Thirteenth Annual Willem C. Vis International Commercial Arbitration Moot
Vindobona, Danubia, March 2006

Ref: CIDRA Arbitration case No. 2005-0013

In the matter of:

Claimant
Oceania Printers S.A.
Tea Trader House
Old Times Square
Magreton, 00178, Oceania

versus

Respondent
McHinery Equipment Suppliers, Pty.
The Tramshed
Breakers Lane
Westeria City 1423, Mediterraneo

MEMORANDUM

for

CLAIMANT

National University of Mexico

~Counsel~

Raúl Aldana, Diego Curiel, Daniela Gómez, Andrea Hernández, Daniela Hernández, Ignacio Piña, Patricia Uribe, Elizabeth Zorilla, Ayesha Borja, Mayán Tejeda

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1. THE ARBITRAL TRIBUNAL IS NOT BARRED BY ANY APPLICABLE STATUTE OF LIMITATIONS TO RENDER AN AWARD ON THE MERITS OF THIS CASE

1.1 SUBSTANTIVE LAW GOVERNING THE PERIOD OF LIMITATION AT ISSUE ALLOWS FOR OCEANIA PRINTERS TO INSTITUTE ARBITRAL PROCEEDINGS

1.1.1 ALTHOUGH CISG IS THE PROPER LAW CHOSEN BY PARTIES, THIS CONVENTION DOES NOT GOVERN ISSUES REGARDING STATUTE OF LIMITATIONS

1 The commercial relationship between McHinery Equipments and Oceania Printers, by their own express choice, is governed by CISG. It is not disputed that from the parties' standpoint, the issue of the statute of limitation is considered a substantive one, [Procedural Order No. 2, statement 4]. It is also incontestable that the substantive law designated by McHinery Equipments and Oceania Printers does not contemplate a statute of limitations in regard to actions brought either before a court of law or an arbitral tribunal. The narrow scope of CISG, which neither contains an applicable limitation period nor governs the question at all, can be evidenced in the Convention's negotiating history, where it was made clear that the issues of prescription should be covered by a separate convention on that matter, namely the UN Convention on the Limitation Period in the International Sales of Goods of 1974. Accordingly, it was agreed that any statute of limitation in regard to actions brought before an arbitral tribunal would not be considered by CISG in order to reach the unification of rules on prescription. [HONNOLD/Legislative History p.195] Nevertheless, it is worth noting for the purposes of supporting our following submissions that, had the Working Group decided to include a specific period of limitation, it would have ultimately been of a range between three and five years [HONNOLD/Legislative History].

2 Importantly, a deliberate *exclusion* from the scope of CISG, -such as that regarding statute of limitations-, must not be confused with a *gap* in said Convention. The difference being that while an issue falling outside CISG's limited field of application is governed by the rules of law deemed to be applicable on the facts of each particular case, an issue covered by CISG but not resolved

by any express rule is said to fall in a gap, which is to be filled in accordance with the Convention's self-contained mechanism and principles.

3 Thus, article 7 of CISG provides that questions concerning matters governed by the Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law. "In light of the broad and pregnant principles underlying the Convention, most interstitial gaps can be filled by using general principles". [MATHER, KRITZER §158]

4 In short, the statute of limitation is not a *gap* in the Convention requiring to be filled, but rather an excluded issue falling outside the scope of CISG, and accordingly, "for claims not governed by CISG, a choice-of-law process must be employed to resolve conflicts between statutes of limitations". [MATHER § 156]

5 It follows that the tribunal must ascertain the applicable law by resorting to the appropriate conflict-of-laws rule. "This power and authority are both implied in the general submission of disputes to arbitration, and in the law or rules governing the arbitration". [MISTELIS p.425]

1.1.2 THE ARBITRATION RULES DESIGNATED BY THE PARTIES PROVIDE A STANDARD TO ASSIST ARBITRATORS IN DETERMINING THE APPLICABLE LAW

6 According to article 32 paragraph 1 of CIDRA Arbitration Rules, the arbitrators should apply the law designated by the parties to rule the substantive issues of the dispute. On the other hand, paragraph 2 of the same rule states that failing such designation by the parties, the arbitral tribunal shall apply the law determined by the conflict of laws rules which it considers applicable.

7 In the present case, as the substantive law chosen by the parties is silent on the matter, and even though the second paragraph of article 32 of CIDRA might not admittedly seem *prima facie* applicable, it is submitted that the arbitrators must necessarily apply the standard provided by the second paragraph of such rule, for it is well settled that arbitrators are empowered to ascertain the substantive rule concerned, pursuant to the conflict-of-laws rules they deem applicable,

whenever the applicable law chosen by the parties proves to be incomplete. [MISTELIS, GRIGERA NAON p.424]

8 Furthermore, a leading commentator endorses the proposition that arbitrators are even entitled to disregard the law chosen by the parties where there is an incomplete character of that law. [FOUCHARD p. 842.] This entails that when the law does not provide an answer to the issue in dispute, the arbitrators are empowered to make reference to another law or the general principles of law. The 1992 ICSID award made in the SPP case provides a clear example of this situation. The arbitral tribunal considered that even if the parties had chosen Egyptian law the arbitrator was entitled to supplement that law by applying supranational rules.

9 In the case at hand, while it is beyond contention that the designation of CISG as the applicable law to the merits of the dispute was indeed made in the present case, as far as this governing law is deliberately silent on the issue of statute of limitations, the Arbitral Tribunal must therefore resort to the most appropriate conflict of laws rule to cure the omission of the substantive law.

10 For its part, CIDRA arbitration rules allow arbitrators to determine a conflict of laws rule they consider appropriate. In fact arbitration tribunals have applied various different conflict of laws systems including conflict rules the tribunal considers appropriate.

11 It is to be noted that "*appropriate"* does not have a limited meaning and can be applied in a broad sense, leaving it to the discretion of arbitrators on the facts and circumstances of each case. For instance, it has been submitted that the provisions "in the European Convention left arbitrators free to select a conflict rule from a national conflict system, a relevant international convention, academic writing, or even a rule which the arbitrators for good or esoteric reasons considered appropriate". [MISTELIS p.431]

12 By the same token, it is widely accepted that in ascertaining the substantive law, arbitrators must take into account "external factors which are associated with the intention of the parties, such as their expectations as to the applicable law or the substantive outcome of the dispute and some considerations such as the needs of international trade, international commercial arbitration and rules and principles of public international law". [GRIGERA, NAON p.221]

13 An Arbitral Tribunal constituted under the Stockholm Chamber of Commerce (Award Number: 117/1999) interpreted the intention of the parties, namely Chinese and European companies, to exclude the application of any domestic law, based on the silence of an applicable law and declared that the application of UNIDROIT Principles "rules of law considered to be most appropriate" in case at hand. In the British Petrolyum v Libya of 1973 arbitration, Judge Lagergren held that the Arbitral Tribunal “is at liberty to choose the conflict of laws rule that it deems applicable, having regard to the circumstances of the case”.

14 Whilst for some time there was the belief that the forum chosen by the parties should have an impact on the applicable law, in modern conflict-of-laws rules arbitrators recognize that is not appropriate to link the legal issues that arise from international contract to a national legal system as “parties are not concerned with the State’s interest in applying its law to the dispute”. [MISTELIS p.426]

15 Following this reasoning, for instance, in ICC case No. 6294, the Arbitral Tribunal stated that it is “an uncontested principle of the prevailing opinion in legal writing that, contrary to the state courts, an international arbitrator is not bound to respect the choice of laws rule of the seat of the arbitration. A similar result is to be found in ICC cases No. 8113 and 11264.

16 Finally, it is well established that the arbitrator is empowered to choose the conflict of laws rule that reaches a neutral character in the arbitration in order to be impartial and independent from the national laws. Accordingly, given that resorting to a national law of either of the parties no doubt would be inequitable, as elaborated herein below, we propose the application by the arbitral tribunal of a de-nationalized conflict-of-laws rule.

1.1.3 THE APPLICABLE STATUTE OF LIMITATION SHOULD DERIVE FROM A DE-NATIONALIZED CONFLICT-OF-LAWS RULE

17 Due to the fact that the substantive law is silent on the matter at issue, it is submitted that, in ascertaining the applicable statute of limitation, a de-nationalized approach must be followed for it

supports the non-national character of the commercial relationship and gives a solution based on generally accepted principles of law.

18 Since a law governing a statute of limitations was not chosen by the parties, the conflict-of laws rule should be based on the uniformity, internationalization and freedom of arbitrators to choose laws that were expected to be reached with arbitration and at the moment of the designation of the substantive law.

19 An important element for the efficacy of international arbitration is that arbitrators are empowered to give effect to the proper law chosen by an appropriate conflict of laws rule. The fact that the parties in the problem at hand chose an international tribunal for the settlement of the dispute implies that they were looking forward to avoid the application of a national law.

20 International arbitration gives arbitrators authority to determine the applicable law that they consider appropriate, as was the case in the arbitration between a United States Seller and a Middle East Buyer, in which arbitrators decided that the most appropriate conflict of laws rule was that arising out of a de-nationalized solution. (ICC No. 7375)

21 As an example of the de-nationalized tendency we refer to a case from ILM court of Paris, between the government of Kuwait and Aminoil, in which taking into account supplementary agreements to the main contract, the Tribunal inferred the intent of the parties with regard to the transaction as a whole, and establishing Kuwait practice under similar contracts, concluded that the government of Kuwait and its associates were clearly invoking the general principles of law in stark contrast to the application of a national law.

22 In the same vein, the French Court of Appeal [Court of Appeal of Paris 20 December 1984] considered the award made in the case *Götaverken* v. *Libya* as a de-nationalized award: the procedure was solely governed by the Arbitration Rules of the ICC, (neutral legal rules) where the parties had not designated an applicable arbitration law, and the arbitrators have done so.

23 In certain legal systems or under certain rules the arbitrators are free to select the choice of laws rule in which in their opinion best satisfies the various imperatives of private international law

(such as predictability, realism and consistency with other choice of laws rule). [FOUCHARD p.474].

24 As the tendency is to pursue the de-nationalized conflict of law system in similar conflicts, the tribunal should apply this system to determine the law applicable to the period of limitations.

25 By way of example, the Commission on European Contract Law supports the fact that the commercial relationships should be governed by lex mercatoria and not by a national law, for that way it has been held that "nobody has the advantage of having the case pleaded and decided by his own law and nobody is handicapped by having it governed by a foreign law" [BERGER].

26 According to the test put forward by an authority to determine whether there was an implicit negative choice, it can be inferred that in the case at hand, by selecting CISG and CIDRA Rules, the parties were conscious that they were giving their contract and eventual dispute "an international character." [BLESSING p.42]

27 Likewise, there is strong support for the proposition that arbitrators are not obliged to choose from existing choice of laws rules, being even "perfectly entitled to invent new ones" [FOUCHARD p.875], which paves the way for the application of a de-nationalized conflict-of-laws- rule in the case at hand.

28 Both jurisprudence and doctrine had recognized that, in the last years, parties to arbitration look forward the detachment from the national laws i.e. (domicile of the parties, nationality, site of arbitration) related to the dispute submitted to arbitration. This late tendency has been named "de-nationalized" or "de-localized" [MANIRUZZAMAN p.383]. Arbitration leaves the door open to arbitrators to apply lex mercatoria and general principles.

29 Leading commentators such as Professor Goldman have advocated the development of some 'supranational' private international law rules, "such as would obviate the problem of resorting to the private international law rules of the seat of the tribunal, or the nationality of the arbitrators. This will mean avoiding the problem of determining which national law is more appropriate or more closely connected". [MANNIRUZZAMAN, GOLDMAN p.383]

30 One of the prime examples of transnational rules is the decision of the arbitral tribunal in the *Norsolor* case, where in the absence of an express choice of law by the parties, the arbitral tribunal, -despite the requirement in the applicable arbitration rules for it to apply a conflict-of-laws rule-, found that both Turkish and French laws were connected with the dispute, with no compelling reason to prefer either law to the other. The arbitral tribunal therefore decided not to choose any national law but instead generally accepted principles of law. [Norsolor v. Pabalk Award No. 3131 ICC]

1.1.4 UNIDROIT PRINCIPLES EMBODY THE MOST APPROPRIATE SYSTEM OF RULES ON WHICH THE APPLICABLE STATUTE OF LIMITATIONS MUST BE FOUND ACCORDING TO THE DE-NATIONALIZED CONFLICT OF LAWS RULE

31 As the substantive rule must derive from a de-nationalized rationale, there can be no doubt that the most appropriate body of rules that best fits the international character of the transaction and dispute is represented by the UNIDROIT Principles, which were developed on a broad comparative law basis and are common to some of the world's legal system. We found support for this proposition by referring to the development of the UNIDROIT Principles reflecting their international character, as well to the correspondence between the UNIDROIT Principles, and the provisions and general principles on which CISG is based.

32 To this end, we refer to the Compania Valenciana case (ICC Case No. 5953), where the arbitral tribunal decided to apply the lex mercatoria because the parties were not able to agree on the application an international legal system or their respective home countries which in the eyes of the sole arbitrator, was sufficient indication for the parties' intention to have a truly international law applied to their contract. In another well known investment dispute, -the Sapphire case-, the Swiss sole arbitrator relied essentially on the negative choice doctrine to de-nationalize the applicable law.

33 In addition, it has been said that UNIDROIT is the most visible expression of lex mercatoria which will reduce uncertainty in the awards [BONELL]. In this respect, ICC tribunals at 7110

award state that UNIDROIT Principles are legal principles drafted by experts from all legal systems for being applied to commercial relations. These principles are inspired in an international uniform law text, CISG. Finally, the arbitrators decided that since UNIDROIT Principles are, rather than ambiguous principles, “clearly enunciated and specific rules coherently organized in a systematic way” and reflect international trade usages, enjoy of a wide recognition all around the world.

34 According to Bonell, since the UNIDROIT Principles were not intended to become a binding instrument aimed at unifying national laws relating to international contracts, they were much less conditioned by the differences existing between the various legal systems. As a result, it was possible for them to address a number of matters which are either completely excluded or not sufficiently regulated by CISG. [BONELL]

35 When the arbitrators think of a non national standard, international law and lex mercatoria had been used, they refer to a set of rules developed to regulate international trade in the business community that have a persuasive character and that can apply to all types of commercial transactions. [FOUCHARD p. 734]

36 In support of our proposition, we rely on the seminal ruling handed down by the Court of Appeal of Grenoble on 23 October 1996, where the UNIDROIT Principles were applied as a means of supplementing CISG. The case concerned a sales contract between a German and a French company. In order to determine its own jurisdiction in conformity with Art. 5(1) of the 1968 Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters, the Court had to appoint the place of performance of the seller's obligation to return part of the price unduly paid by the buyer. CISG, which governed the commercial relationship, is silent on this matter. The Court, while openly rejecting the opposite solution adopted by both French and German domestic law, decided in favor of the buyer's place of business. In doing so, it based itself on the general principle that monetary obligations are to be performed at the obligee's place of business, which could be extracted not only from Art. 57(1) CISG, but also - and more convincingly - from Art. 6.1.6 of the UNIDROIT Principles.

1.1.5 <u>THE CONTROLLING PERIOD OF LIMITATION SHOULD BE OF 3 YEARS</u>

37 The UNIDROIT principles are largely inspired by international uniform law texts already enjoying wide international recognition and generally considered as reflecting international trade usages and practices in the field of international sale of goods.

38 Rather than vague principles or general guidelines UNIDROIT principles are mostly constituted by clearly enunciated and specific rules coherently organized in a systematic way. Chapter 10 on limitation periods addresses all the principal components of any limitation regime, the length of limitation periods, when they begin to run, whether and under which circumstances they may be suspended or begin to run afresh, and whether they may be shortened or extended by parties' agreement, and with respect to each of them provides solutions in conformity with the most innovative trends that have recently emerged in this field worldwide.

39 As exposed by Professor Bonell, "with respect to the length of the limitation periods, this chapter provides for a rather short *general* limitation period combined with a "maximum" cut-off period. Provides for a cut-off period of 10 years, the general limitation period is 3 years in this chapter due to the fact that a 3-year period has only recently become prevalent at domestic level". [BONELL / UNIDROIT Principles 2004]

40 The general limitation period begins to run when the claim accrues, with respect to claims for breach of contract on the date on which the breach occurs, and with respect to claims for non-conformity of the goods on the date of delivery, the latter basically makes the commencement of the general limitation period dependent on the obligee's actual or constructive knowledge of its claim.

41 "The expiration of the limitation period does not extinguish the right to have effect and therefore, the obligor must assert it as a defense, this chapter expressly rejects not only the procedural approach, traditionally adopted in common law systems, according to which the consequence of the obligee's inactivity over a certain period of time is that the obligee is prevented from pursuing its right in court, but also the *strong* substantive approach, peculiar to some civil law systems, whereby the effect of the lapse of time is the extinction of the obligee's right, and opts for the *weak* substantive approach, presently prevailing at international level,

according to which the obligor only has the right to refuse performance". [BONELL/Unidroit Principles 2004

42 Therefore the applicable statute of limitation is article 10.2 of the UNIDROIT Principles, which states that in the issue of limitation periods:

(1) The general limitation period is three years beginning on the day after the day the obligee knows or ought to know the facts as a result of which the obligee's right can be exercised.

(2) In any event, the maximum limitation period is ten years beginning on the day after the day the right can be exercised.

1.2 McHINERY EQUIPMENT´S PROPOSED SOLUTION IS NOT ADMISSIBLE ON GROUNDS OF INOBSERVANCE TO PARTY AUTONOMY WHILE BEING OUT OF STEP WITH GENERALLY ACCEPTED JUDICIAL AND ARBITRAL PRACTICE

43 Respondent submits the applicable law to the issue in dispute is that of Mediterraneo, which contains a period of limitation of two years. Accordingly, based on article 32 of CIDRA Rules, it states that "failing such designation by the parties, the arbitral tribunal shall apply the law determined by the conflict of laws rule which it considers applicable".

44 In this regard, while it is true that according to Mediterraneo's law, the performance characteristic of a sale of goods contract is that of the seller, it is also undisputed that pursuant to Oceania's law, along with other national laws and conventions, there exists an exception to the effect that the contract is governed by the law of the state where the buyer has his place of business at the time of the conclusion of the contract, if it provides expressly that the seller must perform his obligation to deliver the goods in that State, as was the case here.

45 Moreover, as submitted above, it would not be fair to any of the parties, to choose a national law over the other, for their unambiguous intention was expressed in the sense of selecting a neutral or non-national body of norms.

46 On the other hand, McHinery Equipment argues that due to the fact that there was not a choice of law to govern other legal issues than those governed by CISG, the normal rule was to apply the law of the party whose role was characteristic to the contract. We counter this by

asserting that should Respondent's solution were to be followed, the international character of the arbitration would be injured.

47 Having demonstrated that the most appropriate law rule governing the prevailing statute of limitation must derive from a de-nationalized basis, and that same is to be found in article 10.2 of the UNIDROIT principles which provides for a 3 years period of limitation, the arbitral tribunal must accordingly proceed to render an award on the merits of this case.

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2. McHINERY EQUIPMENT SUPPLIERS HAS COMMITTED FUNDAMENTAL BREACH OF CONTRACT DUE TO NON-CONFORMITY OF THE MAGIPRINT FLEXOMETIX MACHINE

48 In this part of the memorandum, it will be shown that the machine delivered to our client is not in conformity with the terms of the contract since it does not fit for the particular purpose made known to the seller. Based on our client's total confidence in seller's skill and judgment, seller should be found liable for this lack of conformity, since this is why our client was not aware and could not have been aware of this lack of conformity at the time of the conclusion of the contract, resulting this in a breach of contract.

49 Thereafter, it will be demonstrated that the breach should be considered as fundamental for the reason that our client was deprived of what he was entitled to expect under the contract, resulting in a substantial detriment which was foreseeable by the seller at the time of the conclusion of the contract.

2.1 THE MACHINE DELIVERED BY MCHINERY EQUIPMENT IS A NON-CONFORMING GOOD, WHICH AMOUNTS TO A BREACH OF THE CONTRACT

50 On 17 April 2002, in a letter addressed to Mr. Norman McHinery, president of McHinery Equipment Suppliers Pty (hereinafter McHinery Equipment), Mr. Roland Butter president of Oceania Printers enquired into the purchase of a machine "capable of printing coated and uncoated papers for wrapping, polyester and also metallic foils" [Claimant's Exhibit No.1]. In the same letter our client, Oceania Printers S.A. stated that the metallic foils will be used in the

confectionary market and that "typical plain and colored aluminum foil for chocolate wrappers may be of 8 micrometer thickness". Our client also stated that with that machine his company would succeed to "develop a commanding lead" in his country [C.E. No.1]. Mr. McHinery answered that the appropriate machine for the task would be the "7 Stand Magiprint Flexometix Mark 8" [C.E. No.2]. On 10 May 2002, Mr. Butter emphasized how crucial for his company was that the machine were to be promptly delivered due to the immediacy [15 July 2002] with which a separate contract with a third party, namely, Oceania Confectionaries, was to be serviced with a projected profit of USD$400,000 a year, for a period of 4 years, subject to renewal at the end of that period [C.E. No. 3]

51 As it turned out, the machine handed over to our client was not fit for printing aluminum foils of 8 micrometers' thickness, which is at odds with our client's express intention, as evidenced by the correspondence between the parties [C.E. No.1 & 3]. The machine delivered was capable of performing three different functions: *"printing coated and uncoated papers for wrapping, polyester and also metallic foils for use in the confectionery market"* [C.E No.1]. More importantly, our client in more than two occasions insisted on the importance of the third function of the machine. As a matter of fact, in C.E. No. 1, Mr. Butter not only made reference to the machine's aluminum foil specification for the purposes of the confectionery market, but also expressed that there was a need in the market of his country for metallic foils of 8 micrometers and with this machine they would be able to fulfill this need, enabling them to develop a commanding lead. At this point, it is to be noted that the development of a commanding lead in the market should be considered by the Tribunal as a prime expectation of our client under the contract. [Supreme Court of Austria (*Oberster Gerichtshof*) 6 February 1996 [10 Ob 518/95]

Further, our client also conveyed to seller that even if "*there are other uses for the machine, of course, the market in Oceania is very small and it is only the Oceania Confectioneries account that makes the flexoprint machine worthwhile"* [C.E. No.3].

52 In the same vein, according to P.O. No.2, the machine's potential profits for 2002 could not have been higher than $10,000 per year, a significantly small amount compared to the $400,000 per year to be rendered from the Oceania Confectionery's contract. If this were the case, it would be more expensive to acquire the machine than the profit obtained for its use. Moreover, even if it is true that a machine capable of printing in no less than 10 micrometers only, could render a

profit of $300,000 for the Oceania Generics' [P.O. No.2, point 20] possible contract, it would be unsound to assume that our client's purpose was to purchase a machine five years before the existence of the possible contract. From this context, it is to be inferred that service of the Confectionery's contract was also an important expectation for our client under the contract.

53 Based on the foregoing, it is incontestable that under article 35 of CISG, McHinery Equipments committed a breach of the contract due to the non-conformity of the machine to the purpose for which it was contracted for, which led to the contract's frustration causing detriment to our client.

2.1.1 THE MAGIPRINT FLEXOMETIX MACHINE WAS NOT FIT FOR THE PURPOSE MADE KNOWN TO THE SELLER UNDER THE CONTRACT

54 As a result of the negotiation history between McHinery Equipments and our client for the sale of the printing machine, a contract was finally executed. Therein, respondent agreed to sell the machine and our client to pay the specified amount for the specified machine [C.E. No.7]. For its part, article 35(1) of the CISG establishes that "the seller must deliver goods which are of the quantity, quality and description required by the contract". If the good delivered does not fulfill these elements, there is a non-conformity under the contract. [Court of Appeal Köln (Oberlandesgericht) 21 May 1996 [22 U 4/96]]

55 By acknowledging that the contract itself does not include any specification as to the machine in question, [P.O. No. 2 at point 9], the intent of the parties becomes decisive to interpret the meaning of the contract [ZIEGEL] and to ascertain the content of their obligations [SCHLECHTRIEM, p. 6-19, BIANCA, p. 272]. According to paragraph 3 of article 8 of CISG, consideration is to be given to all relevant circumstances of the case including the pre-contractual negotiations [EÖRSI, p. 2-16; HONNOLD/Legislative History p.120]. In short, the correspondence between the parties unambiguously evidenced our client's intent for the machine to be capable of printing on aluminum foils of 8 micrometers thickness.

56 The first paragraph of the above-mentioned provision establishes that *"statements made by, and other conduct of a party are to be interpreted according to his intent where the other party knew or could not have been unaware what that intent was"*. Thus, after our client, through the

correspondence, informed the seller about his intent in regard to the machine's capabilities, the seller knew or could not have been unaware what this intent was. The seller's awareness of our intent is to be found expressly in C.E. No.2 where respondent assured our client that he had a machine for "his task", and later on guaranteed our client that with this machine he would be able to meet all his "customers' needs" [C.E. No.6]. It ensues that the seller was totally aware of our client's intent because he could not have possibly ensured Claimant that the machine in question was the one which could have been fit for performing our client's task, if he did not know actually what the task was.

57 On the other hand, Respondent might submit that an exception for the inclusion of negotiations in the interpretation of the contract, applies in this case. However, as explained by professor van Houtte "when parties want to ensure that the negotiation history may not lead to implied contract terms, they may accept a 'four corner clause', indicating that the written contract completely embodies the terms on which the parties have agreed and that this contract cannot be supplemented by prior statements" [VAN HOUTTE, p. 379]. Thus, given the non-existence of a so-called four corner clause in the contract between McHinery Equipment and our client, no exception applies, and therefore, the negotiation history must necessarily be taken into account to determine implied contract terms representing the parties' intent.

58 In the alternative, to the extent that the arbitral tribunal considers that the first paragraph of article 8 is not applicable, pursuant to the second paragraph, our client's statements are to be interpreted according to the understanding that a reasonable person of the same kind as the other party would have had in the same circumstances. In the case at hand, a reasonable person of the same kind of McHinery Equipment would have been someone with the same technical background and expertise in the printing machines' market, and with comparable knowledge of our client's intent through the prior negotiations [FARNSWORTH, p. 98]

59 Thus, this reasonable person in the same circumstances would have understood the importance of our client's expectations, which was to receive a machine capable of printing, if not on all kind of aluminum foils, at least on the minimum thickness mentioned (i.e. 8 micrometers) since our client clearly established through the correspondence that this was his intent. This is another fact that proves that the seller could not have been unaware of the buyer's intent.

[Supreme Court of Austria (Oberster Gerichtshof) 6 February 1996 [10 Ob 518/95]; Landgericht Ellwangen, 21.08.1995, Germany, [1 KfH O 32/95]

60 Finally, for the reason that due consideration is to be given to all relevant circumstances of the case, the subsequent conduct of the parties should be used in determining their intent [SCHLECHTRIEM, ART. 8, p. 39]. After the machine delivered was not capable of printing on 8 micrometer aluminum foils, our client asked the McHinery Equipment's technicians to adapt the machine to this particular thickness, revealing with this subsequent conduct our client's intent yet again. This means that Oceania Printers had not asked for the reparation of the machine when he realized that was not capable of printing on 8 micrometer foils, it would have been clear that this was not his purpose or at least not the main one, at the time of purchase of the machine.

For all the previously exposed circumstances, it is clear what the intent was and that this intent was part of the contractual elements. This is why under article 35 (1), the seller did not comply with his obligation to deliver goods which were of the quality required by the contract. [Fujian Higher People's Court [December 1994].

61 On the facts of this case, the seller not only delivered a non-conforming machine pursuant to the wording of article 35(1) of CISG, but also failed to deliver a conforming good pursuant to the same provision's paragraph (2) (b).

62 In light of article 8 of CISG, it is already clear what the intent of our client was. This particular purpose must be made known to the seller expressly or impliedly. Since the contract does not contain an express statement of the purpose, this must be found in previous correspondence, where we can find that our client impliedly informed it to the seller through the correspondence.

63 According to the Secretariat Commentary of CISG, when the buyer cannot give an exact specification about the good concerned, he may describe the goods desired by describing the particular use to which the goods are to be put [Secretariat Commentary. Art. 35]. Given that at the time of the request of the machine the contract with Oceania Confectioneries had not yet been signed, our client could not be sure about the specific thickness on which the machine would need to print on. This is why in C.E. No 1, our client explained which thickness could be the minimum required for the Confectionery Market as he was already expecting to obtain the contract with Confectioneries Company.

Stating this minimum range for the printing machine and explaining his intention to get the Oceania Confectioneries contract, Mr. Butter exposed to the seller his particular purpose for the specified good.

64 The Magiprint Flexometix received by our client, could not print on 8 micrometer foils because the minimum printing range of the machine was 10 micrometers. As indisputably established in the record, when Oceania Printers' employees tried to use the machine with 8 micrometer foils "it creased the foil and tore it, and multiple color runs were badly out of register" [C.E. No.9]. The machine was in perfect conditions for the use in 10 micrometer foils but the problem is that our client's expectation was to print on 8 micrometers and the seller did not send a machine suitable for this task.

65 Consequently, it is submitted that the good is non-conforming not because it was incapable of working properly but because it was not appropriate for performing our client's task. [Germany Landgericht Heilbronn, 15 09 1997 Case No. 3 KFH O 653/93; Oberlandesgericht Köln, 14.10.2002, Germany, No. 16 U 77/01]. This means that the delivery of a commodity of a different kind as the one contracted for, should be considered as a wrong delivery and therefore treated as a non conformity of the good [SCHLECHTRIEM, p. 6-20; OGH 1 Ob 74/99k (Austria 1999)]. According to this there is a defective performance of the seller and this should be considered as a breach of the contract no matter the relevance of the non conformity [BIANCA p.270].

2.1.2 THE BUYER COULD NOT HAVE BEEN AWARE OF THIS LACK OF CONFORMITY GIVEN HIS ABSOLUTE RELIANCE ON THE SELLER'S EXPERTISE AND BACKGROUND

66 The non-conformity of the Flexoprinter machine has been proven on the preceding paragraphs. However, it may be argued that under the CISG there is a possible exception when seller is not responsible for the lack of conformity of the good and therefore the non-conformity becomes irrelevant for the buyer's claims. Third paragraph of article 35 states that "the seller is not liable under subparagraphs (a) to (d) of the preceding paragraph for any lack of conformity of the goods if at the time of the conclusion of the contract the buyer knew or could not have been unaware of such lack of conformity". According to this article if our client was aware of the lack of

conformity of the printing machine when he signed the contract then respondent is not liable for this non conformity.

67 Nevertheless, in the case at issue, this exception for the non-conformity does not apply given that there are many factors proving the respondent's liability under this paragraph of article 35. These elements to be noted are that, at the time of the conclusion of the contract [C.E. No.7] our client did not know this non-conformity and did not become aware until he tried to print on 8 micrometer thickness aluminum foils and the machine was not able to perform this task. In the Audiencia Provincial de Barcelona case, 28 April 2004, the seller was an expertise in the field and was able to inspect the goods by seeing a sample before the purchase, for this reason the court found that he could not have been unaware of the lack of conformity. In our case the buyer was not able to inspect the machine because it was not functioning and the buyer was not an expert in the matter, therefore he could not foresee the lack of conformity. [Audiencia Provincial de Barcelona, 28 April 2004, Rollo No. 862/2003-B]

68 A further element is that after he let respondent know of his particular purpose for the purchase of the printer, our client totally relied on the seller's skill and judgment in order to have a machine fit for such purpose.

In addition to this, seller must be found responsible for this lack of conformity because he did not clearly provide to our client the adequate information about the product of his sale. All these factors will be now exposed in the light of the facts one at a time. This is supported by the ICC case no. 8782, 1997, where seller was found liable for the delivery of a non confirming machine, not capable of performing the tasks required by the buyer, since "the seller knew, as a concept, exactly what the claimant wanted. The seller, with its technical background and expertise, was in a better position to judge if this concept could be successful than the buyer." For this reason he was found responsible for the lack of conformity. [ICC No.8782, 1997]

69 From the wording of article 35 of CISG it is clear that if the buyer knows that the good is non conforming at the moment of the conclusion of the contract, the seller is not liable for the non conformity. This applies when the buyer obtains goods knowing of the lack of conformity of the product and when he receives them he rejects them for the non-conformity [BIANCA, p.277, Secretariat Commentary, art. 35]. In the present case it is clear that our client did not know at the time of the conclusion of the contract, 27 May 2002 [C.E. No.6] that the Magiprint Flexometix

machine was not capable of printing on 8 micrometer aluminum foils since in the letter of the 1st July, more than one month later, our client stated "we plan on starting production printing next week" [C.E. No. 8]. With this, it becomes totally clear that if our client one month after the conclusion of the contract was still expecting to start the production, obviously the one for the Oceania Confectioneries' contract, it is for the only reason that he was still not aware that the machine he had just obtained was not fit for his particular purpose. This proves that the buyer did not know of this non conformity at the time of the conclusion of the contract.

70 Article 35(3) of CISG establishes two situations about the buyer's knowledge of the non conformity, either he knew about it, either he could not have been unaware of it. We already know that our client did not know about the lack of conformity at the date of the conclusion of the contract, but in the light of the facts it will be verified that he neither knew nor he could have been aware of this non conformity. Leading commentators explain that the use of the wording "could not have been unaware" in the article of CISG does not impose a duty to make a deep investigation but it makes reference to facts that are before the eyes of the one who is making the inspection as well, the one who makes the inspection is not obliged to ask for technical expertise for the inspection [HONNOLD/Legislative History p. 259, BIANCA p. 278].

71 This is why our client was not compelled to make a deep investigation about the specific qualities of the machine when he went to Greece to inspect it, he did not need to be companioned by an expert who acted as a consultant. Furthermore, according to Procedural Order No. 2 Mr. Butter did not see the machine working during the visit to the plant of the previous owner of the machine because it was not in use any more, he could not observe any actual printing of the machine. In the Swiss Federal Supreme Court Case 4C.296/2000/rnd, 2000, the court held that the seller was not liable for the non conformity of the contract because the buyer could have been aware of the lack of conformity, since he examine the good before the purchase; *contrario sensu* to this criteria, in our case it must be found that the seller is liable for the non conformity of the machine since the buyer was not able to witness the actual performance of the machine as to find any inconformity.[Swiss Federal Supreme Court (*Schweizerisches Bundesgericht*) 22 December 2000 [4C.296/2000/rnd]

72 Because of these two situations, it is patent that the inspection of the machine by Mr. Butter was solely aimed at verifying the visible physical condition of the machine, but he could not have been possibly aware by the mere eye-inspection, of the machine's lack of conformity for his particular purpose.

73 In order to determine the conformity of the good relevance is given within article 35 of CISG to the confidence on the seller. If the buyer did not rely or it was unreasonable for him to rely on the seller's skill and judgment when he informed his particular purpose, he cannot claim a lack of conformity of the good requested. This could happen when the buyer selected the goods giving the specific name or brand or when he gave complex specifications about the good wanted [BIANCA, p. 275; Secretariat Commentary, art. 35]. It is worthy noted that our client totally relied on the seller's skill since he only gave to the seller details about his intent and it was the seller who chose the appropriate machine according to him. Hence, if the seller is the one who selected the machine it is because he knew that with this machine our client could fulfill all his needs or it was reasonable that our client believed that. If the seller was not sure about the intent of the buyer or the suitable machine for the task, he should neither have selected a machine nor insisted that it was ideal for our client's task. In addition to this, it would be normal to assume that a seller knows the specifications of the product he is selling and what are these products for.

74 Finally, the seller cannot claim that the buyer could not have been unaware of this lack of conformity since seller did not comply with his duty to inform about the specification of the machine not suitable for printing on 8 micrometer thickness aluminum foils. A general principle of the Convention is the duty to disclose any information significant to the other party for the transaction [HONNOLD, p. 106; FELEMEGAS, Art. 7]. The non-disclosure of the relevant information during the negotiations which affects the contract elements results on the liability of the party withholding the information [NASSAR, p. 148; KESSLER/FINE, p. 404-405] this is why the seller is responsible for not informing the buyer about the minimum printing range of the machine.

75 Respondent may contend that he complied with his duty to disclose all the relevant information about the machine by sending the operating manual to our client enclosed with the contract [C.E. No. 6]. Even if it is true that the specification of the printing range of the machine was in the

manual, it should be found that the seller conduct is misleading, to say the least, given that from the wording of his letter he implied that our client did not need to read the manual because “the machine is easy to operate and is a very reliable machine”, giving by granted that the use of the manual was only necessary for the operation of the machine or to solve a problem with it and clearly not as to verify for specific requirements of the machine. Additionally, he took advantage of the urgency of our client to get a machine to perform the contract [China December 1994 Fujian Higher People's Court (San Ming v. Zhanzhou Metallic Minerals)] with Oceania Confectioneries assuming our client would not have time to read the manual and that, had our client read same, he would not be interested in the machine any more. When situations like these arise, a principle should be applied to hold that a negligent buyer deserves more protection than a negligent seller [FERRARI, p. 90]. Therefore even if the buyer failed to read the manual and this could be found to be an excess of confidence on his part, seller is still responsible for his negligent conduct.

76 For the situations previous mentioned, the exception of the lack of conformity does not apply in this case since our client was not aware and could not have been aware of this circumstance and clearly respondent should be found responsible for his misleading conduct. For all these elements the non conformity results in a breach of contract.

77 Finally, the non conformity of the good could disappear along with the breach of the contract by the repair of the delivered machine within a reasonable time as stated in article 46 of CISG. In C.E. No.10 it is settled that McHinery Equipment technicians were not able to adapt the machine for printing in 8 micrometers. For the failure to repair this non conformity the breach of the contract subsists. In the case of Marques Roque Joachim v. La Sarl Holding Manin Riviere (26 April.1995) the Court of Appeal of the Commercial Chamber of Grenoble, decided in favor of the defendant (seller) in view of the fact that he was able to remedy the lack of conformity.

2.2 THE NON-CONFORMITY OF THE GOOD RESULTS IN A FUNDAMENTAL BREACH PURSUANT TO ART. 25 OF CISG, FOR OCEANIA PRINTERS WAS DEPRIVED OF WHAT IT WAS ENTITLED TO EXPECT UNDER THE CONTRACT.

78 As above mentioned, the non-conformity of the machine constitutes a breach of contract itself since the good was not conforming under the terms of the contract and was not fit for the particular purpose made known to the seller found in previous correspondence. In this section it will be demonstrated that this breach should be considered as a fundamental one. In Gorpischecombinat "Livensky" v. SECOMITA di Pier Georgio Pavan case it was decided that as a result of the non conformity of the good a breach was committed, but this can not be considered as substantially deprive him of what he was entitled to expect under the contract, that is why it does not amounts to a fundamental breach. In our case it must be determined that as a result of the breach from the non conformity our client was substantially deprived of what he was entitled to expect under the contract, amounting to a fundamental breach. [Gorpischecombinat "Livensky" v. SECOMITA di Pier Georgio Pavan Arbitration Court of the City of Moscow In the name of the Russian Federation February 28, 2000 Case # A 40-39073/99-40-395]

79 The concept of fundamental breach under the CISG is recognized in the article 25 of the Convention. From the wording of this article, three elements must be met in order to declare a fundamental breach of the contract. It could seem obvious to mention it, but as a matter of fact it is essential to make clear that, the first element that must exist to claim a fundamental breach is the breach of the contract itself.

80 The second element for the fundamental breach is that our client was substantially deprived of what he was entitled to expect under the contract, namely, to receive a machine capable of printing at least on 8 micrometer metallic foil [Cour d'Appel de Paris, France 04.06.2004, Case No 2002/18702] in order to fulfill his own obligations *vis à vis* a third party. At last, this substantial detriment was foreseeable by the seller as well as by a reasonable person in the same circumstances.

2.2.1 <u>THE BREACH OF THE CONTRACT CAUSED A SUBSTANTIAL DETRIMENT TO OUR CLIENT</u>

81 It is clear that to declare a fundamental breach the first element that must be present is a breach of contract. In the first part of this memorandum it has already been submitted that the intent of our client has been frustrated for the non conformity of the machine. According to Professor Bianca, the non-conformity of a good under article 35 of the Convention establishes a

unique notion of breach of contract [BIANCA, p. 269]. To this extent the mere existence of the non-conformity of the good results in a breach of contract. We have now the first element necessary to claim the existence of a fundamental breach. It will be at this time attested that this breach should be considered as fundamental in the light of article 25 of the CISG. [Cerámica Tudelana, S.A. v. Wassmer Gruppe Spezial Machinen GM*BH.* Court of First Instance Juzgado de Primera Instancia e Instrucción No. 3 de Tudela 29 March 2005]

82 The just mentioned article of CISG states that *"a breach of contract committed by one of the parties 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".* To prove the substantial detriment suffered by our client, it must be first exposed what our client was entitled to expect under the contract. According to C.E. No. 3 it was clear that the particular purpose of our client in purchasing the machine was to fulfill with the Oceania Confectionery's contract, for which the main requirement was to print on 8 micrometer aluminum foils. It is worth noting that a breach is fundamental when the buyer has repeatedly asked for goods that will be used for a particular purpose or where he has informed the seller the particular needs and uses for the purchase and the goods received have defects making impossible this particular use [KOCH, p. 218, LOOKOFSKY EU §6-8]. Since this purpose was frustrated our client was clearly deprived of what he was expecting under the contract.

83 Furthermore, there is a fundamental breach if the injured party is no longer interested in the performance of the contract after the particular breach [SCHLECHTRIEM, p. 59; LIU 2.2]. Our clients solely interest on acquiring the machine was to be able to fulfill on time his contract with Oceania Confectioneries [C.E. No.1], when this contract was cancelled he informed the seller that this "leaves us with almost no business for that machine you sold us. The machine is useless to us". This proves that our client was not interested in the machine after he was deprived of what he was expecting reaffirming the existence of the fundamental breach.

84 The breach committed may be assessed as fundamental not only under the nature of the contractual obligations, but under the gravity of the consequences of the breach as implied by Koch [KOCH, p.218]. Canton Court (*Kantonsgericht*) Schaffhausen Switzerland 27 January 2004 [No. 11/1999/99]

85 The determination of the gravity of the consequences shall be measured in the light of the circumstances of each case and taking into consideration first, the monetary value of the contract and the monetary harm caused by the breach second, how the breach affects the commercial activities of the injured party and third, the remedy oriented approach.[KOCH, pp. 221,262]
In the present case the loss of the monetary value of the contract must be found in the loss produced by the payment of a machine that resulted not functional and at the end was totally useless to our client. [C.E. No.10].The loss of profits consists in the loss of the earnings that the machine would have produced by the contract with Oceania Confectionery [C.E. No.3] if the good acquired had complied with the expectations of the buyer. It is worthy to note that even if the determination of the detriment suffered by the aggrieved party does not depend on the actual monetary amount of the loss [SCHLECHTRIEM, p.59] because it would become impossible to establish what would be the minimum amount necessary to declare a fundamental breach [KOCH, p.266], our client is suffering in this case a really important loss of profits for an amount of $3,000,000.

86 Concerning the commercial activities, followed from the cancellation of the Oceania Confectionery's contract, our client was hindered in continuing the commercial activity and obtaining a commanding lead in the market of his country. As a consequence of this it is clear that our client's commercial reputation in his country was seriously damaged since he failed to fulfill a very important contractual obligation. Furthermore, since the market in Oceania is really small for this kind of machines [C.E. No.3], our client's failure to comply with his obligations could affect his commercial reputation in a larger amount.

87 In the last element consideration is to be given to the possibility of the seller to cure its breach. After the delivery of the machine, our client performed his obligation of examining the goods and give notice to the seller specifying the nature of the lack of conformity within a reasonable time after he has discovered it, in accordance with articles 38(1) and 39(1) of the Convention. Due to the lack of time it was not possible for Mr. Butter to purchase another machine or request substitute delivery of goods pursuant to Article 46(2) to service the Oceania Confectionery's contract. [P.O No.2]. For the impossibility of the seller to cure the breach by sending substitute goods this breach subsists.

88 The existence of these three elements named by Koch to establish a fundamental breach led to a detriment as to substantially deprive our client of what he was entitled to expect under the contract making clear that the arbitral tribunal should find that McHinery Equipment committed a fundamental breach of the contract.

2.2.2 THE IMPACT OF THE CONTRACT'S FUNDAMENTAL BREACH WAS FORESEEABLE TO MCHINERY EQUIPMENT

89 The second part of article 25 of CISG determines an exception for the seller's liability of the fundamental breach when it was not foreseeable for him and for a reasonable person in the same circumstances the detriment caused to the aggrieved party. This leads to a subjective test as this forseeability has to be determined through the eyes of the seller and objective because any reasonable person could have foreseen it.

90 Our client through the correspondence in several occasions informed the seller his purpose to accomplish with another contract and the importance of the specifications needed for the machine to accomplish this contract [C.E. No.3]. At the time of the conclusion of the contract seller should have been aware that the machine delivered did not comply with our needs since what we needed was a machine capable of printing in 8 micrometer thickness aluminum foil and the machine was not designed to print in this thickness [C.E. No 9]. Seller was aware of the substantial detriment resultant from the fundamental breach [ICC No.8782, 1997]

91 In the light of CISG, a reasonable person is "one in the same situation as the non performing party and using reasonable skill and diligence would have known or foreseen the consequences at the time of the conclusion of the contract" [LIU, 2.1] In the present case any reasonable person with the same skill and knowledge in the branch of the selling machine market as Respondent, should be able to sell a machine with the specifications asked by the buyer. In this sense, any reasonable person would have foreseen that the machine sent was not capable of printing on 8 micrometer aluminum foils. Also this reasonable person after our client not only made reference to the third contract [C.E. No.3] and the need of printing on 8 micrometers to fulfill it, but also warned that if the machine was not repaired on time to fulfill his obligations he would hold the seller liable for losses and damages [C.E. No.9], would have been aware or could not have been

unaware at the time of the conclusion of the contract, that the delivery of the non conforming machine would result in the cancellation of this contract, causing a substantial detriment and economic injury to our client.

92 After showing the existence of the breach, that this breach substantially deprived our client of what he was entitled to expect under the contract, and that this substantial detriment was foreseeable for the seller and any reasonable person in the same circumstances the breach of contract amounts to a fundamental one.[Delchi Carrier S.p.A. v. Rotorex Corp. U.S. Court of Appeals (2nd Circuit) 6 December 1995

93 When a fundamental breach is declared, seller has the right to cure the defect by using some remedies available for this pursuant to article 48 of CISG. In this case by the sending of substitute goods within a reasonable period of time, the seller could have mended the fundamental breach. Due to the lack of time it was not possible to send the substitute goods. For this situation, the buyer was entitled to sell the machine if the fundamental breach was not possible to be cured because not other remedy was available and he had already fulfilled his part of the contract: to pay the price of the machine to the seller.

94 Finally, even if the existence of a fundamental breach gives our client the right to avoid the contract according to article 49(1) (a) of CISG, it was not necessary to do so given that there are no further obligations to be performed by our client as he had already paid for the non conforming machine. For this reason he was entitled to sell the machine since it was already of his property. To stress this if the seller tried to re-purchase it for $20,000 it is confirmed that the machine was already our client's [Respondent Exhibit No.2].

3. AS A CONSEQUENCE OF THE BREACH COMMITED BY McHINERY EQUIPMENT, OCEANIA PRINTERS HAS THE RIGHT TO CLAIM DAMAGES IN THE AMOUNT OF USD$2,495.000, IN ACCORDANCE WITH ARTICLES 45 AND 74 OF CISG

3.1 OCEANIA PRINTERS IS ENTITLED TO CLAIM DAMAGES AS PROVIDED IN ARTICLE 45 OF CISG.

95 As demonstrated above, McHinery Equipment breached the contract it had entered into with Oceania Printers, as a consequence of that breach, Claimant is to be considered as the injured party, and Respondent as the breaching party; therefore, the Tribunal must consider Claimant entitled to seek damages under article 45 of CISG.

96 It is noteworthy that damages is not the only remedy the buyer could exercise, once a breach on the part of the seller had occurred, CISG provides three basic remedies, namely: specific performance, damages and avoidance of the contract. [LIU]. Further, there is no hierarchy among the various remedies since article 45 of CISG leaves the buyer the choice of the most suitable recourse to its particular case [HONNOLD p.276] without implying that the affected party can not claim damages when it had exercised another remedy. Therefore, the right to claim damages must be considered as an accumulative or alternative remedy. [PERALES p.170].

97 Hence, it could not be said that Oceania Printers is prevented from claiming damages for having previously exercised its right to claim specific performance by means of requesting from McHinery Equipment to fix the Magiprint Flexometix, as provided in article 45 (a) of CISG. [CIETAC, Printing Machine case, 6 April 1994].

98 For its part, article 45 of CISG states that "…the buyer may: (a) exercise the rights provided in article 46 to 52…". In conjunction, article 46 of CISG states that: "…(3) If the goods do not conform to the contract, the buyer may require the seller to remedy the lack of conformity by repair, unless this is unreasonable having regard to all circumstances. A request for repair must be made either in conjunction with notice given under article 39 or within a reasonable time thereafter".

99 The two requirements needed in order to exercise the right afforded by article 46 of CISG were satisfied by Oceania Printers. First, by giving notice to the seller of his lack of conformity and requesting same to repair the good in order for the latter to be suited to work on the foil products for confectionary wrapping [C. E. No. 9]. Second, by giving said notice to McHinery

Equipment in a reasonable time after discovering the lack of conformity, as evidenced in C.E. No.8, where Oceania Printers stated on 1 July 2002, that the machine was "working properly", and thereafter, Oceania Printers communicated his lack of conformity to the seller by means of a letter of 1st August 2002. [C. E. No. 9]. In the Used Shoes case 2260264/04, the court decided that buyer was precluded from relying on a lack of conformity since he did not examine the goods soon enough and also did not give notice of the non-conformity of the goods within a reasonable period of time.

100 Nonetheless, as our client's expectations could not be fully satisfied by exercising article 46 of CISG alone, it decided to avail itself of his right to claim damages under art. 45 of CISG.

In this vein, article 45 of CISG states that: "If the seller fails to perform any of his obligations under the contract or the Convention, the buyer may… (b) claim damages as provided in article 74 and 77". According to CISG, "an obligation to pay damages arises directly from any objective breach of contract, regardless of fault by the part in breach" [SCHLECHTRIEM p.31] .

It is worth nothing that our client could not declare the contract avoided, as has been settled in the present memorandum. This statement is supported by Roger v. Reynolds case, 2003/AR/2026 10 May 2004, in which the court concluded that the contract could not be declared avoided, since the obligations between the parties were completely fulfill.

In sum, this Arbitral Tribunal must find that Oceania Printers has the right to claim damages as a result of McHinery Equipment's breach of contract.

3.2 OCEANIA PRINTERS IS ENTITLED TO CLAIM DAMAGES IN THE OVERALL AMOUNT OF USD$2,495.000, PURSUANT TO ARTICLE 74 OF CISG.

101 Once this Arbitral Tribunal has determined that Oceania Printers is entitled to claim damages from McHinery Equipment, it is submitted that article 74 of CISG comes into play for the purpose of making the proper calculation of the actual damages. Thus, article 74 of CISG establishes that: "Damages for breach of contract by one party consist of a sum equal to the loss, including loss of profit, suffered by the other party as a consequence of that breach[…]".

102 The purpose of article 74 of CISG is to give a formula to the injured party in order to estimate the damages for breach of contract, which is designed to compensate the loss suffered by him as a consequence of that breach. Hence, the right to claim damages is simply a direct deduction from the principle of *pacta sunt servanda*, since its main effect is to substitute a pecuniary

obligation for the non-performance of the party in breach. In other words, the main purpose of article 74 of CISG is to place the injured party in the position it would have enjoyed if the contract had been performed. [NANDA and RALPH TBT].

103 The rule by which the damages must be measured is: first, by determining what doctrine establishes as direct and indirect loss; and second, by calculating the loss of profit to be included by way of damages, as set out by article 74 of CISG.

104 As a direct loss, our client claims the contract that Oceania Confectionaries cancelled, in which Oceania Printers would have obtained net gains over a period of four years. As put by a leading commentator direct loss must be understood as “all the costs which could bring him into the position he would be in if the contract had been performed”. [ZELLER. p 122].

105 On the other hand, as indirect loss must be understood all of the expenses that does not arise as a necessary and strict consequence of the unlawful act of the party in breach but causes an economical consequence for the injured party; there is no causal relationship, a characteristic which then becomes determinative when classifying a loss as direct, between the breach and the economical loss suffered by the injured party. [ICC case No.10346]

Oceania Printers claims, as an indirect loss, the cost invested for adapting its plant to the installation of the Magiprint Flexometix and, the amount spent by the personnel of McHinery Equipment in testing it.

106 Considering that McHinery Equipment has acceded to pay the monies corresponding to what our client claims by means of indirect lost as well as the resale of flexoprint machine, the present memorandum will only focus on the right that Oceania Printers has to claim the amount of USD$1,600,000 stemming from the cancellation of the contract with McHinery Equipment and its possible renewal.

107 Finally, by loss of profit must be understood the difference in value of the assets before and after the breach. Meaning that, if the contract had been properly performed and the breach had not been committed, the injured party would have enjoyed an increase in his assets, and these must be considered as the lost profit.

108 Both, the loss of profit and the direct loss are sought by Oceania Printers on the same ground, which is the amount that our client expected to earned had the contract with Oceania Confectionaries been performed, which consisted on a sum of USD $ 1,600,000 as a result of four years of contractual commercial relations and a possible renewal of this contract for the same period, given that if McHinery Equipment had delivered our client the appropriate machine

to print on 8 micrometers thickness, it would not have lost that contract and his assets would have substantially accrued.

109 The way in which the term of four years under the contract must be calculated does not have an explicit consideration under the CISG; however, UNIDROIT Principles states in article 7.4.3, that "compensation is due only for harm, including future harm that is established with a reasonable degree of certainty". This principle does not fill a gap, but rather states expressly what the CISG, by implication, included in Article 74 of CISG. [ZELLER p. 128].

What article 7.4.3 of UNIDROIT Principles establishes is considered by doctrine as "future profits". This approach is not new, for instance, in Cory v. Ironworks, the court decided that even though the future profits were those that the buyer actually suffered, they must be recognized and form part of the total compensation package. The court awarded damages on that basis, as otherwise the innocent party could have been left under-compensated and the seller's breach without sanction. [BRIDGE p.130].

Thus, as future takings contained into loss of profit, Oceania Printers claims the amount of USD$160,000 as a consequence of the cancelled contract with Oceania Confectioneries.

110 The essential elements on which calculation of future profits must be based are A) the degree of certainty and B) its foreseeability, which will determine the actual amount.

A) The degree of certainty must be proven through evidence such as documents, witnesses as well as many other objective circumstances that could prove that if the party in breach had performed the contract, the injured party would have actually obtained the profits that he expected under the contract.

111 There was a highly degree of certainty that in the contract with Oceania Confectioneries our client would obtain the profit expected for it, undisputed is that a written contract between Claimant and Oceania Confectioneries came into being, in which Oceania Printers undertook to provide wrapping services for Oceania Confectioneries' products by 15 July 2002, and Oceania Confectioneries to pay for those services an annual amount of USD $400,000 over a four-year term [C. E. No. 3].

A similar fact scenario was present in case of Air Compressors, on 6 December 1995, in which the court decided that the documents in which the contract between plaintiff and third parties was based, proved the certainty of the loss of profit.

112 B) The foreseeability requirement must follow the same rule that article 74 of CISG in its second part establishes. According to this, "such damages may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matter of which he then knew or ought to have known, as a possible consequence of the breach of contract".

113 In this respect, Professor Liu comments that: "the foreseeability was established at common law in the famous case Hadley v. Baxendale and further restated in Victoria Laundry v. Newman Industries. In this regard, it was once thought that Hadley v. Baxendale should be understood as establishing two rules, namely that the damages should be such as may fairly and reasonably be considered as arising either: a) naturally, i.e. according to the usual course of things from such breach of contract itself; or b) as may reasonably be supposed to have been in the contemplation of both parties at the time they made the contract as the probable result of the breach" [LIU].

Summing up, in order to assess the presence of the foreseeability element under article 74 of CISG, it must be considered: a. - the party anticipate the loss at the time of the conclusion of the contract, b. - if the breach was a direct consequence of the loss of profit, c.- if both parties had knowledge that in case of breach, a loss of profit could arise.

114 The future proceeds claimed by Oceania Printers were foreseen by both parties, as it can be inferred from the following:

a. - The parties foresaw at the time of the conclusion of the contract the loss of profit. Since the conclusion of the contract was on 1 July 2002. [C. E. No. 8] and buyer advised seller through its letter of 10 May 2002, of the contract that the former had executed with Oceania Confectionaries and the profits involved therein [C. E. No. 3].

115 b.- The breach committed by McHinery Equipment was a direct consequence of the loss of profit that Oceania Printers suffered, given that the Magiprint Flexometix machine sold to our client was not able to supply Oceania Confectioneries with the printed foil they needed and inevitably, the contract between them was cancelled. [C. E. No. 10].

In support of the foregoing, we rely on the Art Paper case, CIETAC February 2 1996, in which the arbitral tribunal decided that the buyer had the right to claim loss of profit from the seller for due to the breach committed by the seller, the buyer was not capable to fulfill its obligations *vis-à-vis* its customer. See also the Rolled Wire Rod Coil case, CIETAC April 28 1995, and the Chinese Goods case, 19960321, 21 March 1996.

116 c.- Both parties were knowledgeable at the time they contracted, about the loss of profit that the buyer could suffer in case of non-performance with Oceania Confectioneries; on 10 May 2002, Oceania Printers communicated to McHinery Equipment the existence of a signed contract with Oceania Confectioneries [C. E. No. 3].

Based on all the foregoing, the Arbitral Tribunal must find that our client is entitled to claim from McHinery Equipment Suppliers USD$160,000 by way of future profits.

117 However, the amount that Oceania Printers is entitled to claim as a concept of loss of profit must also include the renewal of the contract with Oceania Confectionaries. This was confirmed as early as 1967 in Lavarack v. Woods of Colchester, where the court decided that the mere chance of profit must be compensated.

Indeed, this loss of chance is expressly included in UNIDROIT Principles, whose article 7.4.3(2) states that “compensation may be due for the *loss of a chance* in proportion to the probability of its occurrence.”

118 It must be noted that although this is not a mandatory rule, for this UNIDROIT Principle states “may be” instead of “must be“, as submitted by an authority “the plaintiff has to establish with a reasonable degree of certainty that is profit is possible and that a loss of that profit will eventuate due to the breach of the contract. This in itself has an element of chance…” [ZELLER p. 131].

119 The degree of certainty as a concept of “change” varies from case to case which each state court or arbitral tribunal one analyzes it according to its special circumstances involved, as evidenced in the following decisions:

In Commonwealth v. Amman Aviation, of 1991; the court decided that the Respondent was in a position to claim the <u>total amount</u> of an expected renewal of the three-year border surveillance contract, for they had the necessary experience and aircraft in place.

120 Likewise, in the Licensed Equipment case, ICC 9078; the Arbitral Tribunal decided in favour of Claimant, awarding him the <u>total amount</u> claimed from Respondent, based on the certainty of

degree in the assessments, and the probability of the occurrence of the lost of opportunity and the amount of harm suffered, that he had in his contracts with third parties.

Similarly, in Dried Sweet Potatoes case, CIETAC 14 March 1996; the Arbitral Tribunal decided to grant buyer the total amount he claimed from seller as a loss of profit; for loss of profit included a resale contract that Claimant lost as a consequence of the breach committed by Respondent.

121 On the facts of this case supported by the record, it is submitted that Oceania Printers had, at least, 50% of probability that the renewal with Oceania Confectioneries would occur, given that when the first four years of commercial relationships comes to an end (summer 2006) there would not be another printing company with a flexoprint machine to fulfill Oceania Confectioneries' contract [P. O. No. 2 p. 32]. Based on this assumption, once it became clear buyer was unable to service its contract with Oceania Confectioneries, Reliable Printers,- our client's sole competitor-, purchased in the summer of 2002, a machine with the necessary requirements so as to procure since then, Oceania Confectioneries' contract. [C. E. No.9].

3.2.1 BASED ON A PROPER CALCULATION, DAMAGES BY WAY OF INDIRECT LOSS OWED TO OCEANIA PRINTERS AMOUNT TO USD$95,000.00

122 I.- USD $20,000, being the difference between the USD $42,000 purchase price of the Magiprint Flexometix Mark 8 machine and the USD $22,000 obtained from the machine's resale to Equatoriana Printers.

II.- USD $50,000, being the cost that Oceania Printers invested for adapting its plant to the installation of the Magiprint Flexometix Mark 8 machine.

III. - USD $25,000, being the amount spent by the personnel of McHinery Equipment Suppliers in testing the machine.

The sum of these concepts makes an amount of:	USD $20,000
	USD $50,000
	USD $25,000
	USD $95,000.

123 Accordingly, as Respondent has already agreed to pay the monies corresponding to the above listed damages´ headings but those sums have not been settled as yet, this Arbitral Tribunal must confirm respondent's obligation to pay USD$95,000 by way of indirect loss.

3.2.2 BASED ON A PROPER CALCULATION, DAMAGES BY WAY OF LOSS OF PROFIT OWED TO OCEANIA PRINTERS AMOUNT TO USD $2,400,000:

124 I.- USD$1,600,000 being the annual profit of USD$400,000 that Oceania Printers would have earned from the contract with Oceania Confectionaries using the Magiprint Flexometix calculated over a period of the first four years contract. (USD $400,000 X 4 years = USD$1,600,000).

II. - USD$80,000 being the 50% of the renewal of the contract with Oceania Confectionaries.

The above-listed damages claimed as loss of profit total:

USD$1,600,000
USD$80,000
USD$2,400,000

Consequently, the total amount that Oceania Printers expects from McHinery Equipment is: **USD$2,495,000**

3.2.3 THE AMOUNT OF DAMAGES CLAIMED MUST NOT BE REDUCED IN ANY WAY, AS OCEANIA PRINTERS COMPLIED WITH ITS OBLIGATION TO MITIGATE THE LOSS, IN ACCORDANCE WITH ARTICLE 77 OF CISG.

125 Once the buyer has calculated the total amount of damages, it is acknowledged that this amount could be reduced if the mentioned did not take the measures as are reasonable in the circumstances in order to mitigate the loss suffered by the breach committed form the seller. Thus, Article 77 of CISG states this limitation: “A party who relies of contract must take such measures as are reasonable in the circumstances to mitigate the loss, resulting from the breach. If he fails to take such measures, the party in breach may claim a reduction in the damages in the amount by which the loss should have been mitigated”.

126 The main purpose of article 77 of CISG is to force the party entitled to be awarded damages, to act and become active in order to minimize the loss or to prevent it at all. [LIU]. Following the same line of reasoning, it has been submitted that “once a party has reason to know that

performance by the other party will not forthcoming, he is expected to take such affirmative steps as are appropriate in the circumstances to avoid the loss". [LOOKOSFKY p.294].

127 Therefore, the general rule according to article 77 of CISG, is that once the buyer has taken reasonable measures according to the circumstances he is entitled to claim the total amount of the damages. To the contrary, had he failed to comply with his obligation to mitigate the loss in conformity with the Convention, the party in breach may claim a reduction of the damages.
128 Furthermore, based on the same provision, the injured party has to prove two thresholds: that he acted A.- As a reasonable person, and B.- According to the circumstances.

A.- The CISG does not give an exact meaning of the term reasonableness. However, by way of example, art. 1:302 of PECL determines that reasonableness is to be judged by what persons acting in good faith in the same circumstances and in the same situation as the parties would consider to be reasonable. In particular, in assessing what is reasonable the nature and purpose of the contract, the circumstances of the case, and the usages and practices of the trade or professions involved should be taken into account.

129 The term "reasonableness" gives the parties the possibility of judging whether either of them acted in good faith under the circumstances so as to be considered "reasonable".
Furthermore, according to Professor Honnold, the obligation to mitigate the loss could be followed by a requirement to specific performance in order to fulfill with article 77 of CISG's obligation [HONNOLD p 460].
130 Once Oceania Printers realized the lack of conformity about the machine, it promptly asked McHinery Equipment, to fix it. [C. E. No. 9 and R. E. No. 2]. It is submitted that most buyers in the same circumstances would have asked seller to fix what had been sold, whenever possible.

131 If Oceania Printers would not acted as a reasonable person, he would performed: trying to fix by himself the good, even thought he is not an expert in the Magiprint Flexometix Mark 8 machine; asking from someone else different than McHinery Equipment to fix the Magiprint Flexometix; by not giving notice, to McHinery Equipment the lack of conformity within a reasonable time after he discover it, and he had just waited from Oceania Confectionaries to cancel the contract. Consequently Oceania Printers took such measures as a reasonable person.

132 B.- There is no general rule by which the parties could establish that they acted according to the circumstances. Anyway, the decision on how and in what way the party affected by the breach acted in accordance to mitigate the loss requires a careful examination of all circumstances of a concrete situation, criterion of reasonableness, and the type of loss in question. [DJAKHONGIR].

133 Once the contract with Oceania Confectioneries was cancelled, there was no point in keeping the defective good. [C.E. No.10]. Furthermore, there was not another significant contract for Oceania Printers in which it could use the Magiprint Flexometix, [P.O. No. 2 p. 20]. In 2002 the total value of the potential contracts for which the machine could be used in Oceania did not exceed USD$10,000 per year, rendering a gross profit of perhaps USD$2,000 before depreciation of the machine, compared with the USD$400,000 that he would earned from the contract with Oceania Confectioneries.

134 Based on all the foregoing, it is incontestable that in the case at hand, there was no other way for Oceania Printers to mitigate the loss other than to resell the machine [Resale German case, 1999/AR/9, 20 October 2004]. What is more, at that time Oceania Printers had knowledge that Equatoriana Confectioneries would be interested in acquiring the Magiprint machine. Oceania Printers sold immediately the good to Equatoriana Confectioneries in order to preserve the amount that he expended by purchasing the good from McHinery Equipment.

135 Had buyer not acted according to the circumstances, he would have waited an unreasonable period of time and the machine would have substantially devalued. As a result, buyer would have received a minor amount for the resale than the USD $22,000 he received from Equatoriana Confectioneries.

136 To sum up, this Arbitral Tribunal must declare that Oceania Printers acted as a reasonable person under the circumstances, as required by article 77 of CISG, and consequently, the overall amount claimed by our client by way of damages must no be reduced.

Respectfully submitted,

By:

(signed)

Counsel on behalf of Claimant