(5) Swiss Rules is not inconsistent with the *lex arbitri*, the UNCITRAL Model Law [B].

70. Art. 21(5) Swiss Rules provides that: "The arbitral tribunal shall have jurisdiction to hear a set-off defence even when the relationship out of which this defence is said to arise is not within the scope of the arbitration clause or is the object of another arbitration agreement or forum-selection clause." Hence, the Tribunal acquires jurisdiction to hear the dispute relating to the Sugar Contract because the dispute constitutes a set-off defence within the meaning contemplated in Art. 21(5) Swiss Rules [C]. Furthermore, the CCIG is the appropriate forum to hear the sugar dispute [D].

A. The parties have consented to the application of all the provisions of the Swiss Rules, including Art. 21(5), by its agreement to apply the Geneva Rules.

71. Although the parties did not expressly contract for the Swiss Rules, its application to the present proceedings is with the consent of the parties who had earlier contracted for the Geneva Rules. The Geneva Rules have been replaced by the Swiss Rules on 1 January 2004. The Claimant was informed of this replacement by the CCIG, subsequent to its request of arbitration, and yet it did not opt out of the Swiss Rules in favour of the old Geneva Rules after the Swiss Rules came into force [1]. Alternatively, the Claimant has waived its right to object specifically to the application of Art. 21(5) Swiss Rules [2]. In any case, the parties intended to apply the most up-to-date rules available at the CCIG at the time they commenced arbitration, which were the Swiss Rules [3].

1. The parties did not expressly opt out of the Swiss Rules which have automatically replaced the Geneva Rules after 1 January 2004.

72. The Swiss Rules entered into force on 1 January 2004, replacing the arbitration rules of the six Chambers of Commerce (Chambers of Commerce and Industry of Basel, Bern, Geneva, Ticino, Vaud and Zurich) [Scherer at p.119]. When the Claimant commenced arbitration on 5 July 2004, the Geneva Rules had ceased to take effect in international arbitrations [Scherer at p.119] and the applicable rules which were in force at the CCIG were the Swiss Rules [Problem at p.19].

73. Although the Geneva Rules do not contain any provision dealing with the future amendments of its provisions, Art. 1(1) Swiss Rules states that: "These Rules *shall* govern international arbitrations, where an agreement to arbitrate refers to… the arbitration rules of the Chambers of Commerce and Industry of… Geneva…" (emphasis added). Art. 1(3) Swiss Rules also provides that: "These Rules *shall* come into force on January 1st, 2004, and, *unless the parties have agreed otherwise*, shall apply to all arbitral proceedings in which the Notice of Arbitration is submitted on or after that date" (emphasis added).

74. The use of the word "shall" in the above provisions denotes the mandatory application of the Swiss Rules to international arbitrations commenced at any of the six Chambers of Commerce after 1 January 2004. Hence, as long as the parties have previously contracted for the arbitration rules of one of the six Chambers of Commerce, the Swiss Rules automatically take effect to govern the arbitration in question, unless the parties have expressly agreed otherwise [Scherer at p.120].

75. From the above provisions, it appears that an arbitration agreement entered into before 1 January 2004 will be subject to the old rules, only if both parties expressly agree [Scherer at p.120]. Moreover, it has been held by the Swiss Supreme Court that an opting out of the Swiss Rules in favour of the Geneva Rules requires a *specific agreement* [Imuna v. Octapharma (Switzerland) at p.516; Scherer at p.121]. However, there was no specific agreement between the parties to opt out of the Swiss Rules after the Swiss Rules entered into force in this case. The parties agreed to the application of the Swiss Rules as informed by the CCIG. Since institutional rules are contractual in nature [Gaillard/Savage at p.179; Sonidep v. Signoil (France)], when the parties consent to the application of the Swiss Rules, they are deemed to have agreed to all the provisions therein, including Art. 21(5) which confers jurisdiction on the Tribunal to hear set-off defences.

2. <u>The Claimant has waived its right to object to Art. 21(5) Swiss Rules.</u>

76. Contrary to the Claimant's assertion that its objection to the jurisdiction of this Tribunal to hear the cross-claim was "brought in time" [Claimant Memo. at para.117], it only objected when the Respondent filed its Statement of Defence and Counterclaim [Problem at p.40], by which time the Claimant is deemed to have waived its right to object to Art. 21(5) Swiss Rules.

77. When the Claimant submitted its Notice of Arbitration to the CCIG, it was notified that the Geneva Rules were no longer applicable and a copy of the Swiss Rules was enclosed for the Claimant's perusal [Problem at p.19]. Hence, the Claimant had actual notice of all the provisions in the new Swiss Rules when it commenced arbitration, including Art. 21(5). However, it never objected to any of the provisions of the Swiss Rules. In fact, the Claimant did not object to the application of the Swiss Rules or Art. 21(5) in its letters dated 12 July 2004 [Problem at p.20] and 21 July 2004 [Problem at p.23], and has impliedly consented to all the provisions of the Swiss Rules.

78. The Claimant first raised its objection to Art. 21(5) Swiss Rules [Problem at p.40]

only when the Respondent raised a set-off defence [Problem at p.28] because it realized that this provision could be prejudicial to its claim. Thus, the Claimant has waived its right to object to Art. 21(5) because it did not object to its application immediately. In line with the principle of good faith in international commercial law [Gaillard/Savage at p.819], the Claimant is estopped from objecting to Art. 21(5) Swiss Rules, given that it has impliedly consented to Art. 21(5) and the Respondent had relied on this provision to raise a set-off defence in the present case.

79. In any event, when parties opt to commence arbitration at a particular institution and adopt that institution's procedural rules, they have agreed to surrender the flexibility of "tailor-made" arbitration rules available in *ad hoc* arbitrations in favour of the convenience of automatic incorporation of a book of rules [Redfern/Hunter at p.45; Born at p.12]. Therefore, in choosing a particular institution to administer their arbitration, the parties have in effect also chosen the policy of that institution, which is reflected in its arbitration rules.

3. The parties intended to apply the most up-to-date arbitration rules available at the Chamber of Commerce and Industry of Geneva, which were the Swiss Rules.

80. In relation to the interpretation of contractual terms, the common law looks primarily to the external appearance of the contract which is based on the "expression theory" [Nicholas at p.48; Beale/Hartkamp/Kötz/Tallon at p.556; The Hannah Blumenthal (U.K.)]. On the other hand, the civil law follows the "will theory", which favours the true state of mind of the parties [8 April 1987, Cass. Civ. 3e (France); Nicholas at p.48; Beale/Hartkamp/Kötz/Tallon at p.556] and the surrounding circumstances of the contract [BGH, 23 February 1956 (Germany)]. However, it is doubtful whether this distinction has any provable substance today [Beale/Hartkamp/Kötz/Tallon at p.556] as the common law also allows implied terms to be read into contracts to ascertain the true intention of the parties [Treitel at p.201; Beale/Chitty at p.644; Shirlaw v. Southern Foundries (U.K.); The Moorcock (U.K.)].

81. In the Cocoa Contract, the words of the arbitration clause were very general since the parties merely provided for the "Rules of the Chamber of Commerce and Industry of Geneva" [Problem at p.4]. There are 3 versions of CCIG arbitration rules issued in 1980 [Geneva Chamber of Commerce and Industry Arbitration Rules], 1992 and 2000 [Chamber of Commerce and Industry of Geneva Arbitration Rules] respectively. Subsequently, on 1 January 2004, the CCIG adopted the Swiss Rules [Scherer at p.119]. If the parties had intended any specific set of Rules to govern the present arbitration, specific mention of the

name of that version of the Rules should have been made. This leads to the conclusion that the parties in this case contracted for the current CCIG arbitration rules subsisting at the time the arbitration was commenced, instead of any specific set of rules.

82. On the other hand, since institutional rules of arbitration may change from time to time, it can be implied from trade practice [Art. 8(3) CISG; Art. 1135 French CC; Baker v. Black Sea (U.K.); British Crane v. Ipswich (U.K.)] that parties in international arbitrations intend to adopt the most up-to-date rules for their arbitrations [Craig/Park/Paulsson at p.143]. Furthermore, there is no evidence from the circumstances of this case that the parties only intended the Geneva Rules specifically "as of 19 November 2001" to apply to the present arbitration. Therefore, the parties' intention as ascertained from the arbitration clause is to adopt the most up-to-date rules available at the CCIG which are the Swiss Rules.

B. In any event, the Swiss Rules were the prevailing rules at the time of commencement of arbitration and Art. 21(5) is a reasonable provision which is consistent with the *lex arbitri*.

83. In the present case, the parties are not entitled to rely on the old Geneva Rules because the Swiss Rules were the prevailing rules in force at the time of commencement of arbitration [1]. In any case, the application of Art. 21(5) Swiss Rules cannot be excluded because this provision is neither unexpected nor unjustified [2]. Furthermore, Art. 21(5) Swiss Rules is consistent with the *lex arbitri*, the UNCITRAL Model Law [Problem at p.4], and is applicable to the present arbitration [3].

1. <u>The Swiss Rules were the applicable rules at the time of submission to arbitration on 5 July 2004.</u>

84. The applicable arbitration rules are those in force at the time when the arbitration is commenced, regardless of whether these rules were in existence at the time of the conclusion of the contract [Jurong v. Black & Veatch (Singapore); Bunge SA v. Kruse (U.K.); Cremer v Granaria BV (U.K.); China Agribusiness v. Balli (U.K.); Offshore Int'l v. Banco (U.K.)]. The principle that the rules governing the proceedings are those in force at the time the arbitration is initiated is reflected in Art. 6(1) of the ICC Rules, which provides that: "the parties… shall be deemed to have submitted *ipso facto* to the Rules in effect on the date of commencement of the arbitration proceedings... ". This principle is consistent with the needs of administrative practice as agreements to arbitrate may lie dormant for many years. It is therefore desirable to give parties the benefit of the most up-to-date rules [Craig/Park/Paulsson at p.143].

85. Moreover, this principle is also reflected in the practice of other arbitral institutions.

For example, the ICC Tribunal has applied Art. 12(4) ICC Rules 1998, in force on the date of commencement of the arbitration, in preference to Art. 2(12) ICC Rules 1988, at the time of contracting, despite the objection of a party in that case [ICC Case No. 5622 of 1992]. Furthermore, it has been held that when parties agreed on the London Maritime Arbitrators' Association Small Claims Procedure of 1999, they must have intended that "the procedure current at the relevant date would be the procedure used" [Ranko v. Antarctic (U.K.)].

86. Therefore, the Swiss Rules apply to the present arbitration because they were the applicable rules at the time that the present arbitration was commenced.

2. <u>The parties cannot exclude the application of Art. 21(5) Swiss Rules because it is not an unjustified and unexpected provision.</u>

87. The Claimant argues that the relevant provision of the old version of certain arbitration rules could take precedence over the new provision if the changes in the new provision were structurally and fundamentally different and if the new rules were untenable or surprising [Claimant Memo. at para.113; Komplex v. Voest-Alphine].

88. However, this exception should be construed narrowly to apply only to cases where the new rules contain a provision that is entirely unjustified and unexpected [Scherer at p.121]. In the present case, Art. 21(5) Swiss Rules is not a provision that is completely unjustified and unexpected for the following reasons.

89. First, Art. 21(5) Swiss Rules is not unjustified because the principle behind this provision has received wide support from commentators and academics. It has been said that set-off should be possible in an arbitration even if the obligation that is used to set-off is subject to a different arbitration agreement, and even if the party setting-off could only have brought it as a claim before a different Tribunal [Karrer at p.177; World Arb. & Mediation Rep. 306 (1999); Berger, 1999 at V].

90. Secondly, Art. 21(5) Swiss Rules is not unexpected because it is not a provision that is entirely without precedent. Although the Geneva Rules do not contain any provisions dealing with the Tribunal's jurisdiction with regards to set-off defences, similar provisions are well accepted in other arbitral institutions in Switzerland [Art. 27 Zurich Rules; Art. 29 Basel Rules; Art. 12 Ticino Rules; Art. 16 German-Swiss Chamber of Commerce Rules; Berti/Honsell/Vogt/Schnyder/Blessing at p.183].

91. Moreover, the plans for harmonizing the various arbitration rules of the six Chambers of Commerce have taken place over a long period of time which started from the mid-1990s

[Lévy at N-25]. These changes have not only been advertised in writing, but also via the Chambers' websites over the years [ITA March 2004; Jusletter July 2004]. The adoption of the Swiss Rules has been well publicized in interested circles and known by lawyers who engage in international commercial arbitrations [Procedural Order No. 2 at p.55]. Thus, the parties, being legally advised by counsel, would have constructive notice of the changes pending in the Geneva Rules, including the present Art. 21(5) Swiss Rules.

92. Hence, the parties cannot exclude Art. 21(5) from the Swiss Rules because it is not unjustified and unexpected.

3. Art. 21(5) Swiss Rules is consistent with the UNCITRAL Model Law and is applicable to the present case.

93. Although the UNCITRAL Model Law, as the law governing the arbitration proceedings (*lex arbitri*), does not contain any express provision that deals with the Tribunal's jurisdiction with regards to set-off defences, it does not prohibit parties from raising set-off defences in arbitrations.

94. Art. 23(2) UNCITRAL Model Law states that: "… either party may amend or supplement his claim or defence during the course of the arbitral proceedings…". This provision also applies to allow the Respondent to "amend or supplement" its statement of defence by bringing a counterclaim or a claim for the purpose of a set-off at a later stage [Seventh Secretariat Commentary, Art. 23 at para.8].

95. Moreover, Art. 19(1) UNCITRAL Model Law provides that: "Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings." This provision establishes the principle of party autonomy in governing the procedural conduct of the arbitration [Holtzmann/Neuhaus at p.564] and allows the parties to tailor the rules according to their specific needs and wishes, including referring to standard rules for institutional arbitrations [Seventh Secretariat Commentary, Art. 19 at para.2].

96. The freedom of the parties, under Art. 19, is subject only to the mandatory provisions of the UNCITRAL Model Law [Seventh Secretariat Commentary, Art. 19 at para.3; Holtzmann/Neuhaus at p.564]. The analytical commentary on Art. 19 UNCITRAL Model Law lists the mandatory provisions which the parties may not derogate from. However, Art. 21(5) Swiss Rules, in extending the Tribunal's jurisdiction to hear cross-claims in the form of set-off defences, does not conflict with any of these mandatory provisions. In particular, Art.

21(5) Swiss Rules does not contradict the principle of fairness in Art. 18 UNCITRAL Model Law and the other mandatory provisions concerning the conduct of the proceedings or the making of the award [Arts. 23(1), 24(2), (3), 27, 30(2), 31(1), (3), (4), 32 and 33(1)(a), (2), (4), (5) UNCITRAL Model Law; Seventh Secretariat Commentary, Art. 19 at para.3].

97. Hence Art. 21(5) Swiss Rules is consistent with the UNCITRAL Model Law and the Respondent is entitled to rely on this provision to raise a set-off defence arising from the Sugar Contract.

C. The Tribunal has jurisdiction to hear the cross-claim relating to the Sugar Contract because the claim falls within the scope of Art. 21(5) Swiss Rules.

98. Art. 21(5) Swiss Rules operates in the present case to extend the Tribunal's jurisdiction to cover the cross-claim under the Sugar Contract even though this dispute does not fall within the scope of the arbitration clause in the Cocoa Contract [1]. This dispute constitutes a set-off defence within the meaning of the Art. 21(5) Swiss Rules [2] and even if the Tribunal finds that the present dispute is a counterclaim instead of a set-off, Art. 21(5) Swiss Rules can also be interpreted to cover a counterclaim as the difference between a set-off defence and a counterclaim is minimal in the present case [3].

1. <u>Art. 21(5) Swiss Rules extends the Tribunal's jurisdiction to hear the cross-claim under the Sugar Contract even though the dispute does not fall within the scope of the arbitration clause in the Cocoa Contract.</u>

99. An extension of the Tribunal's jurisdiction to accommodate a set-off defence can be expressly agreed upon by the adoption of certain institutional rules [Berti/Honsell/Vogt/Schnyder/Wenger at p.470], even if the set-off arises from a different contract or is the object of another arbitration agreement [Lew/Mistelis/Kröll at p.154]. In fact, many arbitral institutions in Switzerland provide for rules that allow a set-off defence which arises from a different arbitration agreement to be heard by the Tribunal, such as Art. 27 Zurich Rules, Art. 29 Basel Rules, Art. 12 Ticino Rules and Art. 16 Swiss-German Chamber of Commerce Rules [Berti/Honsell/Vogt/Schnyder/Wenger at pp.154, 183; Berger, 1999 at V].

100. Similarly, the drafters of the Swiss Rules intended to extend the Tribunal's jurisdiction on defences raised by the Respondent [Claimant Memo. at para.124] and Art. 21(5) Swiss Rules provides an exception for this Tribunal to hear the cross-claim relating to the Sugar Contract, even though the dispute does not fall within the scope of the arbitration clause in the Cocoa Contract.

2. <u>The present dispute relating to the Sugar Contract is a set-off defence within the meaning of Art. 21(5) Swiss Rules.</u>

101. Although it has been suggested that a set-off defence, in order to be admissible in an arbitration proceeding, must arise out of the same legal relationship [Berger, 1999 at 3; Art. 19(3) UNCITRAL Arbitration Rules; §33(1) Moscow Rules] or be closely connected to the main claim [Arb. Law Monthly Nov. 2004 at p.5; National Westminster v. Skelton (U.K.) at p.76; Ronly v. JSC (U.K.); Benford v. Lopecan (U.K.)], Art. 21(5) Swiss Rules operates as an express exception to the requirement of a close connection between the main claim and the set-off defence. Hence, the set-off defence arising under the Sugar Contract does not have to be intrinsically linked to the main claim in the Cocoa Contract in order to be admissible.

102. Moreover, it is immaterial that the set-off is pleaded as a "counterclaim" in this case [Newfoundland Govt. v. Newfoundland Railway (U.K.); Young v. Kitchin (U.K.)] because the distinction between a set-off defence and a counterclaim is to be determined as a matter of law and is not governed by the language used by the parties in their pleadings [Hanak v. Green (U.K.)]. Therefore, in the present case, notwithstanding the terminology chosen by the parties, the cross-claim arising from the Sugar Contact constitutes a set-off defence within the meaning of Art. 21(5) [Wood at p.244].

3. <u>In any event, there is negligible difference between a set-off defence and a counterclaim in this case as Art. 21(5) Swiss Rules can be interpreted to cover both.</u>

103. Even if the Tribunal finds that the cross-claim relating to the sugar dispute is not a set-off defence but merely a counterclaim, Art. 21(5) Swiss Rules still operates to confer jurisdiction on this Tribunal to hear the cross-claim. This is because Art. 21(5) Swiss Rules can be construed to cover both set-off defences and counterclaims.

104. The Respondent acknowledges that there are differences in the legal definitions of set-off defences and counterclaims [Claimant Memo. at para.124]. However, when claims of money are at stake in international arbitrations, set-offs and counterclaims are "only a hair's breadth away" from each other [Wood at p.13]. This is because both may be based on the same factual pattern, which is the co-existence of asserted claims between the parties [Berger, 1999 at p.465]. Hence, a set-off in international arbitration is sometimes regarded as a "counterclaim in disguise" [Berger, 1993 at III].

105. Moreover, the outcome of a counterclaim, the order of a "net" judgment between the parties, is also similar to that of a set-off [Berger, 1999 at III]. In some jurisdictions, counterclaims and set-offs are closely intertwined [Berger, 1999 at III; Art. 70 French

Nouveau Code de Procédure Civil]. In fact, many international arbitration rules treat a set-off and a counterclaim as the same thing. Under the UNCITRAL Model Law, a Respondent, raising the plea of set-off, has to state the facts supporting its defence in the same manner as it would have to support a counterclaim [Seventh Secretariat Commentary, Art. 23 at para.7]. The same applies under Arts. 19(4), 18(2) of the UNCITRAL Arbitration Rules and Art. 42(c) of the WIPO Arbitration Rules. In addition, a party invoking set-off in an ICC arbitration will have to pay an advance on costs as if it had raised a counterclaim [Art. 30(5), ICC Rules 1998]. Therefore, in this case, there is negligible difference between a set-off defence and a counterclaim, especially since both disputes concern monetary claims [Wood at p.13].

106. Furthermore, the scope of Art. 21(5) Swiss Rules is very wide. This provision is intended to cover a set-off defence "even when the relationship out of which that defence is said to arise is not within the scope of the arbitration clause or is the object of another arbitration agreement or forum-selection clause". Hence, this provision encompasses all forms of cross-claims, including counterclaims which do not have any connection with the main claim.

D. The Chamber of Commerce and Industry of Geneva is the appropriate forum to hear the cross-claim arising under the Sugar Contract.

107. The Claimant argues that the Oceania Commodity Association is the accurate forum to hear the sugar dispute because it specialises in commodity arbitrations [Claimant Memo. at para.92]. However, it makes no difference in this case whether the Oceania Commodity Association or the CCIG hears the dispute under the Sugar Contract because this dispute only involves general issues relating to commodity trade.

108. Where the dispute only involves general questions of law or trade practices, specialised arbitration facilities such as the Oceania Commodity Association have no particular advantage over arbitration institutions for international commercial arbitration in general [Procedural Order No. 2 at para.6]. Furthermore, an expert tribunal is not required to determine the quality of sugar. In any case, the Claimant and the Respondent do not belong to any association that would require arbitration in any particular arbitration institution [Procedural Order No. 2 at para.6].

109. The Claimant also argues that since the present arbitration is subject to the Expedited Procedure under Art. 42 Swiss Rules, it would be too complex for this Tribunal to hear the set-off defence relating to the Sugar Contract [Claimant Memo. at para.96]. Notwithstanding

the fact that Expedited Procedures are only suitable for determination of certain issues, it has been acknowledged that quality determination is an issue that is capable of being resolved using Expedited Procedure [Lew/Mistelis/Kröll at p.550]. Hence, the set-off defence under the Sugar Contact is suitable for determination using the Expedited Procedure.

110. Moreover, even if an arbitration held in Oceania facilitates the collection of evidence with regards to the cross-claim relating to the sugar contract [Claimant Memo. at para.95], it is still more economical and efficient for this Tribunal to hear this dispute as a set-off defence instead of setting up another Tribunal in Oceania, which will result in additional time and expenses to the parties.

V. EVEN IF ART. 21(5) SWISS RULES DOES NOT APPLY IN THE PRESENT CASE, THE TRIBUNAL STILL HAS JURISDICTION TO HEAR THE CROSS-CLAIM RELATING TO THE SUGAR CONTRACT AS A SET-OFF DEFENCE.

111. Even if the Tribunal finds that Art. 21(5) Swiss Rules does not apply to the present arbitration, the Tribunal still has jurisdiction to hear the cross-claim relating to the Sugar Contract because the arbitration agreement under the Cocoa Contract can be interpreted broadly to allow a set-off defence to be raised [A]. In the present case, this Tribunal has jurisdiction to hear the cross-claim relating to the Sugar Contract as it satisfies the requirements of a set-off defence [B]. Furthermore, the complete determination of the Cocoa Contract requires the Tribunal to deal with this cross-claim [C].

A. The arbitration agreement under the Cocoa Contract can be interpreted broadly to allow a set-off defence to be raised.

112. The Tribunal, when interpreting arbitration agreements, must look to the parties' intention [Respondent Memo. at para.80] and there is a common presumption that the parties wish to resolve all their disputes in a single arbitration instead of splitting the jurisdiction between different Tribunals [Karrer at p.176]. Accordingly, ordinary rules of interpretation lead to the suggestion that arbitration agreements should be interpreted very broadly [Karrer at p.176]. Hence, in this case, the arbitration agreement under the Cocoa Contract can be interpreted broadly to encompass a set-off defence.

113. In international arbitrations, there is an increasing trend to assume that as a rule, the Tribunal has jurisdiction to hear a set-off defence based on a cross-claim that is subject to a different arbitration agreement [Berger, 1999 at III]. This approach is based on the need to find procedural efficiency in international arbitrations by encouraging the elimination of

disputes between parties [World Arb. & Mediation Rep. 306 (1999) at V(II)]. Hence, "clear indications" are required for "exceptional cases" where the parties intend to exclude the Tribunal's competence over such cross-claims [ICC Case No. 5971 of 1995].

114. The Claimant asserts that procedural economy is not an important aspect in arbitration *at all* and the value of forum selection clause prevails over the need for efficiency [Claimant Memo. at para.120]. However, it has been recognised that in the eyes of the parties to a standard arbitration agreement, the parties' interest to have their claim and cross-claim decided simultaneously and in one single instance outweighs the interest to preserve a different competent Tribunal for the cross-claim [Honsell/Vogt/Schnyder/Wenger at 28].

115. Similar to consolidation of arbitral proceedings, allowing this Tribunal to hear the cross-claim in this case reduces costs, increases speed and makes proceedings more efficient [Platte at III(i); Redfern/Hunter at p.174; Leboulanger at pp.54, 55, 62]. This makes more commercial sense [Mustill at pp.393-402], as separate proceedings would result in a possible delay of related business transactions and inconsistent decisions [Nicklisch at p.69; Gaillard/Savage at p.36; Abu Dhabi v. Eastern Bechtel (U.K.)].

116. The Claimant argues that since the Sugar Contract was entered into later in time than the Cocoa Contract, it prevails over the Cocoa Contract and any dispute arising under the Sugar Contract can only be referred to arbitration in Oceania [Claimant Memo. at para.97]. Nevertheless, it has been acknowledged that the existence of incompatible arbitration or forum selection clauses does not automatically render it impossible to set-off obligations [Karrer at p.177].

117. Moreover, contracts are primarily designed to prevent disputes or to resolve them amicably [Karrer at p.177]. Therefore, in light of the increasing trend of hearing a set-off defence from a different arbitration agreement, it will make commercial sense for the parties who have a long standing business relationship in the present case [Problem at p.2] to have the dispute resolved by the Tribunal already in place [Karrer at p.177].

B. The cross-claim under the Sugar Contract satisfies the requirements of a set-off defence.

118. Generally, a set-off is a form of extinction of two obligations of the same kind existing reciprocally between two parties [ICC Case No. 3540 of 1980]. However, its nature continues to be controversial and varies from jurisdiction to jurisdiction [Goode, 1988 at p.132]. In this case, where neither the UNCITRAL Model Law nor the CISG, defines a set-

off defence [OLG München, 28 January 1998 (Germany); OLG Koblenz, 17 September 1993 (Germany); UNCITRAL CISG Digest, Art. 74 at para.13], it is possible to derive from the laws of various jurisdictions and general principles of law [ICC Case No. 3540 of 1980] the common criteria that have to be fulfilled in order for a set-off defence to arise.

119. The cross-claim arising from the Sugar Contract in the present case constitutes a set-off defence because the main claim and the cross-claim satisfy the requirements of a set-off defence under general principles of law which are mutuality of claims [1], obligations of the same kind [2], mature claims [3] and liquidity [4]. Furthermore, the set-off in this case is not precluded by contract and does not prejudice the interests of the parties [5].

1. <u>There is mutuality of claims in this case.</u>

120. In the first place, in order for a set-off defence to arise, there has to be mutuality in the sense that the creditor of one claim is the debtor under the other claim, and vice versa [Zimmermann at p.45; Art. 1289 French CC; § 387 GBG; Art. 1241 Italian CC; Art. 1195 Spanish CC; Art. 6:127(2) Dutch BW; §§ 1438, 1441 Austrian ABGB; Art. 440 Greek AK]. In common law, the underlying idea is often expressed by stating that the claims must exist between the same parties and in the same right [Ince Hall v. Douglas Forge (U.K.); Shand v. Atkinson (New Zealand); Peel v. Fitzgerald (Australia); Derham at pp.15, 108, 441, 467, 493; Goode at p.263]. In this case, the set-off defence is not invalidated on the grounds of lack of mutuality because the Respondent is the debtor in the Cocoa Contract and the Claimant is the debtor in the Sugar Contract [Wood at p.766].

2. <u>The main claim and the cross-claim are obligations of the same kind.</u>

121. Secondly, the obligations owed by the parties towards each other must be of the same kind. Hence, a money claim can only be set-off only against a money claim, while a debt for the delivery can only be set-off against a claim for the delivery of the same kind in the civil law [Zimmermann at p.48; § 387 German BGB; Art. 6:127 Dutch BW; § 1438 Austrian ABGB; Art. 440 Greek AK; Art. 1234(I) Italian CC; Art. 1196(2) Spanish CC; Art. 1291(I) French CC]. In addition, the common law confines set-off to money debts only [Goode at p.265; Wood at p.461]. In the present case, both the main claim and the set-off defence are monetary claims as well as obligations of the same kind.

3. <u>The main claim and the cross-claim are mature claims.</u>

122. Thirdly, both the main claim and the cross-claim must be due and enforceable in order for the cross-claim to qualify as a set-off defence in both civil law and common law

jurisdictions [Zimmermann at p.50; §§ 387, 390(I) German BGB; Art. 6:127(2) Dutch BW; Art. 1243(I) Italian CC; Art. 1196 (3 and 4) Spanish CC; Art. 440 Greek AK; Wood at p.68; Goode at p.260]. This requirement is also satisfied as both the debts under both contracts had matured by the time of commencement of arbitration [Richards v. James (U.K.)].

4. The main claim and the cross-claim are liquidated.

123. Fourthly, in both civil law and common law jurisdictions, the main claim and the cross-claim must be liquidated in order for a set-off defence to arise [Zimmermann at p.51; Art. 1291 French CC; Art. 1243 Italian CC; Art. 1196(4) Spanish CC; Art. 1244 Greek AK; Wood at p.52]. Both the claims must be certain [Zimmermann at p.51] and commensurable [Wood at p.1152]. In fact, money claims are usually treated as liquidated in England and other jurisdictions [Wood at p.1153]. Hence, in the present case, the requirement of liquidity is satisfied as the amount of damages claimed under both contracts has been ascertained.

5. The set-off defence in this case is not excluded by contract and does not prejudice the Claimant's interest.

124. Finally, the set-off defence in the present case is not excluded by contract [Zimmermann at p.56] as there is no indication that the Cocoa Contract rules out the possibility of a set-off defence. In fact, the arbitration agreement can be interpreted broadly to favour the raising of a set-off defence [Respondent Memo. at paras.112-117]. Moreover, the *lex arbitri* in this case, the UNCITRAL Model Law, does not prohibit the Respondent from raising a set-off defence [Respondent Memo. at paras.93-97].

125. Furthermore, the Claimant's interest is not prejudiced by the set-off defence in this case. Although cross-claims may be used as a delaying tactic or retaliatory device [Ulmer at pp.33, 42] in international arbitrations [Berger, 1999 at III], the set-off in this case is raised in good faith. The parties are not deprived of their right to be heard and the right of equal treatment under Art. 18 of the UNCITRAL Model Law.

126. Even though the Claimant argues that the parties are entitled to appoint only three arbitrators instead of six under the arbitration agreements [Claimant Memo. at para.93], the Claimant is not disadvantaged as neither party will have preferential treatment over the other [Lew/Mistelis/Kröll at p.406; Honatiau at II]. As long as both parties are treated equally in that each party has a choice of nominating an arbitrator [Berger, 1993 at pp.316-318], the right to nominate three arbitrators need not be treated as sacrosanct [Stippl at p.57].

C. The complete determination of the claim under the Cocoa Contract requires the set-off defence arising out of the Sugar Contract to be dealt with in the present arbitration.

127. Since the complete determination of a claim necessarily entails the consideration of any objections raised in relation to that claim, the Tribunal should be allowed to decide on all defences which are raised against that present claim ("*le juge de l'action est le juge de l'exception*"), and consequently also on the merits of the set-off in that case [Berger, 1999 at V(ii); Perret at p.303; ICC Case No. 5971 of 1995].

128. The "*le juge de l'action est le juge de l'exception*" principle (the judge of the action is the judge of the exception/defence) is frequently used by the Swiss Federal Tribunal and is the prevailing doctrine in Switzerland [Berger, 1999 at fn.131]. Furthermore, this principle is reflected in institutional rules, such as Art. 21(5) Swiss Rules and Art. 27 Zurich Rules, which respond to the need of the parties seeking a determination in respect of all unsettled controversies [Barin/Blessing at p.303]. The general thrust behind this principle is of a highly practical nature. It is said to avoid "overly formalistic" solutions [ICC Case No. 5971 of 1995] and thereby preserve the procedural economy of arbitration. The simultaneous adjudication of claims and cross-claims via the set-off defence is in the presumed interest of the parties to the arbitration [Berger, 1999 at V(ii)]. Therefore, when faced with a situation where the arbitration clauses differ from each other, the Tribunal may in the appropriate case, exercise their *kompetenz-kompetenz* in accordance with Art. 16(1) UNCITRAL Model Law to hear a set-off defence [Platte at II].

VI. THE AWARD OF THIS TRIBUNAL WILL BE ENFORCEABLE UNDER THE UNCITRAL MODEL LAW AND THE NEW YORK CONVENTION.

129. It must be emphasised from the outset that this Tribunal should not be concerned with the question of enforceability of the award as it is only instructed to rule on its jurisdiction with regards to the Sugar Contract. However, in response to the Claimant's argument that the award issued by this Tribunal will be invalid and unenforceable if the cross-claim relating to the Sugar Contract is heard [Claimant Memo. at para.119], it is the Respondent's position that the arbitral award issued by this Tribunal will not be invalidated by either the UNCITRAL Model Law or the New York Convention as the sugar dispute does not involve matters beyond the scope of submission to arbitration [Art. 34(2)(a)(iii), UNCITRAL Model Law; Art. V(1)(c), New York Convention], for the aforementioned reasons [Respondent Memo. at paras.69-128].

VII. THE RESPONDENT IS ENTITLED TO SET OFF THE DAMAGES OWED TO IT UNDER THE SUGAR CONTRACT.

130. For the foregoing reasons, the Respondent is entitled to claim the full contract price under the Cocoa Contract, up to USD 385,805 [A]. In any event, even if the Tribunal finds that the Respondent cannot recover the full amount of damages under the Sugar Contract, it is still entitled to set-off the amount claimed by the Claimant under the Cocoa Contract, up to USD 289,353 [B].

A. The Respondent is entitled to set-off the full amount of damages up to USD 385,805 owed to it under the Sugar Contract.

131. Even though it has been said that a set-off is a mere defence mechanism and not a device to attack [Stein v. Blake (U.K.) at p.966; Berger, 1999 at III], the fact that the amount pleaded in set-off exceeds the amount pleaded in the main claim does not prohibit the Respondent from recovering the full amount of damages owed to it under the Sugar Contract [The Transoceania Francesca (U.K.)]. Thus, in this case, the Respondent is entitled to claim the full amount of the contract price, USD 385,805, under the Sugar Contract.

132. Moreover, even if the Tribunal finds in favour of the Claimant with respect to the Cocoa Contract, the Respondent would still be entitled to recover from the Claimant the balance after the cross-claim has extinguished the main claim [The Transoceania Francesca (U.K.)].

B. In any case, the Respondent is still entitled to set-off the amount up to USD 289,353 that is initially claimed by the Claimant under the Cocoa Contract.

133. A set-off occurs as long as the debtor can reduce or extinguish the amount of the creditor's claim by his own cross-claim [Derham at p.1]. Hence, even if the Tribunal holds the view that the Respondent cannot recover the full amount of damages under the Sugar Contract, the Respondent is at least entitled to set-off the amount pleaded by the Claimant under the Cocoa Contract, which is USD 289,353.

VIII. PRAYER FOR RELIEF

134. In accordance with the Tribunal's Procedural Order No. 2:

Counsel for the Respondent requests that the Tribunal find against the Claimant because:

1. The Respondent is exempted from liability for damages because the EGCMO embargo in Equatoriana constituted an impediment;
2. The Claimant is not entitled make the cover purchase because it was not entitled to avoid the Cocoa Contract;
3. The Claimant is not entitled to claim USD 289,353 for the difference between the cover purchase price and the Cocoa Contract Price;
4. Even if the Claimant has the right to damages, the amount to be paid by the Respondent should be limited to USD 172,026;
5. The Tribunal has jurisdiction to hear the cross-claim with respect to the Sugar Contract;
6. The Respondent is entitled to claim damages owed to it under the Sugar Contract.

135. Consequently, the Respondent respectfully requests the Tribunal to order:

1. The Claimant to pay the Respondent the sum of USD 385,805, being the full contract price of the Sugar Contract;
2. The Claimant to pay interest at the prevailing market rate in Equatoriana on the said sum from 18 December 2003 until the date of payment;
3. The Claimant to pay the costs of arbitration, including the costs incurred by the parties

Signed:

Counsel for the Respondent