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ICC Arbitration News

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Final Report on Construction Industry Arbitrations

Recent Developments in Brazilian Arbitration Legislation

Unidroit Principles of International Commercial Contracts in ICC Arbitration

Commentary of ICC Awards 1999 – 2001
Extracts from ICC Awards 1999 – 2001

BULLETIN

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The Unidroit Principles of International Commercial Contracts in ICC Arbitration, 1999 – 2001

Introduction

The present report is a follow-up to an initial article on the application of the Unidroit Principles of International Commercial Contracts in ICC arbitration,¹ which was published in volume 10, no. 2 of this *Bulletin*. That article covered 23 cases decided between 1995 and 1998.² The present study covers the period from January 1999 to December 2000, during which the Unidroit Principles were applied in 14 ICC cases.³ In light of the increasing interest in the Unidroit Principles, it has been thought that an update on the subject would be instructive and helpful.

To aid comparison, the same basic classification will be adopted in this report as in first one, where a distinction was made between application of the Unidroit Principles as the proper law of the contract, their application as a means of interpreting or supplementing applicable national law, and their use as a means of interpreting or supplementing international uniform law.

Applications of the Unidroit Principles

ICC reference	Where published	Type of application
24 7365 Final award May 1997	Court decisions relating to the award: US District Court, S.D. Calif., 7 December 1998 (1999) XXIVa <i>Yearbook Commercial Arbitration</i> (Y.B. Comm. Arb.) 875-881 (including reference to the Unidroit Principles); (1999) XXIVa Y.B. Comm. Arb. 287-293; Trib. gr. inst. Paris 21 May 1997, [1997] <i>Revue de l'arbitrage</i> (Rev. arb.) 417-427; Paris 15 September 1998, [1999] Rev. arb. 103-120 (Annot. P. Lalive).	As a means of interpreting/supplementing applicable national law.
25 7819 Partial award August 1999	(2001) 12:2 <i>ICC International Court of Arbitration Bulletin</i> (ICC IC Arb. Bull.), this issue, 56-57.	As a means of interpreting/supplementing CISG.

¹ See F. Marrella & F. Gélinas, 'The Unidroit Principles of International Commercial Contracts in ICC Arbitration' (1999) 10:2 ICC IC Arb. Bull. 26. For a fuller analysis of these issues, see F. Marrella, 'La nuova lex mercatoria. Principi Unidroit e usi dei contratti del commercio internazionale' in *Trattato di diritto commerciale e di diritto pubblico dell'economia diretto da Francesco Galgano* (Padova: CEDAM, forthcoming, 2002).

² Although the Unidroit Principles were officially introduced in May 1994, no reference was made to them in an ICC arbitration until 1995.

³ This update also includes an award from 1997 (no. 7365), which was not included in the previous report.

26	8547 Final award January 1999	(2001) 12:2 ICC IC Arb. Bull., this issue, 57-60.	As a means of interpreting/ supplementing ULIS.
27	9474 Interim award February 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 60-67.	As the proper law of the contract.
28	9479 Final award January 1999	(2001) 12:2 ICC IC Arb. Bull., this issue, 67-73.	As the proper law of the contract.
29	9594 Final award March 1999	(2001) 12:2 ICC IC Arb. Bull., this issue, 73-76.	As a means of interpreting/ supplementing applicable national law.
30	9651 Final Award July 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 76-81.	As a means of interpreting/ supplementing applicable national law.
31	9753 Final award April 1999	(2001) 12:2 ICC IC Arb. Bull., this issue, 82-84.	As a means of interpreting/ supplementing applicable national law.
32	9759 Preliminary award July 1999	(2001) 12:2 ICC IC Arb. Bull., this issue, 84-88.	As a means of interpreting/ supplementing applicable national law.
33	9797 Final award July 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 88-95.	As the proper law of the contract.
34	9875 Final award March 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 95-99.	As the proper law of the contract.
35	10022 Partial award August 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 100.	As a means of interpreting/ supplementing applicable national law.
36	10114 Final award March 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 100-102.	As a means of interpreting/ supplementing applicable national law.
37	10335 Final award September 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 102-106.	As a means of interpreting/ supplementing applicable national law.
38	10346 Final award December 2000	(2001) 12:2 ICC IC Arb. Bull., this issue, 106-115.	As a means of interpreting/ supplementing applicable national law.

I. The Unidroit Principles as the proper law of the contract (*lex contractus*)

In order to highlight the reasoning of international arbitrators, a distinction will be drawn between cases in which parties made an express reference to the Unidroit Principles and those in which no such choice was made. In the latter case, the choice was made by the arbitrators, pursuant to article 17 of the ICC Rules of Arbitration of 1998⁴ or article 13 of the former (1988) version of the Rules.

1. Choice of *lex contractus* by the parties

In three of the new cases, the parties chose the Unidroit Principles as the governing law in their original contract or during the arbitration proceedings.⁵ The Principles were here considered either as international trade usages, an expression of modern international commercial law, or general principles of law.

In case 9479, the dispute concerned the interpretation of a trademark licensing agreement. During the proceedings, the respondent argued that the contract should be revised by replacing some of the agreed terms with those of Council Directive 89/104/EEC of 21 December 1988 to approximate the laws of the Member States relating to trademarks. The respondent pleaded it had suffered hardship, as defined in article 6.2.2 of the Unidroit Principles.⁶ The arbitral tribunal found that the parties' express choice of New York law to govern their contract related only to its validity. No other national law having been agreed upon, the tribunal concluded that the contractual provisions and international trade usages should be applied to decide remaining contractual issues. It considered the Unidroit Principles to be an accurate representation of international trade usages and on this basis came to the conclusion that no hardship had been suffered.

In case 9474, at the suggestion of the arbitral tribunal, the parties agreed on the application of 'the general standards and rules of international contracts'. In the arbitrators' view, there was no one convention directly expressing such principles. Whilst the United Nations Convention on Contracts for the International Sale of Goods (CISG) could be thought to embody universal principles of international contracts, its application to that particular case would have required the parties expressly to choose it in their contract. The arbitral tribunal also pointed to other more recent texts expressing current general standards and rules of commercial law which could equally have been used, such as the Principles of European Contract Law (PECL), the Unidroit Principles of International Commercial Contracts and domestic laws too, both common law and civil law (e.g. the Uniform Commercial Code of the United States).

The third case – 9797 – has already been the subject of much discussion in various publications. For present purposes, suffice it to say that in the final award the sole arbitrator eventually found the principles of contractual interpretation needed to decide the case embodied in the Unidroit Principles and PECL.⁷ The former were further used to establish a number of important conclusions such as: (a) the 'member firms' implicit obligation to

intention of the parties even if this differs from the literal meaning of the words.) and, further, Unidroit Principles, art. 4.1(2) ('If such an intention cannot be established, the contract shall be interpreted

according to the meaning that reasonable persons of the same kind as the parties would give to it in the same circumstances.') and PECL, article 5:101(3) ('If an intention cannot be established

according to (1) or (2), the contract is to be interpreted according to the meaning that reasonable persons of the same kind as the parties would give to it in the same circumstances.').

⁴ ICC Publication 808, available from the Secretariat of the ICC International Court of Arbitration and on the ICC Court's web site: www.iccarbitration.org

⁵ Cf. case 8331 (1999) 10:2 ICC ICArb. Bull. 65, where the parties agreed that the Arbitral Tribunal shall apply the relevant agreements between the parties and, to the extent that the Arbitral Tribunal finds it necessary and appropriate, the Unidroit Principles of International Commercial Contracts of May 1994 shall be applied by the Arbitral Tribunal.

It may also be noted that during the period of reference a further partial award was rendered in case 7110. This case was considered in the first report, to which the reader is referred.

⁶ Article 6.2.2 (Definition of hardship): There is hardship where the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party receives has diminished, and

(a) the events occur or become known to the disadvantaged party after the conclusion of the contract;

(b) the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract;

(c) the events are beyond the control of the disadvantaged party; and

(d) the risk of the events was not assumed by the disadvantaged party.

⁷ Unidroit Principles, art. 4.1(1) ('A contract shall be interpreted according to the common intention of the parties.') and Principles of European Contract Law (PECL), art. 5:101(1) ('A contract is to be interpreted according to the common

cooperate and to pursue their professional practice in accordance with the principles of good faith and fair dealing inherent to international contracts';⁸ (b) party Z's duty of best efforts 'to ensure cooperation, coordination and compatibility among the member firms' practices';⁹ (c) release of the parties from their obligation to carry out and receive further performance, upon termination of their contract;¹⁰ and (d) the impossibility for party X to claim full compensation as defined in article 7.4.2 of the Unidroit Principles.¹¹

These cases show modern arbitration to be increasingly affected by the multiplication of general principles of contract law. In award 9797 the arbitrator felt it was necessary to refer to two sets of principles, which is in itself striking, since the case was a good example of global litigation, where the Unidroit Principles could have sufficed. There is a risk that such multiplication may undermine the Unidroit Principles and complicate choice-of-law problems in international arbitration. The phenomenon therefore needs to be monitored.

2. No explicit choice of law by the parties

The Unidroit Principles have been applied by arbitrators even where the parties did not expressly refer to them.¹² In such cases they are generally treated as an expression of *lex mercatoria*.

In case 9875, the dispute turned on the interpretation of an exclusive licensing agreement between two companies, one from Western Europe, the other from Asia. According to the contract, the claimant was granted an exclusive right to sell the respondent's products in Europe. The claimant contended that the respondent had entered into a separate agreement with a third party breaching the initial exclusive agreement. There was no choice-of-law provision in the contract, and the arbitrators decided to deal with this question in a partial award. Using the objective method, they found there to be no significant connection, which, in the words of the arbitral tribunal, revealed 'the inadequacy of the choice of a domestic legal system to govern a case like this', covering the manufacture and sale of products in various parts of the world. Nor could the choice of Brussels as the seat of the arbitration lead to application of Belgian law. The only path open to the arbitral tribunal was to resort to *lex mercatoria*, defined as rules and usages of international trade originating from operators, arbitral decisions and institutions such as Unidroit. At the same time, however, the arbitral tribunal took account of relevant national laws concerning intellectual property rights issues raised during the proceedings.

II. The Unidroit Principles as a means of interpreting or supplementing applicable national law

The number of cases illustrating this category of application is on the increase. As noted in the previous report, such an application falls outside the scope of the Preamble of the Principles. It is a type of application that has been developed by arbitral practice in order to confirm a solution based on other legal grounds. Its effect is to give a transnational status to the application of a domestic law. A distinction will be made between cases in which the parties referred to the Principles and those in which the arbitral tribunal introduced the Principles without a specific request from the parties.¹³

⁸ Unidroit Principles, art. 1.7: '(1) Each party must act in accordance with good faith and fair dealing in international trade. (2) The parties may not exclude or limit this duty.'

⁹ Unidroit Principles, art. 5.4.2: 'To the extent that an obligation of a party involves a duty of best efforts in the performance of an activity, that party is bound to make such efforts as would be made by a reasonable person of the same kind in the same circumstances.'

¹⁰ Unidroit Principles, art. 7.3.1(1): 'A party may terminate the contract where the failure of the other party to perform an obligation under the contract amounts to a fundamental non-performance'; and art. 7.3.5(1): 'Termination of the contract releases both parties from their obligation to effect and to receive future performance.'

¹¹ (1) The aggrieved party is entitled to full compensation for harm sustained as a result of the non-performance. Such harm includes both any loss which it suffered and any gain of which it was deprived, taking into account any gain to the aggrieved party resulting from its avoidance of cost or harm. (2) Such harm may be non-pecuniary and includes, for instance, physical suffering or emotional distress.'

¹² E.g. cases 7375, 8261, 8501, 8502, 8503. See F. Marrella & F. Gellinas, *op. cit.*

¹³ This distinction reflects that made in article 17(1) of the ICC Rules of Arbitration (1998).

1. Application requested by parties

Growing awareness amongst parties of the existence of the Principles has led to their increasing use. Thus, arbitrators apply the Principles not only to reach a solution consistent with general principles of law, but also because this is the wish of the parties.

In case 9759, the Principles were used to determine the validity of an arbitration clause in which a national law was chosen to govern the parties' contract. The parties disagreed in their interpretation of the arbitration clause, which they sought to elucidate during the arbitral proceedings by referring to the Unidroit rules of interpretation. Referring to articles 4.5¹⁴ and 1.6(2)¹⁵ of the Principles, the arbitral tribunal found that the parties had intended to resort to arbitration and that their arbitration agreement was valid.

Case 10114 concerned an after-sales agreement between an East European and a Chinese company, in which there was no choice of law. During the proceedings the Chinese claimant argued for the application of Chinese law, calling at the same time for the application of international practices, as expressed in the Unidroit Principles and CISG, noting that the latter concerns sales contracts only. The East European respondent contended that Chinese law should apply 'to the extent CISG, Unidroit or general principles of international trade law do not prevail over or complete the Chinese law'. The arbitral tribunal reasoned as follows: Chinese law is applicable by mutual consent; CISG is part of Chinese law and is applicable *sub specie*; the Unidroit Principles are rules of law within the meaning of article 17(1) of the ICC Rules. In its final decision it dismissed the claim for punitive damages as neither Chinese contract law nor the principles of international trade law contained any provision for such damages.

Another interesting illustration of the joint application of national law and transnational principles is found in case 9651. The contract underlying the dispute between the parties was governed by Swiss law. However, it also contained a clause referring to 'justice, equity and good conscience', which led the respondent to refer to the Unidroit Principles as 'a useful guide in relation to such principles of justice and equity as are internationally acceptable'. The respondent was alleging that the claimant had obtained the contract by fraud and material misrepresentation. In order to decide difficult issues of contract interpretation, the arbitrators resorted to transnational principles, finding that principles of contract interpretation drawn from Swiss law were consistent with Indian law, 'all civilized jurisprudence' and the Unidroit Principles.

Case 10022 illustrates an application of the Unidroit Principles via the notion of trade usages and article 17(2) of the ICC Rules of Arbitration.¹⁶ The claimant argued that since arbitrators are required to take into account international trade usages and since the Unidroit Principles are a codification of trade usages, the arbitrators should rely on the Unidroit Principles. This however begs the question of what is meant by 'take account of trade usages', which has been and still is a source of much discussion amongst scholars.¹⁷ It is also unclear whether or not the Unidroit Principles are a codification of trade usages.¹⁸ Besides, they are not alone: as already mentioned, there are also the Principles of European Contract Law and other similar codifications may be developed in the future. Will the multiplication of such principles of uniform contract law lead arbitrators to multiply their references to them *ad abundantiam*? There would seem to be a tendency in this direction, without as yet any clear solution to the choice-of-law problems this will raise.¹⁹

2. Application by arbitrators

In four cases a solution reached via the applicable national law was confirmed by reference to the Unidroit Principles.

14

'Contract terms shall be interpreted so as to give effect to all the terms rather than to deprive some of them of effect.'

15

'Issues within the scope of these Principles but not expressly settled by them are as far as possible to be settled in accordance with their underlying general principles.'

16

'In all cases the Arbitral Tribunal shall take account of the provisions of the contract and the relevant trade usages.'

17

See Fouchard, Gaillard, Goldman, *On International Commercial Arbitration*, edited by E. Gaillard & J. Savage (Kluwer Law International, 1999) at 844ff; E. Gaillard, 'La distinction des principes généraux et des usages du commerce international' in *Etudes offertes à Pierre Bellet* (Paris: Litec, 1991) 203; F. S. Nariman, 'International Commercial Arbitration and the Rule of Law' (1991) 2:2 ICC IC Arb. Bull. 7; A. Kassis, *Théorie générale des usages du commerce* (Paris: LGDJ, 1984).

18

See especially Final Award in case 8873 (1999) 10:2 ICC IC Arb. Bull. 78. (1998) 125 J.D.I. 101 (Annot. D.Hascher).

19

However, see the practical solution adopted in article 32-A of the ICC Model International Franchising Contract (ICC Publication 557, 2000) and the commentary on the model contract by E. Jolivet, 'Loi applicable et règlement des différends dans le contrat-modèle de franchise internationale CCI' [2000:4] *Cahiers de droit de l'entreprise* 30.

²⁰ These principles are stated in articles 1.3 and 1.7 of the Unidroit Principles. Art. 1.3: A contract validly entered into is binding upon the parties. It can only be modified or terminated in accordance with its terms or by agreement or as otherwise provided in these Principles.' Art. 1.7: see *supra* note 9.

²¹ 'Each party shall cooperate with the other party when such cooperation may reasonably be expected for the performance of that party's obligations.'

²² See *supra* note 8.

²³ (1) The non-performing party is not liable for harm suffered by the aggrieved party to the extent that the harm could have been reduced by the latter party's taking reasonable steps.
(2) The aggrieved party is entitled to recover any expenses reasonably incurred in attempting to reduce the harm.'

²⁴ (1) The parties are bound by a usage to which they have agreed and by any practices which they have established between themselves.

(2) The parties are bound by a usage that is widely known to and regularly observed in international trade by parties in the particular trade concerned except where the application of such usage would be unreasonable.'

²⁵ Art. 4.1: '(1) A contract shall be interpreted according to the common intention of the parties. (2) If such an intention cannot be established, the contract shall be interpreted according to the meaning that reasonable persons of the same kind as the parties would give to it in the same circumstances.' Art. 4.2: '(1) The statements and other conduct of a party shall be interpreted according to that party's intention if the other party knew or could not have been unaware of that intention.

(2) If the preceding paragraph is not applicable, such statements and other conduct shall be interpreted according to the meaning that a reasonable person of the same kind as the other party would give to it in the same circumstances.'

Art. 4.3: 'In applying Articles 4.1 and 4.2, regard shall be had to all the circumstances, including:

- (a) preliminary negotiations between the parties;
- (b) practices which the parties have established between themselves;
- (c) the conduct of the parties subsequent to the conclusion of

In case 9594, the arbitrators applied English law on mitigation of damages, noting that 'a similar standard has been established internationally, primarily in the Unidroit Principles'. In case 9753, the sole arbitrator gave due consideration to the Czech Commercial Code as well as to broader principles such as *pacta sunt servanda* and the duty to cooperate in good faith as proper grounds for resolving the dispute.²⁰

More interesting than case 10346, where there are brief references to the Unidroit Principles, articles 5.3,²¹ 1.7,²² 7.4.8,²³ and 7.3.1 on withholding performance, confirming solutions drawn from Colombian law, is the final award in case 10335. Here, a shareholders agreement was interpreted according to Greek law, expressly chosen by the parties. The sole arbitrator showed the specific rules on interpretation contained in articles 173 and 200 of the Greek Civil Code to be common to most civil law systems. He thence showed these rules to be consistent with the Unidroit Principles since: '[m]odern international commercial law is evolving in the same direction (cfr., for example, articles 1.7, 1.8²⁴, 4.1-4.3²⁵ of the Unidroit Principles of International Commercial Contracts)'.²⁶

These cases once again show the importance to arbitrators of a neutral set of transnational principles to underpin the validity of their decisions beyond applicable national law.

III. The Unidroit Principles as a means of interpreting or supplementing international uniform law instruments

Without entering into the continuing debate over national versus autonomous means of interpreting and supplementing international uniform law conventions,²⁷ we here simply note the techniques adopted by ICC arbitrators in this field.²⁸

In case 8547, the arbitral tribunal used the Unidroit Principles to supplement the Uniform Law on the International Sale of Goods (ULIS), deciding that the respondent was entitled to stop payment because of the non-conformity of the goods delivered. It reached this conclusion on the basis of *exceptio non adimpleti contractus*, a concept reflected in article 7.1.3 of the Unidroit Principles, to which reference was made via article 17 of ULIS.

In case 7819, where French law was applicable, the arbitral tribunal referred both to article 55 of CISG and to article 5.7²⁹ of the Unidroit Principles in order to conclude in favour of the

the contract:
(d) the nature and purpose of the contract;
(e) the meaning commonly given to terms and expressions in the trade concerned;
(f) usages.'

²⁶ The use of 'for example' followed by a reference to the Unidroit Principles is becoming a technique commonly employed by arbitrators to show that their decision is in line not only with the applicable national law but also with principles enjoying wide international consensus. See also case 9651.

²⁷ See e.g. P. Schlechtriem, ed., *Commentary on the UN Convention*

on the International Sale of Goods (CISG), 2d ed. (Oxford: Clarendon Press, 1998) sub art. 7, and M. Gebauer, 'Uniform Law, General Principles and Autonomous Interpretation' (2000) 5 *Unif. L. Rev.* 683.

²⁸ It is clear that if the *lex contractus* is a given national law, that law may incorporate specific international conventions.

²⁹ '(1) Where a contract does not fix or make provision for determining the price, the parties are considered, in the absence of any indication to the contrary, to have made reference to the price generally charged at the time of

the conclusion of the contract for such performance in comparable circumstances in the trade concerned or, if no such price is available, to a reasonable price.
(2) Where the price is to be determined by one party and that determination is manifestly unreasonable, a reasonable price shall be substituted notwithstanding any contract term to the contrary.
(3) Where the price is to be fixed by a third person, and that person cannot or will not do so, the price shall be a reasonable price.
(4) Where the price is to be fixed by reference to factors which do not exist or have ceased to exist or to be accessible, the nearest equivalent factor shall be treated as a substitute.'

validity of a sales contract lacking provisions on price. This case is noteworthy since the arbitrators did not refer to the Principles in order to interpret CISG, but rather used them to confirm a solution already expressed in CISG, which, as part of French law, was applicable in the case in question. By referring to the Principles, the arbitrators sought to demonstrate that a contract where the price is not expressly determined is valid and consistent with international commercial practice.

These two cases confirm the possible interplay between the Unidroit Principles and international uniform sales conventions.

IV. Exclusion of the Unidroit Principles

In none of the cases examined for the present report was the application of the Principles considered and ruled out.³⁰ They were always applied either pursuant to a request by at least one of the parties or due to a lack of choice of applicable law.

Conclusion

As far as the application of the Unidroit Principles as *lex contractus* is concerned, this seems to be more characteristic of very large economic arbitrations³¹ than small ones, which consistently prefer a traditional approach based on conflict of (national) laws.

Parties and arbitrators are increasingly aware of the possibility of applying the Unidroit Principles, particularly in conjunction with domestic law.³² However, in some awards arbitrators tend to mix rules from different sources without explaining the reason for their selection, focusing instead on the solution of the issues. This approach can be condoned only from a pragmatic standpoint. Confusion in the choice-of-law process leads to a risk that arbitrators may fail to apply the proper law, which could be detrimental to the legal quality of their final product – the award.

Reference to different sets of general principles of contract law (Unidroit Principles, PECL, and whatever else may emerge around the world) may generate problems of 'conflicts of principles'. Whilst we may know how to solve conflicts of laws, 'conflicts of principles' are quite another matter and arbitrators would be well advised to use the technique of multisourcing with extreme caution.

Finally, as regards use of the Unidroit Principles to interpret and supplement international uniform law conventions, the predilection continues to be towards CISG. However, arbitral behaviour may change, as shown by cases 9474 and 7819. The latter, in particular, shows arbitrators using the Principles to confirm a solution already existing in CISG. Their reasons for doing so are that they will be sure that the CISG is in line with international practice and standards such as those expressed by the Unidroit Principles. Could this be a sign that CISG is beginning to age? Time will tell . . .

³⁰ Examples of previous cases where the Unidroit Principles were excluded are 8873, 9029 and 9419. See F. Marrella & F. Gélinas, *op. cit.*

³¹ E.g. 9797, where the amount in dispute was more than ten billion dollars.

³² This applied to 10 of the 21 cases studied in the previous report covering the period 1995-1998 (*i.e.* approximately 48%) and to 8 of the 14 cases studied in the present report (*i.e.* around 57%).

Extracts from ICC Awards

Referring to the

Unidroit Principles of International Commercial Contracts

Partial Award in Case 7819

September 1999

Original in French

Place of arbitration: Paris, France

1988 ICC Rules of Arbitration

In the extracts published here, details not indispensable for the intelligibility of the award may have been expunged from the original text. Names of parties have been replaced in English by '[Claimant]' and '[Defendant]' (1988 Rules) or '[Respondent]' (1998 Rules) and the equivalent in French. Awards originally drafted in English or French – the official working languages of the ICC International Court of Arbitration – are reproduced in their original language. Otherwise, the text published here is an English translation of the original.

Claimant, a bank, and Defendants, a syndicate of insurance companies, entered into a number of insurance contracts, subject to French law, to cover the possible frustration, due to political circumstances in Brazil, of international sales contracts financed by Claimant. Since the exporting companies had failed to deliver by the previously extended deadline for doing so, Claimant made a claim to Defendants under the insurance contracts, contending that governmental measures in Brazil had prevented the exporters from abiding by their sales commitments and made it impossible for them to repay the advance funding they had been granted by Claimant. Defendants questioned the grounds upon which these claims were made, arguing that the facts referred to by Claimant did not constitute a political risk within the meaning of the insurance contracts and that there was a lack of causality between the events upon which the insurance claim was based and the harm suffered by Claimant. They also accused Claimant of providing them with insufficient information prior to the signing of the insurance contracts. In its partial award, the arbitral tribunal first considered whether or not the underlying sales contracts were valid, as Defendants had argued that they could not be considered as binding due to the deficiency of the price clause. In responding to this point, the arbitral tribunal referred to article 55 of the United Nations Convention on Contracts for the International Sale of Goods and article 5.7 of the Unidroit Principles.

'La défenderesse a contesté la validité des contrats d'exportation selon le droit brésilien, pour indétermination du prix. [...]

[La défenderesse] a dénoncé l'« absence de risque réel », du fait de l'absence de toute force obligatoire des contrats tenant au mécanisme de fixation du prix, et en veut pour preuve que rien ne permet de fixer le prix au-delà de mars 1990.

[La demanderesse] répond que selon l'article 1^{er} des contrats les parties s'engagent respectivement à vendre et à acheter, qu'il s'agit d'opérations tout à fait courantes dans le commerce international considéré, lesquelles s'exécutent quotidiennement nonobstant les objections éventuelles tirées d'une analyse civiliste; au demeurant, les contrats ont été renouvelés et la clause de prix pouvait parfaitement fonctionner.

En ce qui concerne tout d'abord le défaut d'examen des contrats commerciaux par [la défenderesse], le Tribunal observe que les contrats d'assurance ont été conclus au printemps 1989, les premiers rééchelonnements des contrats commerciaux intervenant quelques mois plus tard et les avenants n° 2 des polices étant signés en août 1990 après plusieurs mois de discussions. [La défenderesse] avait donc à chacune de ces étapes le loisir d'examiner de près les contrats commerciaux, de s'enquérir auprès des acheteurs d'une imperfection éventuelle et de mesurer la portée de la *red clause*.

Selon le droit brésilien tel qu'il ressort des débats échangés entre les parties, le caractère déterminable du prix suffit à la validité des contrats. Interrogée par [la défenderesse], la société [...] (acheteur dans les contrats litigieux) a expressément confirmé la régularité et l'efficacité des contrats. Il s'agit d'opérations normales et récurrentes, sur des marchandises qui ont un prix de marché. Par la clause dite d'« arrosage », les acheteurs s'engageaient à prendre les quantités de sucre nécessaires pour que la banque soit remplie de ses droits, en cas de chute des cours. Le Tribunal note surabondamment que la vente sans fixation préalable d'un prix est courante dans le commerce international, comme le montrent la convention de Vienne du 11 avril 1980 sur la vente internationale de marchandises (art. 55) ainsi que les principes Unidroit relatifs aux contrats du commerce international (art. 5.7).

Aucune irrégularité des contrats ou absence de caractère obligatoire n'a par ailleurs été invoquée par les vendeurs dans les procédures judiciaires brésiliennes. Certains ont au demeurant procédé à des livraisons partielles, avant et après le mois de mars 1990. Leur intérêt à livrer résultait des garanties prises par [la demanderesse] sur le matériel, dont l'exécution s'est poursuivie jusqu'à l'intervention de la force publique (même si finalement celle-ci a échoué devant les risques de troubles sociaux) ainsi que des nantissements de sucre, sur lesquels il y aura de revenir.

Compte tenu de ces différents éléments, le Tribunal conclut à la réalité des contrats litigieux.⁷

Final Award in Case 8547

*January 1999
Original in English
Place of arbitration: Paris, France
1998 ICC Rules of Arbitration*

Respondent (buyer) suspended payments to Claimant (seller), following the delivery of defective goods. Claimant continued to demand payment, despite an alleged agreement between the parties settling their accounts. The parties had differing views on the terms applicable to the sales transactions between them. Claimant (seller) contended that they were subject to the terms of a telex it had sent to Respondent on 3 December 1991. Respondent objected, claiming that it could not be considered to have accepted these terms.

as it had proposed alternative terms regarding free-of-charge time, price and insurance in its reply of 4 December 1991. Claimant's telex of 3 December 1991 contained an arbitration clause referring to ICC in Paris and an applicable law clause referring to the Convention relating to a Uniform Law on the International Sale of Goods (The Hague, 1 July 1964). In deciding whether or not Claimant had made a valid claim, the arbitral tribunal referred to articles 4.5 (contract interpretation) and 7.1.3 (non-performance) of the *Unidroit Principles*.

(1) The applicable law on the substance of the case is The Hague Convention of 1.7.64 as the law chosen by the Parties and the *Unidroit Principles* as supplementary rules which the Arbitral Tribunal deems appropriate to apply where necessary in accordance with art. 17 sect. 1 ICC Rules.

(a) As stated in provision no. 20 of Claimant's telex of December 3, 1991, the contract shall be governed by "the Uniform Law for the international sale of corporal movables (Hague Convention 1/7/64)". This clause has evidently been accepted by Defendant. Its telex of December 4, 1991 shows no objection concerning the applicable law proposed by Claimant.

The Arbitral Tribunal is therefore of the opinion that the relationship of the Parties is governed by the substantive law chosen in no. 20 of Claimant's telex. This includes the Convention relating to a Uniform Law on the International Sale of Goods (ULIS) and the Convention relating to a Uniform Law on the Formation of Contracts for the International Sale of Goods (ULF).

According to art. 4 ULIS, the Conventions shall apply where they have been chosen as the law of the contract by the parties, regardless of whether or not the States of their places of business are parties to the Convention. This is in accordance with the principle of party autonomy, which states that parties are free to choose the law to govern their contract.

(b) In so far as the Conventions ULIS and ULF did not cover all questions and referring to article 17 of the ICC Arbitration Rules, the Arbitral Tribunal felt it appropriate to turn to the *Unidroit Principles* which provide useful complement to fill the lacuna and allow to find proper solutions.

(2) The contract was not concluded by exchange of telexes, because the Defendant proposed certain new conditions in its answering telex of December 4, 1991, which materially altered the terms of the contract according to art. 7 ULF. Defendant asked for different conditions concerning the free of charge time regarding delivery, the guaranteed price for all of 1992, and insurance of the goods by seller up to delivery to the end user. The different terms requested by Defendant concern mainly the price of the goods and the insurance risk of the seller.

Such demands for changes in the contract by the other parties are considered by jurisprudence to be material alterations which must be specifically accepted by the party having made the initial proposal. . . . Because the price of the goods is an "essentiale negotii", anything concerning the price must be considered as a material alteration. The insurance and delivery risk of the seller or buyer are also important terms of the contract, as each party must be able to calculate its possible costs beforehand.

Therefore the telex sent by Defendant on December 4, 1991 constitutes a counter-offer and should have been answered by Claimant – either containing a confirmation of the different terms or a new offer. Silence itself cannot have the effect of acceptance, see art. sect. 2 ULF.

(3) However, the contract was formed by Claimant commencing with performance of the contract. The provisions of the contract as proposed in Claimant's telex of December 3, 1991

and not disputed between the parties at any time are valid. The rest of the provisions were negotiated with each delivery:

- (a) Claimant began to deliver goods on December 6, 1991 and continued to do so until August 1992. Defendant accepted delivery of the goods. The contract was formed between the parties the latest with the first delivery by Claimant. According to art. 6, para. 2 ULF "acceptance may also consist of the dispatch of the goods".
- (b) The contract was not – as suggested by Defendant – renegotiated wholly for each delivery. It continued to exist as the legal framework of the parties to which specific alterations or amendments may have been made from time to time. Those alterations or amendments have no bearing on the present dispute.
- (c) Neither Claimant nor Defendant ever objected to the terms of performance of the contract during the time period of delivery of the goods. According to the theory of [implied contract confirmation] this is to be interpreted as agreement on the undisputed terms of the contract as presented in the telex of December 3, 1991, unless the parties specifically agreed on other terms during its performance. Therefore, the provisions of the contract are primarily applicable, supplemented by the rules of ULF and ULIS.

When taking into consideration the internationality of the relations between the parties, the Unidroit Principles become relevant. Article 4.5 Unidroit Principles states that contract terms should be interpreted as to give effect to as many of them as possible. Therefore, if the parties at one point agreed on certain provisions, this needs to be taken into account when trying to resolve a dispute.

In the present case, the Defendant in its answering telex mainly wanted to alter the matters of price and insurance. Since these matters were put in writing for each and every delivery (as shown by the telexes), they can be said to have been renegotiated and agreed upon every time within the existing framework of the contract.

...

- (5) It was the Defendant's right to stop payment because of the non-conformity of the goods.

...

- (b) Although the degree of non-conformity of goods has not been proven, it was the Defendant's right to suspend payment after raising the *exceptio non adimpleti contractus*.

The contract was to be performed step by step, *i.e.* payment was to follow the delivery of goods. If the goods are not of the quality agreed upon in the contract, the buyer must give notice of the non-conformity. Until an agreement is reached between the parties as to the degree of the lack of conformity and as to how to proceed in regard to the non-conformity, the buyer does not have to pay the price. The further development of the contract at that point is unclear. It would amount to a curtailment of the rights of the buyer if he had to continue payment of the goods without knowing what will happen in regard to the non-conformity.

This is not expressly stated in ULIS, but follows from the general principles of law referred to in article 17 ULIS. According to article 7.1.3 Unidroit Principles a party may withhold its performance until performance has been effected by the other party. Thus the above reasoning is in accordance with these principles of law.

- (c) Once the seller knows of a possible non-conformity it is his duty to act upon this knowledge to clear up the degree of the non-conformity.

Since the oral hearing . . . it is undisputed that a meeting took place in . . . , the place of business of . . . , the end user of the purchased products, concerning the quality of the goods. This is proof of the fact that Claimant knew of the possible non-conformity of the goods.

The degree of non-conformity is therefore irrelevant in regard to the right of the Defendant to suspend payment. It is sufficient that Defendant informed Claimant of the non-conformity and then suspended payment until an agreement concerning the lack of conformity was reached. Defendant suspended payment after the meeting in . . . took place. This is not a violation of Defendant's contractual duties.'

Interim Award in Case 9474

February 1999

Original in English

Place of arbitration: Paris, France

1988 ICC Rules of Arbitration

*In 1990, Claimant, a state bank, ordered from Defendant, a securities manufacturer, a certain quantity of banknotes in given denominations. Defendant undertook to ensure that the highest quality standards were applied to the manufacture of the banknotes and to remedy any errors beyond acceptable limits. The notes were delivered late and the smaller denominations failed to meet security and quality requirements. Independent inspections of the notes confirmed the deficiencies noted by Claimant. An agreement was made in 1992 to redesign, print and supply the denominations concerned according to revised specifications at a specially reduced price in recognition of Defendant's responsibility in the matter. Further delays occurred and further defects were discovered in the new samples, leading Claimant to renew its complaints and to question whether Defendant was in a position to perform the contract satisfactorily. In an attempt to resolve their differences, the parties entered into an agreement in 1993, whereby Defendant undertook to supply satisfactory notes at its own cost and, subject to security and quality requirements being satisfied, Claimant granted Defendant the right to contract for future issues of banknotes. However, Claimant continued to be dissatisfied with the notes produced, while Defendant was unwilling to repay an advance due to be returned to Claimant. Upon being informed by Claimant that it could not for the time award a further contract to Defendant, the latter initiated arbitration proceedings, asking for Claimant to be ordered to award it such a contract or, failing this, to provide compensation. Defendant's claims were subsequently considered as withdrawn, due to its failure to pay the first half of its advance on costs, leaving Claimant's counterclaim for damages as the main claim in the case. With the agreement of the parties, the arbitral tribunal rendered the present interim award on various issues linked to the 1993 agreement between the parties. In so doing, it referred to the *Unidroit Principles* when examining the applicable law, the validity of the agreement (articles 3.5 and 3.8) and the eligibility of the claims (article 7.3.2, notice of termination).*

Applicable law

'[1] According to the arbitration clauses, the Arbitral Tribunal should decide "fairly". The meaning of these clauses was discussed with the parties . . .

Both parties accepted the Arbitral Tribunal's proposal to apply "the general standards and rules of international contracts" (Procedural Order No. 1, para. 1, that amended the Terms of Reference).

[2] The Tribunal is of the opinion that these "general principles of contract law" are not directly expressed in a specific international convention.

(a) The States of both parties are now bound by the UN Convention on Contracts for the International Sale of Goods ("the Vienna Convention"). However, many of the circumstances of the present arbitration predate [Claimant State]'s ratification of the Convention.

Although it is generally recognized that the Convention embodies universal principles applicable in international contracts, whether or not the States of the parties are signatories of the Convention (see esp. Final Award in case no. 5713 of 1989, Collection of ICC Arbitral Awards 1986-1990, p. 223 ff), the Tribunal considers that, if the parties had wanted to submit their agreements to the convention, they would have introduced an express clause in that sense.

Besides, in the opinion of the Tribunal, the 1993 Agreement is not merely a sale of goods contract; even if the Agreement has been concluded in the frame of a sale of goods, it entails other components which are typical of a settlement agreement.

(b) There are other recent documents that express the general standards and rules of commercial law, in particular the Principles of European Contract Law and the Unidroit Principles of Commercial Contracts.

Nevertheless the general standards and rules of international commercial law have to be applied to the specific circumstances of the case and in particular to the object of the contract that reflects the intentions of the parties.

The Tribunal shall tackle this issue more precisely as to each one of the specific questions it has to solve in this award.

[3] The general principles of international contracts may also be found among various rules of domestic law, of both common and civil law systems, as applied to international contracts, such as the American Uniform Commercial Code.

The Tribunal considers however that in the present litigation neither [Defendant State's] nor [Claimant State's] law offers relevant and applicable rules. This may be inferred again from the fact that the parties did not refer expressly to any of their domestic rules.

Validity of the 1993 agreement

The question

[4] The question at issue in this section is related to contentions made by the Bank in regard to fraud and mistake that could affect the validity of the 1993 Agreement.

The position of the parties

[5] (a) According to the Bank, the 1993 Agreement must be considered null and void . . . According to [Defendant], Mr [X] was paid . . . as "Public Relation and Consulting Fees" relating to the settlement agreement with the Bank . . . [Defendant]'s non-disclosure of the payment of this generous fee to Mr [X] constitutes a fraudulent non-disclosure of a circumstance which according to reasonable standards of good faith should have been disclosed, with

reference to the Unidroit Principles of International Commercial Contracts, arts. 3.5 and 3.8, and the Principles of European Contract Law 1997, art. 4.107 . . .

(b) According to [Defendant], the Bank's charges, according to which [Defendant] made improper payments to Mr [X] in connection with the conclusion of the 1993 Memorandum of Agreement, are false, unsupported by any evidence and made with malicious and defamatory intent . . .

The position of the Tribunal

[6] The Arbitral Tribunal is of the opinion that the Bank's allegations of fraud and mistake against the validity of the 1993 Agreement are not supported by sufficient evidence and must therefore be rejected.

[7] First of all, the payment of "Public Relations and Consulting fees" to Mr [X]. It has not been demonstrated that this payment was done with a fraudulent intent, as it may be inferred from the following arguments and facts.

(a) Even if Mr [X] was formerly a representative of the Bank, he had been introduced to [Defendant] as no longer being the latter's representative. . . .

Finally, the nature of the relationship between the Bank, [Defendant] and Mr [X] may also be confirmed by the fact that the Governor . . . referred to discussions with Mr [X] as to discussions with an "outsider" . . .

(b) In addition, Mr [X] had never met anyone of [Defendant] before the meeting . . .

(c) Moreover, the fact that he had represented [Defendant] on some occasions was well known to the Bank, and this from the beginning of the negotiations . . .

(d) Thus, the payment did not amount to corruption and its non-disclosure to a fraudulent non-disclosure.

[8] Secondly, the **extent of the influence**. The Bank which has the burden of proof of its allegation did not bring sufficient evidence of its allegations as to the exact extent and consequences of Mr [X]'s undue influence.

Moreover, it did not prove that Mr [X] knew enough about the agreement to be able to influence and induce the Bank fraudulently. Finally, the Bank confirmed the agreement without reservation and never referred to the fact that its consent could have been vitiated.

[9] Thirdly, the **responsibility and effect of the mistake** that has been alleged to influence the conduct of the Bank is not supported by sufficient evidence.

(a) The mistake, that was due to the paper supplier's concealment, is not sufficiently established in that their consequences on the Bank's conduct were not direct. Indeed, the non-disclosure of the fraudulent payment to Mr [X], in case it was established, does not demonstrate that the latter, or [Defendant], was also responsible for the non-disclosure of the paper supplier's action.

(b) This is confirmed by the fact that the Bank had communicated at once that it was dissatisfied with the banknotes delivery. This comforted [Defendant] in its opinion that it was not necessary to communicate facts that were already partly known by the Bank. This does not in any case establish any intent of concealing these precise facts from the Bank . . .

[10] The Arbitral Tribunal is of the opinion that the Bank's allegations against the validity of the 1993 Agreement have not been sufficiently established and must therefore be rejected.'

Eligibility of the claims

The question

[11] [Defendant] claims that the Bank is barred and/or estopped from claiming non-compliance with the terms of the 1993 Agreement.

[Defendant] contends that the Bank is precluded from asserting its claims of non-performance for the reason that, in reliance to its affirmations or conduct as to the contrary, [Defendant] incurred considerable harm. It relies on the general concept of waiver and estoppel.

[12] This issue relates to the question of whether the Bank had an affirmative duty to inspect the banknotes for conformity and if not, whether its silence implied an acceptance. In the event of defects, another issue is the issue of the existence of a duty to give notice, of the extent of the notice period and of the precise content of this notice.

The position of the parties

[13] (a) According to the Bank, [Defendant] cannot meet the burden of proof as to its allegations that the Bank is barred or estopped from claiming non-compliance with the 1993 Agreement . . .

As to the alleged waiver of the Bank's rights, [Defendant] did not receive unequivocal information from the Bank that it had tendered satisfaction of its obligations to the 1993 Agreement. The fact that the Bank required the reimbursement of its advance payment for the banknotes . . . and the cost of the banknote quality inspection did not imply that it renounced its other rights under the 1993 Agreement . . . Besides, [Defendant]'s tender clearly demonstrated that it was not acting in reliance on any alleged rights under the 1993 Agreement and that it was submitted to new essential terms and conditions . . . Such a conduct may neither be interpreted as an unequivocal waiver of rights . . . nor as an estoppel by which the Bank would be precluded from asserting a right when it caused another to change his condition to his detriment . . . The Bank did not cause [Defendant] any harm by not awarding the tender to it and it did not give [Defendant] any reasons to rely to its detriment upon the exclusivity of the reasons stated . . .

As to the inspection and notice duties, even if they are subject to the general principles of law, parties are generally free to derogate from or vary the effect of any of the principles embodied in conventions of international law . . . Indeed, for the Bank, the terms of the . . . 1992 Memorandum meant that [Defendant] would remain responsible for banknotes which had not been inspected but which were found to contain printing errors during the period of issue . . . [Defendant]'s allegations as to the nature of the inspection that the Bank carried on after the first delivery and the derived course of conduct are erroneous as to its promptitude and completeness . . . Besides, according to the Bank, the 1993 Agreement being an executory accord, it is not subject to the principles governing international sales contracts, but only to general contract principles . . . Indeed, the fact that the quantity of banknotes agreed on was to be printed free of charge, the agreement was not a "transfer of goods in exchange for a price expressed in money" . . . Beside the argument of the contractual nature of the Agreement, an executory accord is meant to grant a "limited window of opportunity" within which an obligee can render performance thus making any concern about the cure of non-performance and its consequences on the price secondary . . .

The Bank had actually notified [Defendant] on 10th May 1994 that [Defendant] had delivered many bad quality banknotes . . . Assuming that the Bank was required to give notice and that the 10th May 1994 letter was not sufficient, the Bank considers that the reasonable time of a notice, according to the Unidroit Principles, art. 7.3.2, is meant to prevent any harm due to

uncertainty as to whether the Bank would accept the performance, which was not the case given the nature of executory accord of the Agreement . . . Given these conditions and the strains of the econo-political concerns and the reimbursement question, the Bank did act within a reasonable time . . .

In case the Tribunal decides that arts. 38 and 39 of the Vienna Convention should apply to the Agreement, the Bank claims that art. 40 of the same convention would defeat Defendant's right to rely on the Bank's alleged failure to give notice, since [Defendant] knew or could have been aware of the facts the lack of conformity relates to and could have disclosed them to the Bank . . . This principle may also be found in various national laws . . . Indeed, [Defendant] was aware of the Bank's concerns about specific quality defects of the banknotes printed between 1990 and 1992 . . . Even assuming that the Bank had a duty of notice and that it was not given in conformity with art. 39, art. 44 of the Vienna Convention states that it could still be able to claim damages if it has "a reasonable excuse for its failure to give the required notice" . . .

(b) According to [Defendant], the Bank met none of the conditions that should be fulfilled once the banknotes had been delivered and received . . .

The Bank's representations and statements testify a relinquishment of rights and an intent not to assert any rights, *i.e.* a waiver or estoppel of its rights . . . The Bank is indeed estopped from asserting claims of non-performance by [Defendant] since [Defendant] incurred considerable harm in reliance on the Bank's assurance of its performance and its inconsistent conduct . . . Moreover, according to civil law principles and the rules applied in international practice, a forfeiture of rights can be said to occur without consideration or reliance, depending on the circumstances.

The Bank's arguments that the law of sales does not apply to the Agreement are "far-fetched" . . ., since an agreement, that was nothing more than an embodiment of the modified terms . . ., may be a sales contract. The amendment of a sales transaction must not indeed necessarily be supported by consideration . . . and may be done by mere agreement of the parties (art. 29 Vienna Convention and art. 2-209 UCC . . .). Besides, the banknotes printed pursuant to the 1993 Agreement are not excluded as money or negotiable instruments from the Vienna Convention and the UCC rules . . .

The extent of the duty of a buyer of goods to inspect the goods that have been delivered depends on the precise circumstances and in particular the course of conduct or customary relationship between the parties, as deriving from the 1990, 1992 and 1993 Agreements . . . [Defendant] acknowledges the prompt (within two months) and meticulous inspecting of the banknotes delivered in 1992 in accordance with the first two Agreements . . . It holds however that this course of conduct was the one that was legitimately held to apply to the 1993 series and that the Bank did not respect it by not conducting any inspecting from 1993 to 1995 . . .

[Defendant] further claims that the Bank did not respect its duty of prompt notice. This duty derives not only from legal principles, but also from the course of conduct that may be derived from the behaviour of the Bank after the first delivery of banknotes in 1992 . . . The 1992 Memorandum of Agreement, that set particular rules as to the inspection and notice of defects, did not have the meaning implied by the Bank, of waiving the applicability of international contract rules, and in view of the mass of contractual documents, this Memorandum did not constitute more than a "freely, formally and unequivocally agreed" contractual waiver of the legal principles applicable. It was certainly not a course of conduct between the parties exempting the Bank from virtually all of the recognized rules applicable to international contracts . . . It was superseded by further agreements and was only entered on an *ad hoc* basis for as long as the inspection was not completed . . . Further, the Bank's interpretation according to which a buyer could only notify defects he has found straight away years later

seems unreasonable . . . Such a clause of "everlasting guarantee" cannot be inferred from the course of conduct of the parties . . .

The fact that no notification of defects was communicated until over three years later cannot be considered as constituting a prompt notice . . . as it is confirmed by reference to the average notification period for overt defects according to art. 39 of the Vienna Convention, the UCC or national laws, which is at the most 6 months . . . This view may be confirmed by the fact that the Bank strongly insisted from 1993 onwards on the reimbursement of its 10% deposit without mentioning the defects it now alleges at all . . . The Bank's mention of the existence of many bad quality banknotes in a letter dated 10th May 1994 lacked the specificity required by a notice under art. 19 of the Vienna Convention . . .

The Bank may not excuse its conduct under art. 40 of the Vienna Convention; the scope of art. 40 is to protect the buyer against the bad faith of the seller. [Defendant]'s knowledge of the Bank's habits of thorough inspections and the fact that the parties had foreseen the services of a technical expert tend to prove that the Bank knew the non-conformity of the banknotes. Besides, it was inconsistent with good faith for the Bank to be aware of the defects and wait . . . Further, the Bank had no valid excuse under art. 44 of the Vienna Convention: this Article is not intended to condone a breach of good faith that derives from inconsistent and misleading conduct and statements that may not be justified by "econo-political concerns" . . .

Finally, the outer limit of two years for a notification of defects according to the Vienna Convention, or six months according to French law, carries also a limit for the existence of the cause of action based thereon . . . The Bank is therefore barred from prosecuting its claims for failing to bring a claim within a reasonable time.

The position of the Tribunal

[14] It constitutes a general principal of international contracts that a party may be regarded as barred from pursuing its claims for having renounced its rights expressly or tacitly, by a waiver or an estoppel, or simply for having missed a reasonable notice period.

The burden of proof lies on the party that alleges the waiver or the estoppel. The evidence requirements are very strong given the stringent consequences of a waiver or an estoppel.

(a) To renounce its rights expressly, the Bank would have had to clearly state its intentions and nothing in the facts supports it did at the time [Defendant] claims it did.

The fact that the Bank required the reimbursement of its advance payment for the banknotes and the cost of the banknote quality inspection did not imply that it renounced its other rights under the 1993 Agreement. . . .

In these conditions, the Tribunal considers that the Bank did not act as to waive its rights under the 1993 Agreement.

(b) To renounce its rights tacitly requires that one adopts an attitude that implies a relinquishment of one's rights, such as a voluntary omission to inspect the goods or to give a timely notice of its defects.

One should note however, as to the alleged estoppel of the Bank's rights that would derive from its incoherent attitude regarding the 1996 tender, that [Defendant]'s tender demonstrated clearly that it was not acting in reliance on any alleged rights under the 1993 Agreement. It was by contrast submitted to new essential terms and conditions . . . and sufficient evidence and notice was given all along to [Defendant] of its inability to guarantee the security of the banknotes tendered . . . The Bank did not therefore give [Defendant] any reasons by an allegedly incoherent conduct to rely to its detriment upon the exclusivity of the reasons stated.

The issue of the coherence and signification of the Bank's attitudes, and thus of an estoppel of its rights under the 1993 Agreement, further depends on the existence of a duty to inspect and to give a timely and precise notice. It is the purpose of the following lines to discuss this issue.

[15] As established earlier . . . the Tribunal is invited by the arbitration clause to decide "fairly". With the agreement of the Parties, this has been interpreted as a reference to the general standards and rules of international contracts.

The Tribunal does not regard itself as bound by the provisions of any international convention in particular. It considers that the provisions of the Vienna Convention do not apply directly to the present arbitration. If the parties had meant so, they would have inserted in their agreement a concrete reference to it. The issue should therefore be assessed in a broader perspective.

[16] The Tribunal renounces examining in detail whether the Bank gave notice of the default properly and in due time; the question may therefore stay open. Indeed, the Tribunal considers that in view of all circumstances it cannot decide to deprive the Bank of its rights to claim compensation for the violation of the 1993 Agreement. Various reasons may be brought forward:

(a) First of all, it is a general recognized principle of commercial law that a vendor cannot rely on a buyer's failure to inspect the goods and to give timely notice of defects, if the vendor has adopted a conduct which is not in conformity with his own duties. Especially, it is generally admitted that the vendor is precluded from asserting the non-conformity of the notice if it has concealed the existence of the defect (see in particular art. 40 of the Vienna Convention). The same principle applies if the vendor gave the buyer specific guarantees regarding the quality of the goods.

(b) In the present case, [Defendant] knew that there had been flaws among the previous deliveries . . . and especially as to the paper that had been delivered . . . It had therefore committed itself to new deliveries of quality and to double check all banknotes . . . It seems however that it did not abide by its duty, as confirmed by the different reports mandated by the Bank . . .

One may therefore consider that [Defendant] accepted to deliver banknotes without having evidenced to the Tribunal that it had performed its duty to inspect. It constitutes a general principle of international contracts that a party cannot claim the violation of a duty to inspect when it has concealed a defect it was aware of.

(c) Secondly, the particular nature of the relationship between the parties. The 1993 Agreement was concluded in a spirit of conciliation. It meant to put an end to past disputes. [Defendant] committed itself to print new series and deliver banknotes that complied with the contractual requirements. The Bank renounced its past claims and even agreed to future contracts with [Defendant]. As to the general spirit of the agreement, it intended to compromise in order to reach a mutual agreement.

(d) Thirdly, the general attitude of [Defendant] in this matter is a further argument. The Tribunal regards as far-fetched that [Defendant] invokes the Bank's delay in order to free itself from a part of its obligation under the 1993 Agreement. [Defendant] adopted indeed a negative conduct, especially since it waited more than two years before it accepted to pay the amount it owed. Even in view of the likely link with the provisional award of a new contract, [Defendant]'s reluctance to promptly settle the outstanding sums, especially the Bank's advance payment, meant that the Bank was reluctant to give notice of defects in a straightforward manner, as the Bank feared that [Defendant] might then refuse to reimburse

the sums due . . . To use the wording of the Bank, it was treated as a hostage and not as a business client. . . .

[17] In these conditions, the Arbitral Tribunal considers that the Bank may not be deprived of its rights and claims arising from the violation of the 1993 Agreement.

Final Award in Case 9479

February 1999

Original in English

Place of arbitration: Paris, France

1988 ICC Rules of Arbitration

First Claimant and Defendant, both Italian companies, were created upon the dissolution of a family partnership specialized in the manufacture of textiles. The former inherited the right to use the registered trademark, whereas the latter was entitled to use the company name only as a means of identifying itself as a corporate entity or as the producer of the fabrics manufactured by it, but not as a trademark. To this end the two parties entered into an agreement giving Defendant clear and detailed instructions on the way in which the company name was to be reproduced on labels and finished items of clothing. This was to avoid confusion between the trademark belonging exclusively to First Claimant and its affiliate, Second Claimant (a company registered in the USA), and the mere right of identification. Claimants accused Defendant of breaching this agreement by reproducing the company name in such a way that customers were misled and that the trademark was depreciated. Accordingly, it claimed compensation. Defendant retorted by requesting that the parties' agreement over use of the trademark be amended in light of the European trademark Directive EEC/89/104, claiming it had suffered hardship since the introduction of this directive. In deciding upon Defendant's counterclaims, the Arbitral Tribunal referred to articles 6.2 (hardship) and 5.8 (duration of contract) of the Unidroit Principles.

Applicable law

'Before dealing with the claims and counterclaims, the Arbitral Tribunal must express its views as to the law applicable to the merits of the dispute, since the parties are in disagreement in this regard.

According to article 13(3) of the ICC Rules of Arbitration: "The parties shall be free to determine the law to be applied by the arbitrator to the merits of the dispute. In the absence of any indication by the parties as to the applicable law, the arbitrators shall apply the law designated as the proper law by the rule of conflict which he deems appropriate."

According to article 13(5) of the same Rules: "In all cases, the arbitrator shall take account of the provisions of the contract and the relevant trade usages."

As a result of these provisions, an arbitral tribunal must first apply the provisions of the contract, in the light of and, in case of need, supplemented by the usages of international trade,

provided the validity of such provisions is not questioned by the parties or [such provisions] do not appear to the tribunal to be incompatible with international public policy in the sense of truly or transnational public policy (see Pierre Lalive, "Transnational (or Truly International) Public Policy and International Arbitration", in ICCA Congress Series No. 3, p. 257). In case the arbitral tribunal does not find in the contract or in the usages of international trade a solution to the problems raised by the parties' claims, it must revert to the law applicable to the contract. If any of the parties contends that one or more provisions of the contract, or the contract as a whole, are null and void, an arbitral tribunal must decide the question by referring to the mandatory rules of the law applicable to the contract or to any mandatory rules which it would be justified to apply, bearing in mind that the applicability of such rules must always be confronted with the real intention of the parties and their legitimate expectations.

In the instant case, the parties have dealt with the problem of the law applicable to the Agreement in its article 12(b) which reads:

In view of the facts that one of the parties to this Agreement and Stipulation is a New York corporation having its principal office in such State, the litigation settled herein took place in New York and this Agreement and Stipulation was negotiated substantially in New York, the parties hereto agree that the law of the State of New York (without regard to its conflicts of law rules) shall determine any dispute relating to the validity of this Agreement and Stipulation.

None of the parties now dispute that the law of the State of New York governs the validity of the Agreement. However, while the Claimants consider that the intention of the parties was that the Agreement be generally subject to the law of the State of New York, [Defendant] proposes a restrictive construction of article 12(b) which would exclude from the province of the law of the State of New York any question which is not stricto sensu a question of validity. In particular, [Defendant] underscores that what it describes as "the restoration to equity of the contract", in fact the main object of its counterclaims, is not governed by the law of the State of New York. It is [Defendant]'s view that, with the exception of the question relating to its validity, the Agreement is governed by Italian law, on the basis of the 1980 Rome Convention regarding the applicable law to contractual obligations, which has been incorporated within the Italian conflict regulations by article 57 of the Italian law of May 31st, 1995.

On the basis of the briefs exchanged by the parties and the oral argument presented by counsel at the ... hearing, the Arbitral Tribunal came to the conclusion that when the parties indicated in article 12(b) of the Agreement that any dispute relating to its validity would be determined according to the law of the State of New York, they were perfectly aware of the restrictive implication of the language that they were using. Indeed, the first draft of the Agreement ... indicates that "the laws of the State of New York shall be the law pursuant to which this Agreement shall be construed and enforced at any arbitration proceedings brought under this Agreement". A comparison of this language and of that of article 12(b) of the Agreement eventually executed in 1987 leads to the conclusion that, after negotiations, the parties agreed to restrict the intervention of the law of the State of New York to questions relating to the validity of the Agreement.

However, contrary to [Defendant]'s submission, this finding does not imply that the parties were contemplating that any other state law would govern their Agreement. On the contrary, their silence after negotiations as to the applicable law indicates that they considered that the intervention of a national law was necessary for problems of validity only. In the context of an ICC arbitration concerning a contract which was supposed to be performed in the whole world that implied intention of the parties is quite reasonable and in perfect conformity with the interpretation of articles 13(3) and 13(5) of the ICC Rules exposed above by the Arbitral Tribunal.

Thus, the Arbitral Tribunal finds that any question concerning the validity of the Agreement must be decided under the law of the State of New York. Any other question will have to be decided according to the provisions of the Agreement in the light of, and, in case of need, supplemented by the usages of international trade. Whenever necessary, the Arbitral Tribunal will have regard to international public policy.

Defendant's counterclaim

(i) The principal counterclaim of [Defendant] is that the Agreement should be modified, only for its effects on the "European Territory", by a substitution of the terms of its article 7(b) with the terms of article 6 of the EEC/89/104 Directive. The Claimants object to such modifications.

By European Territory, the parties mean the territory of the European Union.

[Defendant]'s position

[Defendant] explains that the above mentioned EEC/89/104 Directive, which was issued after the execution of the Agreement in 1987, explicitly allows the owner of a name to use it in its commerce, as long as it does so in a manner consistent with honest and fair principles, even when said name constitutes the trademark of another businessman. Since [Defendant] entered into the Agreement at a time when Italian law (namely the Bima law of 1967) restricted drastically the use of a name as a trademark when such name was used as a trademark by someone else, the liberalization introduced by the European Directive put [Defendant] in a situation of hardship. On the basis of article 6.2 of the Unidroit Principles, [Defendant] is entitled to an equitable modification of the Agreement so that, on the territory of the European Union, [Defendant] might benefit from the liberal solutions resulting from the application of the Directive. As a further justification for its requests, [Defendant] also refers to article 1467 of the Italian Civil Code.

The Claimants' position

The Claimants first stress that the law of the State of New York is applicable to [Defendant]'s request for equitable modifications of the Agreement and that, under the New York law, a Court (or an arbitrator) should not modify a contract because of a change of law, even should this change create additional burdens or advantages for either party. The Claimants, although on a slightly different basis, come to the same conclusion by application of Italian law. In particular, they point out that the entry into force of the EEC Directive cannot be seen as an "extraordinary and unforeseeable event".

The Arbitral Tribunal's position

As explained above, the Arbitral Tribunal has found that the law of the State of New York only applies to the validity of the Agreement and that [Defendant]'s request for equitable modification of the Agreement cannot be characterized as a question of validity of the Agreement. Moreover, the Arbitral Tribunal has found that besides the law of New York, no national law had been made applicable to the Agreement. Thus, since the provisions of the Agreement do not contemplate the possibility of its modifications on equitable grounds, the Arbitral Tribunal will turn to the usages of international trade in order to supplement the provisions of the Agreement. In this respect, [Defendant] has referred to the Unidroit Principles which the Arbitral Tribunal recognize as an accurate representation, although incomplete, of the usages of international trade.

Article 6.2.2 of the Unidroit Principles reads:

There is hardship where the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party receives has diminished, and

- (a) the events occur or become known to the disadvantaged party after the conclusion of the contract;
- (b) the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract;
- (c) the events are beyond the control of the disadvantaged party; and
- (d) the risk of the events was not assumed by the disadvantaged party.

According to article 6.2.3, paragraph 4:

If the Court finds hardship it may, if reasonable,

- (a) terminate the contract at a date and on terms to be fixed, or
- (b) adapt the contract with a view to restoring its equilibrium.

However, these provisions must be read in conjunction with article 6.2.1 which reads:

Where performance of a contract becomes more onerous for one of the parties, that party is nevertheless bound to perform its obligations subject to the following provisions on hardship.

On the basis of the above-mentioned definitions, the Arbitral Tribunal admits that it would be entitled to make an equitable modification of the Agreement, but it is not convinced that [Defendant] is being faced with a situation which may be characterized as "hardship".

Indeed, the issuing of the EEC Directive did not alter in any way the equilibrium of the Agreement among the parties. The situation of [First Claimant] and its affiliates remain unaffected insofar as their entitlement to the . . . trademark is not concerned by the Directive. [Defendant] does not meet any new difficulty in complying with the restriction on the use of the . . . name. As a matter of fact, [Defendant] does not really allege that so would be the case. Indeed, the thrust of [Defendant]'s submission is that since the EEC Directive has been made, the Agreement imposes on the use of the name . . . restrictions which have disappeared from the laws of all countries members of the European Union. As a result, the Agreement, into which [Defendant] entered in order to meet the requirements of the Italian Bima law deprives it of a freedom in the use of the name . . . that it would enjoy in the absence of the Agreement. It is the reason why [Defendant] requests the Arbitral Tribunal to substitute article 7(b) of the Agreement with the terms of article 6 of the EEC Directive as far as its effects on the territory of the European Union is concerned. [Defendant] would obtain more or less the same result with its subordinate counterclaims aiming at obtaining the termination of the Agreement at least as regards its effects in Europe.

The Arbitral Tribunal does not accept the view, expressed by the Claimants, that a change in the law cannot be the source of hardship. It may well be the case, when a new law makes the performance of the contractual obligations of a party more onerous or when the value it receives from the performance of the other party is severely reduced. However, the Arbitral Tribunal has already found that the introduction of the EEC Directive had no effect on the performance of the Agreement by the parties. In reality, [Defendant]'s position, in a nutshell, is that it would have had no reason to enter into the Agreement should the EEC Directive have been introduced before April 1987. This has nothing to do with hardship, which is a notion which may play a role when the performance of a contract is at stake but has no function in the formation of contracts. Even if it is probable that [Defendant] would have entered into the Agreement, as drafted in 1987, after the adoption of the EEC Directive in 1989, a subsequent evolution of the legislative context of a contract does not constitute a hardship when it does not destroy the balance of the parties' respective obligations. Moreover, without denying that the parties had in mind the Italian Bima law when they executed the Agreement, it was not made

to be enforced in Italy only nor in Europe. The Agreement is a global arrangement, due to be enforced in the whole world. This is underscored by the introduction to the Agreement:

Whereas the parties, after extensive negotiations, have agreed that it is in their respective interests and the interest of their Affiliates that the rights of the parties are fixed and determined in a manner which will avoid, as much as possible, future conflicts, with respect to the use of the trademark . . . and create definitive understandings applicable to all jurisdictions in which the parties may so legally contract, and in which their respective products are sold and may be sold and/or distributed.

This language indicates that the parties wanted to enter into a final settlement of their conflicts relating to the use of the trademark . . . by agreeing on an arrangement applicable whenever in the world. This probably explains that they limited the scope of the law of New York to the validity of the Agreement, since its worldwide application was at odds with the intervention of a specific national law to govern its performance.

Irrespective of the fact that the adoption of EEC Directive does not constitute a situation of hardship, [Defendant]'s contention that the Agreement be modified in so far as its effects in the territory of the European Union are concerned is in direct contradiction with the intention of the parties to organize their relations as to the use of the trademark . . . by harmonized solutions applicable in any jurisdiction, whatever be the content of the law in that jurisdiction. [Defendant] is suggesting a balkanization of the Agreement which is incompatible with its very spirit. Should [Defendant]'s approach be followed, there would be no reason not to substitute later on article 7(b) of the Agreement by the provisions of the law of Ruritania, as far as its effects in Ruritania are concerned, if the law of Ruritania was more liberal than the provisions of the Agreement. For the above-mentioned reasons, the Arbitral Tribunal decides to dismiss [Defendant]'s first and principal counterclaim.

(ii) In a subordinate counterclaim, [Defendant] requests the Arbitral Tribunal to terminate the Agreement, due to hardship, at least as regards its effects in Europe.

The Claimants object to that subordinate counterclaim as they do in respect of the principal counterclaims, for very similar reasons. In reality, the termination of the Agreement is one of the two solutions available in case of hardship. As indicated in article 6.2.3, para. 4 of the Unidroit Principles, a Court (or an Arbitral Tribunal) may either terminate a contract or adapt it with a view to restoring its equilibrium.

As the Arbitral Tribunal has found that the existence of a situation of hardship had not been established and as modifying the Agreement, in its scope in the case of partial termination, in view of the evolution of the law in a specific country or in a group of countries is incompatible with the real intention of the parties which wanted a global application of the Agreement, [Defendant]'s subordinate counterclaim must be dismissed as well as its principal counterclaims.

(iii) In a further subordinate counterclaim, [Defendant] requests the Arbitral Tribunal to ascertain and state that, since the Agreement provides for perpetual obligations, [Defendant] is entitled to recede from it and to terminate it, at least as regards its effects in Europe. In its brief of . . ., [Defendant] has clearly specified that its request concerned only the effects of the Agreement in the European Union, stating that "the whole agreement is not put into question, since the scope of the Agreement extends to the entire world". [Defendant]'s position in this respect is that perpetual obligations are valid only when they just reproduce prerogatives existing under the law. Since it is not any longer the case for the restrictions opposed by the Agreement to the use of the name . . . in the European Union, in the light of the EEC Directive, the perpetual obligations deriving from the Agreement are null and void and the Agreement must be terminated for this part of the world.

The Claimants object to that subordinate counterclaim that the perpetuity pointed out by [Defendant] is just the obvious consequence of the potential perpetuity of the right to the trademark, in the sense that the obligations undertaken by the parties on the basis of the Agreement last as long as the trademark. They add that they are the ones which should complain to be obliged to tolerate in perpetuity [Defendant]'s certain behaviour which intrudes upon their exclusive right.

The Arbitral Tribunal must stress at the outset, that it results from the text of the Agreement that the real intention was that its effects would not be limited in time. The preamble of the Agreement indicates that their intention was to "create definitive understandings". This intention is confirmed by provisions such as article 12(b) or 12(c) which endeavour to make its avoidance or termination particularly difficult, if not impossible. Thus, it is indisputable that the Agreement creates perpetual rights and obligations. As rightly observed by the Claimants such indefiniteness of the duration of the Agreement is a direct consequence of the indefiniteness of the duration of the trademark . . . the ownership of which is recognized to [First Claimant], against the recognition of [Defendant]'s rights to use "[name]" for identification purpose only, under specific conditions".

[Defendant] is right when it contends that perpetual obligations may be terminated under many national laws, although its counterclaim is grounded mainly on Italian law. For example, it is worth indicating that article 5.8 of the Unidroit Principles reads: "A contract for an indefinite period may be ended by either party by giving notice a reasonable time in advance". However, the Arbitral Tribunal is not satisfied that [Defendant] is entitled to a termination of the Agreement, effective in the territory of the European Union, as [Defendant] has specified precisely. As a matter of fact, this understandable geographical restriction in the scope of [Defendant]'s request for termination is a symptom of its misconception.

As admitted by [Defendant] . . . , a perpetual obligation is valid when "it merely reproduces legal precepts". The problem is that the parties have deliberately avoided submitting the Agreement to any national law, with the exception of problems regarding its validity for which the law of the State of New York is applicable, in order to facilitate its worldwide application. As a result, it is meaningless to compare the rights and obligations created by the Agreement with any national legal precepts to decide whether they reproduce them or not. Since the introduction of the EEC Directive, the Agreement does not any longer reproduce legal precepts in the territory of the European Union, if it even did in all the member countries, but it may still do so in other jurisdictions or even be more favourable to [Defendant] than the law of such other country, the probable reason why [Defendant] did restrict the effects of its request to the territory of the European Union. Here again, [Defendant] intends to achieve a balkanization of the Agreement which goes directly against the real intention of the parties.

The Arbitral Tribunal's view is that, with the 1987 Agreement, the parties have defined, with a view of its worldwide application, the respective status of the owner of the trademark . . . and of the owner of the name . . . , irrespective of the legal precepts of any national law. Thus, there are no legal applicable precepts to be compared with in order to decide whether the Agreement just reproduces them or not. In such a situation, the Arbitral Tribunal must respect the intention of the parties which is clearly expressed in the Agreement and, as such, does not need to be supplemented by the usages of international trade, unless it would be contrary to international public policy. It is obviously not the case. First, although the right to terminate a perpetual obligation is recognized in many national laws, it does not amount to a rule of international public policy. But, more significantly, such right is generally excluded, as already mentioned, when the perpetual rights and obligations are just a reproduction of legal precepts. Thus, the perpetuity as such cannot amount to a violation of international public policy. After all, it would be enough to find just one national law in the world which embodies legal precepts comparable to those introduced by the parties within the Agreement to validate its perpetual

character under that law. The very fact that the parties chose to organize their relations outside of any national law is not contrary to international public policy as well, as illustrated, for instance, by the provisions of article 1496 of the French New Code of Civil Procedure. Thus, by defining themselves the legal precepts applicable and confirming them in an Agreement with a worldwide scope and an indefinite duration, the parties have exercised prerogatives that the Arbitral Tribunal must recognize. In any case, [Defendant] has never contended that the Agreement was against international public policy, as confirmed by its apparent wish to see it applied outside the territory of the European Union.

On the basis of the above, [Defendant]'s second subordinate counterclaim is dismissed.

Final Award in Case 9594

March 1999

Original in English

Place of arbitration: London, UK

1988 ICC Rules of Arbitration

*Claimant, a Spanish company, agreed to manufacture and install industrial machinery for Defendant, a company based in India. Following the installation of the equipment, various technical problems arose, which led Defendant to withhold the final part of its payment, despite Claimant's efforts to solve the defects and overcome their differences. Claimant began arbitration proceedings in which it claimed that Defendant had breached its contractual obligations and that it should be ordered to pay the outstanding balance of the purchase price and compensation for damage to Claimant's international public image. Defendant responded with a counterclaim in which it accused Claimant of various breaches of contract concerning, amongst other things, equipment defects and delayed performance. It also claimed consequential damages. Under English law, which the parties had chosen as the law applicable to their agreement, the award of damages is subject to the likelihood and the mitigation of the loss. With regard to the second of these limitations, the sole arbitrator referred to article 7.4.8 of the *Unidroit Principles*.*

'The general rule concerning damages under English contract law is that of *restitutio in integrum*: the party who suffered the damages should be put in the same position as it would have been if the contract had been performed. This principle is, however, subject to the following limitations: (1) the degree of likelihood, namely, the types of damage which a contract breaker shall be responsible for and (2) mitigation of the loss, a duty of the party who suffered the damages to limit or altogether avoid the consequences of the breach. (See also Beavan, "Limitations upon Damages in Contract", Legal Executive 1996, July Supplement p. 10, which discusses the three significant limitations to the recovery of damages, namely: the remoteness of damage, causation, and the duty to mitigate loss.)

(1) The degree of likelihood

The requisite degree of foresight which may be attributed to the contract breaker was set by *Hadley v. Baxendale* 9 Excl. 341 as either (a) the damage as may fairly and reasonably be regarded as arising naturally (according to the usual course of events) from the breach or

(b) damages which could have been foreseen by the contract breaker because of special knowledge which he had at the time of making the contract. This rule was restated and revised in *Victoria Laundry (Windsor) Ltd. v. Newman Industries Ltd.* [1949] 2 K.B. 528 and the decision of the House of Lords in *Czarnikow Ltd. v. Koufos* [1969] 1 A.C. 350.

In more recent cases this rule has again been reaffirmed. See *Seven Seas Properties v. Al Essa* [1993] 3 All E.R. 577 and *Kpobraror v. Woolwich Building Society* [1996] 4 All E.R. 119.

These principles are generally stated in section 53 of the Sale of Goods Act, 1979.

It may be presumed that when [Claimant] entered into the Agreement with [Defendant] it knew that [Defendant] wanted to purchase [industrial machinery] to produce parts for their consequent sale to the . . . industry. It was not expressly provided in the Agreement when such [machinery] should be delivered in India and when it should start operating. However, at the meetings and in correspondence between the parties these dates were more or less fixed. There were delays, on some occasions due to [Claimant], on others to [Defendant]. In any event, it may be presumed that [Claimant] knew that delay in the planning scheduled could cause [Defendant] to suffer damages, and that if the machinery did not comply with quality requirements it would have consequences in its productivity. However, it may not be presumed that, when signing the Agreement, [Claimant] knew that [Defendant] was supposed to sell parts to its joint venture partner . . . from a certain date, nor the internal conditions of such joint venture.

[Claimant] could have foreseen that if it did not conclude the whole commissioning process of the machinery within a reasonable time and that if the machinery did not comply with quality requirements, [Defendant] would suffer significant loss. The question is whether [Claimant] could have foreseen that its delay would cause the large amount of loss claimed by [Defendant].

To sum up, both parties are responsible for delays and quality damages to the machinery. While [Claimant] should be held responsible for specific items where it is contractually liable and compensation is awarded to [Defendant], it is difficult, if not impossible, to assign responsibility for consequential damages when both parties share in that responsibility. Furthermore, it is necessary to take into account [Defendant]'s obligation to mitigate the losses as discussed below.

(2) Mitigation of losses

According to McGregor,¹ the rule for mitigation of losses is based on three principles:

- (a) The first and most important states that the plaintiff must take all reasonable steps to mitigate the loss to him consequent upon the defendant's breach and cannot recover damages for any loss he could have avoided but has failed, through unreasonable action or inaction, to avoid.
- (b) The plaintiff can recover for loss incurred in reasonable attempts to avoid loss.
- (c) The plaintiff cannot recover for avoided loss.

Concerning the first rule, the law requires the plaintiff to take all reasonable steps to mitigate the loss consequent on the defendant's breach, and refuses to allow him any loss which is due to neglect to take such steps. This rule is illustrated in the leading case of *British Westinghouse Co. Ltd. v. Underground Electric Ryhs Co. of London Ltd.* [1912] A.C. 673 at 689, where Lord Haldane stated the following:

The fundamental basis is thus compensation for pecuniary loss naturally flowing from the breach; but this first principle is qualified by a second, which imposes on a plaintiff the duty

¹ *McGregor on Damages*, 15th edition, 1988.

of taking all reasonable steps to mitigate the loss consequent on the breach and debars him from claiming any part of the damage which is due to his neglect to take such steps.

The plaintiff's duty to mitigate is not a duty to himself but to the defendant, as specified by Lord Pearson in *Darbishire v. Warren*: [1963] 3 All E.R. 310.

The true meaning is that the plaintiff is not entitled to charge the defendant by way of damages with any greater sum than that which he reasonably need to expend for the purpose of making good the loss. In short, he is entitled to be as extravagant as he pleases but not at the expense of the defendant.

On the other hand the nature of the mitigation of damage has been defined as a question of fact and not a question of law in *Payzu Ltd v. Sanders* [1919] 2 K.B. 581.

A similar standard has been established internationally, primarily in the Unidroit Principles of International Commercial Contracts (1994) which state in sub-section (1) of article 7.4.8 as follows:

The non-performing party is not liable for harm suffered by the aggrieved party to the extent that the harm could have been reduced by the latter party's taking reasonable steps.

This brings us back to an examination of whether [Defendant] took all reasonable steps to mitigate the loss consequent to [Claimant]'s breach of quality/delay. In its closing brief, [Defendant] argued that it acted to mitigate its loss by accepting the machinery since should it have rejected the machinery it would have certainly incurred much greater losses. However, [Defendant] did not seem to consider the possibility of mitigating its loss through negotiation and accommodation. [Defendant] should have accepted the offers made by [Claimant] after the commissioning to sign a provisional acceptance of the line.

In *Payzu Ltd. v. Sanders* [1919] 2 K.B. 581, Lord Scrutton indicated that according to his experience in considering what steps should be taken to mitigate the damage, continued relations with the party in default should be included. Likewise, he compared service and commercial contracts pointing out that "in commercial contracts it is generally reasonable to accept an offer from the party in default".

In any event, supposing [Defendant] could have deemed this offer unacceptable (though it was not), what did [Defendant] do to effectively mitigate its losses?

[Defendant] continued using the machinery to produce a large amount of parts, in spite of its alleged collapsing state, and it cannot be said that [Defendant] took serious measures to repair the defects in the [machinery]. Only when . . . and . . . carried out their studies for the purpose of this arbitration in October 1997, more than a year after [Claimant] had left India, were those problems dealt with. [Defendant] had ample opportunity to mitigate its losses at an earlier stage and it only took reasonable steps to do so once these arbitration proceedings were filed.

Several cases illustrate this rule. In *Simon v. Pausons & Leafs* [1993] 38 Com. Cas. 151 (C.A.) the plaintiff ordered certain material from the defendant which he promised to stock for the plaintiff, but he failed to do so, as a result of which, the plaintiff lost an appointment as maker of clothes to a school. The Court of Appeals refused to award her damages for such loss of appointment because, *inter alia*, she knew of the defendant's breach and had opportunity to buy equivalent material but made not attempt to do so. In *Tucker v. Linger* [1882] 21 Ch. D. 18, a landlord failed to supply materials to the tenant (in breach of covenant) to repair the premises and the tenant failed to recover for damages caused to crops in his barn due to bad weather because the barn had not been repaired, since he ought to have provided himself with materials to carry out the repair and charge the landlord with its price.

Under these circumstances recovery of losses due to [Claimant]'s alleged breach of quality is not granted since the losses were mitigable and could have been contained by [Defendant] through either further negotiation (by accepting [Claimant]'s offer) or by having taken the timely steps required to repair the machinery.'

Final Award in Case 9651

August 2000

Original in English

Place of arbitration: Zurich, Switzerland

1988 ICC Rules of Arbitration

Claimant, a German company, entered into an agreement with Defendant, an Indian company, to supply the latter with industrial equipment. The parties subsequently signed a further contract for a related automation system. 15% of the price of this contract was to be paid immediately and the balance in successive instalments by way of promissory notes. Disputes arose between the parties following the loss of the promissory notes, delayed delivery of the equipment and malfunctions. Defendant stated its wish to return the automation system, upon which Claimant filed its Request for Arbitration. The first issue dealt with by the Arbitral Tribunal in its majority award was that of the applicable law. The parties' contract contained a section 5, entitled 'Law and Arbitration', worded as follows:

The law of Switzerland shall be applicable to this contract and accordingly this contract shall be subject to and construed in accordance with Swiss law.

All disputes arising in connection with this contract, shall be first tried to be settled in a friendly manner between the Buyer and the Seller. If an agreement cannot be reached, the dispute will finally be submitted for Arbitration to the International Chamber of Commerce, the court to be seated in Zurich, Switzerland. The arbitration committee will apply its rules and regulations and the Parties will accept the arbitration award as binding.

*In interpreting this clause, the Arbitral Tribunal referred to articles 1.7, 2.15, 3.8, 3.9, 4.1 and 4.2 of the *Unidroit Principles*.*

'What is the law applicable?

[1] The Parties have filed, for Claimant, a "Submission on the Question of Applicable Law" dated 15 October 1998, with annexure [sic] and for Defendant a "Submission" of 14 August 1998 supplemented by a file containing seven English cases, as well as the following texts:

- The Principles of European Contract Law, 1997
- EC Convention on the Law Applicable to Contractual Obligations, Rome, 1980
- Principles of International Commercial Contracts, 1994, Unidroit
- UNCITRAL Notes on Organizing Arbitral Proceedings
- Convention on the Law Applicable to International Sales of Goods, The Hague, 1955
- Convention on the Law Applicable to Contracts for the International Sale of Goods, The Hague, 1986
- United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, New York, 1958.

Hearings were held in Zurich on . . . to hear Parties on this issue. Both Counsel requested only an "indication" on this point, not necessarily an award. . . . After extensive deliberation, the Arbitral Tribunal instructed the Parties . . . that they would have to structure their case on the tentative assumption that Swiss law would be held applicable, and they so did.

[2] When preparing this Award, the Arbitral Tribunal reconsidered the question of applicable law and we found as follows.

Position of the Parties

...

Claimant's case

[3] Claimant contends that the seat of the arbitration being in Zurich entails that the 12th chapter of the Swiss Private International Law of 18 December 1987 [hereafter PIL] is applicable, and notably article 176, para. 1 PIL, which provides that "The provisions of this chapter shall apply to all arbitrations if the seat of the arbitral tribunal is situated in Switzerland and if, at the time when the arbitration agreement was concluded, at least one of the Parties had neither its domicile nor its habitual residence in Switzerland".

The two requirements of article 176 PIL are met in this case, namely

- a) Parties have chosen Zurich for seat of the Arbitral Tribunal . . .
- b) Parties have neither their domicile nor their habitual residence in Switzerland.

[4] Claimant further cites article 187, para. 1 PIL, providing that "The Arbitral Tribunal shall decide the case according to the rules of law chosen by the Parties".

[5] Claimant also points to article 13, para. 3 of the ICC Rules of Conciliation and Arbitration of 1 January 1988 (applicable under . . . the Terms of Reference agreed upon by the Parties . . .). This provision reads as follows:

The Parties shall be free to determine the law to be applied by the arbitrator to the merits of the dispute. In the absence of any indication by the Parties as to the applicable law, the arbitrator shall apply the law designated as the proper law by the rule of conflict which he deems appropriate.

[6] It is Claimant's case that the principle of party autonomy, allowing the Parties to choose the law applicable to the merits, is both a tradition of Swiss law and a general principle of conflicts of laws. Claimant cites the ICC Interim Award of 16 November 1984¹ to show that this principle has already been applied in the case of a litigation between a US supplier and an Indian buyer.

[7] Claimant further contends that the choice of law by the Parties has to be regarded as determinative as to all aspects of their dispute, and namely also as concerns the possible nullity of the Contract for misrepresentation (as has been pleaded on behalf of the Defendant).

Defendant's case

[8] Defendant states its case on the merits to be on the basis that Claimant obtained the Contract by fraud and material misrepresentation, further that the performance certificates were also obtained by fraud, and that Claimant is guilty of a fundamental breach of contract. These issues would require to be resolved in accordance with Indian law and/or in accordance with the principles of justice, equity and good conscience.

[9] Defendant also accepts that a contract can indicate a choice of law by the parties. However, it states that there may be exceptions on the grounds of public policies. Further,

there are accepted limitations on the choice of law by the parties. Now in the present case, according to the Defendant, the Contract has the closest connection with India.

[10] As concerns the reissue of promissory notes, such a claim is based on general principles of law, and on principles of justice, equity and good conscience, but not, according to Defendant, on any clause of the Contract. However the Arbitral Tribunal shall not discuss that issue further, as Claimant no longer claims for reissue of the promissory notes.

Claimant now requests an order for payment of the Contract price . . . This claim is undoubtedly based on the Contract . . .

[11] As concerns its own claims, Defendant and Counter-Claimant insists that they are based essentially on allegations of misrepresentation and fraud in obtaining the Contract. The negotiations, pre-contractual and post contractual, were conducted mostly in India. If misrepresentation and/or fraud are alleged to have been made in India, Indian law would apply rather than Swiss law, all the more so because an Indian company needs various permissions to enter into such contracts as the one under consideration at present, and a number of representations made by the foreign party are carried by the Indian party to the Indian Government.

[12] Moreover, where one of the Parties claims that the Contract itself is tainted by fraud, it would be incongruous to decide this issue by reference to the contractual choice-of-law clause.

[13] Finally, Defendant submits that the principles of justice, equity and good conscience should apply. Fraud is accepted in all civilized jurisprudences. The principles of Unidroit on International Commercial Contracts are a useful guide in relation to such principles of justice and equity as are internationally acceptable.

Findings of the Arbitral Tribunal

[14] The rule under Swiss Law is that the interpretation of a choice-of-law clause is subject to the law chosen by the parties (article 116, para. 2 *in fine* PIL).² The true intent of the legislature may be apparent from article 118, para. 1, second sentence of the 1978 draft to the PIL: (translation: "The [choice-of-law] is subject to the law of which the choice is in issue").³

Law applicable to the choice-of-law clause

[15] Now, Article 116, para. 2, second sentence is innovative, in the sense that the case law anterior to the 1987 PIL seems to have entertained the notion that the *lex fori* would be applicable to the choice of law. Therefore, it is no longer possible indiscriminately to rely on the cases published before 1 January 1989 (entry into force of PIL of 18 December 1987) and notably on ATF 79 II 295. As a consequence, modern commentary is to the effect that the principle of party autonomy, its extent and its limitations, are governed by the law chosen by the parties.⁴

[16] Therefore, the applicable law to the interpretation of the Section 5 of the Contract is the Swiss law as the law chosen by the Parties.

[17] Abroad, the more traditional approach to this question seems to have been, at least in the past, that the *lex fori* would be applicable to the construction of the choice-of-law clause.⁵

[18] Finally, international arbitral awards sometimes refer to a "transnational rules on conflicts of laws".⁶ Presumably, if found to exist on that particular point, such a "transnational rule" might indicate as applicable to construe a choice-of-law clause either the law chosen by the parties or the *lex fori*.³

² See M. Keller/J. Kren Kostkiewicz, *IPRG Kommentar* (Zurich, 1993) no. 54 *et seq.* on art. 116 PIL.

³ See Keller/Kren Kostkiewicz, *op. cit.*, no. 56 on art. 116.

⁴ See B. Dutoit, *Commentaire de la loi fédérale du 18 décembre 1987*, 2d ed., Basel 1997, note 14 on art. 116.

⁵ See e.g. Paul Lagarde, in *Colloque de Fribourg relatif au projet suisse de loi fédérale sur le droit international privé*, Fribourg 27-28 April 1979 (Zurich 1979) p. 46, para. 1(a) *in fine*. This appears also to be the English rule of law . . . , thus presumably the Indian rule as well.

⁶ See e.g. ICC award no. 1434 (Collection of ICC Arbitral Awards 1974-85, p. 264).

⁷ See in that sense art. 8, para. 1, of the Rome Convention of 1980, to which Switzerland is not party, and below no. [25] (c).

⁸ For example in *Dallal v. Bank Mellat* [1986] Q.B. 441, the agreement to refer an existing dispute to arbitration was held to be governed by the *lex fori* (seat of the arbitration) (which is admittedly a slightly different question). In *The Hollandia* [1983] 1 A.C. 565 (577), the House of Lords held that the (English, that is the *lex fori*) Carriage of Goods by Sea Act 1971 had the effect of prohibiting an express choice of foreign law where it had the effect of lessening the carrier's liability. This is also a slightly different question . . . However, both cases point to the rule that under English law, the law of the forum may apply to the scope of the arbitration and to the interpretation of the choice-of-law clauses.

[19] Whatever the method that would be followed, Swiss law is applicable in the present case to the interpretation of section S of the Contract, since Parties opted for the Swiss law to govern their Contract and the *lex fori* is that of Switzerland as seat of the arbitral tribunal under a clause on the resolution of disputes that is not the object of any controversy between the Parties, save for the present question of the applicable law.

Principle of interpretation under Swiss law

[20] It is a tenet of Swiss law that no interpretation is necessary when the true and common intent of the party is clearly expressed in the Contract.⁹ Article 4.1 of the Unidroit Principles also refers to the common intent of the parties.

However, the governing principle for the interpretation of any declaration of intent is the so-called "principle of confidence" ("Vertrauensgrundsatz", "principe de la confiance")¹⁰ under which a seemingly clear wording may be shown not to convey the true intent of the parties.¹¹ According to that principle, the declaration is neither understood in the sense of what the declaring party may have had in mind nor in accordance with the literal sense of the wording, but in the meaning which the addressee could in good faith attribute to it. As good faith requires the addressee to consider all aspects allowing the understanding of the declared intent, the wording is not the only test.¹² Article 4.2(2) of the Unidroit Principles provides for the same test, article 1.7 of the same Principles imposing further the overriding duty of good faith.

Proper interpretation

[21] In the present case, there is a clear wording: under para. 1 the "Contract" is the subject matter of the agreement and is subject to Swiss law, whereas para. 2 concerns "all disputes arising in connection with the agreement". That seems at first sight to leave no doubt as to the interpretation of section S. Nonetheless, as the Parties may or may not have thought that a dispute might involve something else than a contractual issue, the wording alone is not decisive.

[22] As Counsel for Claimant was questioned on that very wording during the hearing held... in Zurich, her answer was that the wording of that clause was standard. Under "Contract" should be understood everything which is connected with the Contract, also including the conclusion of the Contract and precontractual negotiations. Counsel for Defendant, on the other hand, declared that there is a marked difference between the two paragraphs of Section S.

[23] Now, under the principle of confidence, would not a reasonable businessman reading section S in its entirety think that all disputes arising in connection with the said agreement should be governed by the law chosen by the Parties in the preceding paragraph? All those disputes should certainly be referred to arbitration. In fact, it is not obvious that reasonable businessmen would be alert to the difference between a "contractual issue" and "an issue arising in connection with a contract".

Furthermore, it would appear somewhat strange if businessmen would, as a matter of common intent, choose two different laws to rule on their relationship, to wit the law of the Contract and some other law for the negotiation of the agreement.

Finally, it might be well assumed that a reasonable businessman would consider that a wrongful act which would allegedly have been committed during the negotiation of the Contract would be related more closely to the contractual side of the case.

In this regard, it will be noted that under Swiss law, the most authoritative commentary is to the effect that precontractual liability is not a case of tortious liability, but a case of contractual liability subject to article 97 CO rather than article 41 CO, or a case of *sui generis* liability.¹⁵

⁹ See e.g. ATF 111 II 457.

¹⁰ See ATF 111 II 287 (the principle of confidence applies in any event).

¹¹ E. Bucher, "Law of Contracts" in E. Dessenmontet & T. Ansay, eds., *Introduction to Swiss Law* (The Hague, Boston, London, 1997) p. 140.

¹² See E. Bucher, *op. cit.*

¹³ Von Tuhr Peter, *Allgemeiner Teil des schweizerischen Obligationenrechts*, vol. I (Zurich, 1974) p. 193; P. Engel, *Traité des obligations en droit suisse*, 2d ed. (Berne, 1997) pp. 751-752, with many quotations for the various views on p. 749.

The Arbitral Tribunal does not have to decide on this particular controversy at that point in time. The controversy itself is, however, sufficient to show why reasonable businessmen would understand section 5 of the agreement as not dividing the disputes arising “in connection with” the Contract into two categories, to wit the “contractual ones” and the “precontractual ones”, even if they were to be alert to the difference between “contractual issues” and “issues arising in connection with the contract”, which is uncertain.

[24] Therefore, the Arbitral Tribunal finds that section 5 contains a choice-of-law clause that is also intended to bear on any issue relating to the conclusion of the Contract.

Severability of the choice-of-law clause

[25] Is the choice of law clause severable in the sense that it is not tainted by any possible misrepresentation or fraud as to the main contract?

(a) The doctrine of severability of the arbitration clause is generally admitted nowadays, in the sense that the validity of the arbitration clause is independent from the main contract.

(b) The issue before us is whether the choice-of-law clause is also to be applied where the whole contract is alleged to be vitiated by fraud or misrepresentation.

One authority has been cited by Claimant.¹⁴ Another authority states that “Parties do not expect that on issues of formation and validity of the choice-of-law agreement, a law other than the chosen law could apply (...) Both the *lex fori* and the objectively determined *lex causae* should be excluded in that regard (...) the objective *lex causae* because the parties did not want to have it applied to their contract.”¹⁵

In fact, such independence of the choice-of-law clause had been recognized a long time ago by the Federal Tribunal.¹⁶ It explains the solution that the legislature adopted in article 116, para. 2 PIL: “because the contract choosing the applicable law is independent from the main contract”,¹⁷ it is well possible that the form requirement governing the choice-of-law clause might be different from the form requirement governing the main agreement. Very well-known authors also state that “the law which (if the choice-of-law as made by the parties is not vitiated) is to govern the contract determines if the choice-of-law clause is valid or invalid, for example because of mistake, misrepresentation or fraud”,¹⁸ or that “claims for *culpa in contrabendo* and other claims relating to the formation of the choice-of-law clause fall under the law selected by the parties”.¹⁹

Therefore, the severability and independence of the choice-of-law clause is a well-settled principle of Swiss international private law. Thus, Swiss commentary is to be followed when it states that the law chosen by the Parties is applicable even to the question whether the will of the parties was vitiated.²⁰

(c) Assuredly, the question was put to the Arbitral Tribunal by Counsel for Defendant whether Swiss law should apply to the question whether Swiss law governs the choice of law. Counsel for Defendant termed this to be a *circulus vitiosus*. However, this logical difficulty is only apparent. The principle of party autonomy is recognized by all the legal orders that are connected with the present contract, be it the German, the Indian or the Swiss legal order. The decision in *Vita Food Products Inc. v. Unus Shipping Co. Ltd.*²¹ on which Defendant relied, allows party autonomy, as does article 116 PIL and article 27 of the German law on international private law of 25 July 1986 (following art. 3 of the Rome Convention). The principle of party autonomy is also recognized in international arbitration.²² Further, there seems to have been no decided case in England striking down a choice of law because it would not be “*bona fide* and legal”.²³ Therefore, the party autonomy seems to be really unrestricted in spite of the limitations that were mentioned by Lord Wright in the *Vita Food* case.

¹⁴ P. Karrer, *Das IPR der IPRG-Schiedsgerichte in der Schweiz*, in *Schiedsgerichtsbarkeit* p. 333.

¹⁵ Keller/Kren Kostkiewicz, [op. cit.] no. 54 on art. 116.

¹⁶ See e.g. ATF 102 II 145: “This agreement is a so-called choice-of-law clause [“*Verweisungvertrag*“], which determines the law applicable to the main contract, but which must be distinguished from that contract and is to be judged on its own”. This is still valid under the PIL: see e.g. Amstutz, Vogt, Wang, *IPRG, Basler Kommentar*, 2d ed. (1996) no. 32 on art. 116 PIL.

¹⁷ I. Schwander, “Zur Rechtswahl im IPR des Schuldvertragsrechts” in *Festschrift Max Keller* (1989) p. 474; see also B. Dutoit, [op. cit.] no. 15 *in fine* on art. 116 PIL; according to Keller/Kren Kostkiewicz, [op. cit.] no. 52-53 on art. 116 PIL, the same solution would apply in Germany.

¹⁸ See F. Vischer, “Das Internationale Vertragsrecht nach dem neuen schweizerischen IPRG-Gesetz”, *Basler Juristische Mitteilungen* (1989) p. 194.

¹⁹ I. Schwander, [op. cit.] p. 482.

²⁰ Keller/Kren Kostkiewicz, [op. cit.] no. 59 *in fine* on art. 116 PIL.

²¹ I. Schwander, [op. cit.] at 481-482.
²² R. P. Umbricht, *Die immanente Schranken der Rechtswahl im internationalen Schuldvertragsrecht* (thesis, Zurich, 1963) p. 75, no. 14, states that no case decided the question (until then, 1963, of course).

²³ [1939] A.C. 277.

²⁴ See e.g. W. L. Craig, W. W. Park, J. Paulsson, *International Chamber of Commerce Arbitration*, 2d ed. (New York, Paris, 1990) p. 123, citing awards in cases 5505 and 4145 (resp. *Collection of ICC Arbitral Awards 1986-1990* p. 151-152 and *Collection of ICC Arbitral Awards 1974-1985* p. 559).

²⁵ See *Dicey and Morris on The Conflict of Laws*, 11th ed. (1987) p. 1172.

Now, party autonomy must be respected even where there was allegedly misrepresentation or fraud in the conclusion of the agreement. The first law to apply to the existence and validity of the choice-of-law contract is therefore the law "which would govern it ... if the contract or term were valid" (art. 8, para. 1 of the Rome Convention on the Law Applicable to Contractual Obligations of 1980; see to the same effect article 116, para. 2, 2d sentence PIL; the same solution was already adopted in article 2 III of The Hague Convention on the law applicable to the international sale of movable property of 1955). It is only if "it appears from the circumstances that it would not be reasonable to determine the effect of [a party's] conduct in accordance with" that law that the law of this party's residence might apply (art. 8, para. 2 of the Rome Convention). Therefore, Swiss law is properly to apply to the question of the validity of the choice-of-law clause.

(d) Besides, it will be noted by way of superabundance that the English approach, if it were to be followed, would not entail a different solution.

According to a "decision of the Court of Appeal which is not without its difficulties",²⁴ *Mackender v. Feldia A.G.*,²⁵ a choice of foreign law might not be effective in England if by English law there had been no *consensus ad idem* ("e.g. because of the plea of *non est factum*, or, perhaps, of fraud").²⁶ But even if the English rule referring to the *lex fori* would appear to be different from the Swiss one, the result would be the same, because Switzerland is the forum in the present case. It has been explicitly stated ... by Counsel for Defendant that Defendant did not contest the validity of the arbitration proceedings; the seat of the arbitral tribunal being in Switzerland, Swiss law shall apply to the question of fraud whether the Swiss law of conflict (art. 116, para. 2 PIL) or the English rule of the *lex fori* applies.

(e) Finally, it deserves mention that article V(i)(a) of the New York Convention on the Recognition and Enforcement of Arbitral Awards allows for a rejection of the arbitral award, among other grounds, when the agreement to arbitrate is not valid under the law which the parties have chosen. This shows that a concept common to all civilized jurisprudence is that the choice of law shall be respected even if the contract is alleged to be null and void for fraud or misrepresentation.

(f) While finding that Swiss law applies, the Arbitral Tribunal is however aware that the issue of fraud and misrepresentation would not be adjudicated otherwise were Indian law to be found to apply on these issues. Indeed, as has been said already, the avoidance of a contract for wilful deception is a common understanding of all civilized jurisprudence. For example, article 2.15(2) of the Unidroit Principles provides that "a party who negotiates or breaks off negotiations in bad faith is liable for the losses caused to the other party". Article 3.8 provides for avoidance of a contract by a party in case of fraudulent misrepresentation or fraudulent non-disclosure of circumstances which, according to reasonable commercial standards of fair dealing, the other party should have disclosed. Article 3.9 provides for the avoidance by reason of a threat leading a party to conclude the contract. Further, principles of justice, equity and good conscience will be legitimately applied by the Arbitral Tribunal for the purpose of determining the scope and manner of applying the law, and what should be the nature and extent of the relief to be granted, as those principles are referred to in Swiss law (see e.g. art. 4 Civil Code and art. 42, para. 2 CO).²⁷

²⁴ *Dacey & Morris* p. 1177.

²⁵ [1967] 2 Q.B. 590.

²⁶ *Dacey & Morris* p. 1177.

Final Award in Case 9753

May 1999

Original in English

Place of arbitration: Brussels, Belgium

1988 ICC Rules of Arbitration

An agreement was made between Claimant, a British company representing a consortium, and Defendant, a Czech state entity, to secure financing for the development of a location in the Czech Republic. The agreement covered the preparations and discussions prior to the possible conclusion of a contract relating to actual development. The agreement was governed by Czech law. Differences arose between the parties, leading Claimant to initiate arbitration proceedings in which it requested the sole arbitrator to confirm that the agreement was valid and binding on both parties, to declare that Defendant had breached the terms of the agreement and to order Defendant to perform its obligations under the agreement. Defendant contested these claims. It considered the agreement to be void since the consortium was not a legal entity. It also questioned the validity and the nature of the agreement. After dealing with these points and deciding that the parties had entered into a valid and binding agreement the purpose of which was essentially for the parties to cooperate with each other, with a view to the development of the location in question, the sole arbitrator turned to the alleged breach of contract and its consequences and referred to articles 1.3 and 1.7 of the *Unidroit Principles* in support of his findings.

[1] The Claimant alleged that the Defendant did not meet its obligations under the Agreement and requested the Arbitrator to declare the breach of contract, to direct the Defendant to specific performance or to oblige it to pay damages. The Defendant denied the breach of contract and requested dismissal of the claim.

...

[2] On ... a meeting was held between the parties and doubts were raised by the Defendant as to the binding character of the Agreement and the status of the Claimant. The Claimant in a letter dated ... sent to the Defendant referred to these doubts stating that "Clearly there are misunderstandings relating to the intent of the *pactum de contrabendo* in particular and its construction and obligation placed upon both parties." ...

[3] The Defendant's general director in the letter dated ... addressed to the legal representative of the Claimant stated: "[Defendant] consider[s] the above-mentioned '*pactum de contrabendo*' legally irrelevant, as the facts (matters) agreed to in the above-mentioned agreement were not fulfilled at the time given therein, and although not due to the fault of any of the parties this agreement is at the present time unenforceable. Following the successful procurement of the architectural study of locality, [Defendant] shall proceed in two stages. In the first stage it intends to seek by the form of a tender a suitable firm who shall prepare the project offering the best solution for the area and satisfying the needs of [Defendant] and the City of ... In the second stage there would be a shorter form of tender which should result in the appointment of an investor. ... [Defendant] do[es] not exclude the cooperation with [Claimant] or its advisors in the process of fulfilment of the above-mentioned conditions."

[4] During 1994 the legal representatives of the Parties tried to reach an agreement on the legal assessment of the Agreement of 1992 but without success. The Defendant expressed doubts whether the Agreement was binding. The letter dated ... sent by the head of legal

department of the Defendant to the Claimant's legal representative contained the following sentences: "What is new for [Defendant] is a note contained in the Memorandum to the effect that [...] Consortium as a party to the *pactum* has no legal personality under English law and that the member firms in such association agreed that [Claimant] (which is not a party to the *pactum*) would negotiate with [Defendant] on behalf of them. In accordance with Czech law a conclusion can be drawn on the basis of such fact that the *pactum* may not legitimately have come into existence for the party described therein lacks legal personality, *i.e.* does not have any rights or obligations thereunder. The position of [Claimant] towards [Defendant] is the same. The firms associated in the [...] Consortium are not parties to the *pactum* either. If they authorized [Claimant] to represent their interests including conclusion of contracts, they will at first have to assess the quality of representation and services expected to be provided to them by [Claimant]. In spite of the views regarding the *pactum de contrabendo* not being shared in full, [Defendant] [is] still ready to continue the intended co-operation in commercial plans provided that the first step towards new cooperation should be reaching an agreement regarding legal opinion in respect of the *pactum* and looking to solutions both in legal and real terms"...

[5] The Parties could not come to an understanding on these points and negotiations stopped.

[6] The Defendant has confirmed several times its willingness to cooperate with the Claimant but it did not accept the validity and binding force of the Agreement referring to several problems such as the existence of the Consortium which was known to the Defendant since several years. This behaviour meant in reality refusal to cooperate.

The Arbitrator has taken into consideration that under paragraph (1), section 264 of the Czech Commercial Code in determining the rights and duties arising from a relationship of obligations, account is also taken of the business practice (trade usage) prevalent in a particular field of business, unless these are contrary to the contents of the contract or to the law. There are no special usages in the particular field of business but general principles of business practice have importance, too. Such general principles are *pacta sunt servanda* and to cooperate in good faith (articles 1.3 and 1.7 of the Unidroit Principles of International Commercial Contracts, Ph. Kahn, "Les principes généraux du droit devant les arbitres du commerce international", *Journal du droit international* 2, 1989, p. 327). Fair business conduct is one of the main principles of the Czech Commercial Code too (section 265).

On the basis of the above-said the breach of the agreement by the Defendant has been stated.

[7] According to section 365 of the Czech Commercial Code: "A debtor is in default if he fails to perform his obligation duly and in time until the obligation is duly performed, or until the obligation is discharged in another manner. However, the debtor is not in default if he is unable to perform his obligation due to the default by the creditor."

[8] The Defendant alleged that the Claimant did not fulfil its obligation. However, taking into consideration the documents submitted by the parties it can be stated that the basic problem of the realization was in the administrative field, in obtaining the necessary permits for the construction, the administrative conditions of the realization of the project were missing. The letters of the Defendant in ... leading to the arbitration proceedings did not refer to any default by the Claimant but challenged the validity of the Agreement. Therefore, the Arbitrator considered that the allegation of the Defendant was irrelevant from the point of view of the present case.

[9] On the basis of the above points the Agreement is considered as valid and binding upon the parties. During the proceedings no one of the parties has stated that the project has

become impossible and there is no evidence of the impossibility in the documents submitted by the parties either.

[10] According to section 366 of the Czech Commercial Code: "Unless the law provides otherwise with regard to individual types of contracts, a creditor may insist on proper performance of an obligation by the debtor while the latter is in default on his performance."

[11] Consequently, the Claimant is entitled to request performance of the obligation meaning in the present case continuation of collaboration and cooperation with the aim of realizing the project and is entitled to request preferences as specified by the Agreement. However, as it is decided above, the parties are not bound to conclude a contract as in the case of a *pactum de contrahendo* under the rules of the Czech law. The Defendant has referred to the statute of limitations with respect to the request concerning the conclusion of the future contract. The request for performance of the obligations to cooperate and to give preference are not statute-barred (sections 387, 392, 403 Czech Commercial Code).

[12] The Claimant presented its request for damages in an alternative way. As the Defendant is obliged to perform its obligations according to the first request of the Claimant, it is not dealt with whether the Defendant should be obliged to pay damages in accordance with the alternative request, presented in view of the possible dismissal of the first request.

Preliminary Award in Case 9759

August, 1999

Original in English

Place of arbitration: Paris, France

1988 ICC Rules of Arbitration

Claimant, a financial institution based in a European country (X), and Defendant no. 1, a company based in a South-West Asian country (Y), entered into a credit agreement, which was guaranteed by Defendant no. 2, also based in country Y. In order to recover repayments due to it, Claimant initiated arbitration proceedings, on the basis of a clause in the credit agreement entitled 'Law and Jurisdiction' (article 14). According to this clause, the credit agreement was to be governed by and construed in accordance with the law of country X and any disputes arising out of it that could not be readily settled by mutual agreement were to be 'submitted to the International Chamber of Commerce for settlement under their rules and regulations, in Paris'. Defendants contended that this clause did not constitute a valid arbitration agreement. This was the first question that the arbitral tribunal addressed in its preliminary award. In interpreting the arbitration clause it referred to articles 1.6(2) and 4.5 of the Unidroit Principles.

[Defendant No. 1]'s position

[Defendant No. 1] contends that (i) there exists no arbitration agreement under the provisions of the Credit Agreement and (ii) alternatively, such arbitration clause is invalid under the rules and practices of international arbitration.

[Defendant No. 1] contends that the Credit Agreement contains no arbitration agreement

since no reference to arbitration as a mode of settlement is made under article 14.2 of the Credit Agreement. Furthermore, the reference to the ICC Rules and Regulations is not a sufficient indication since it does not specify what exact mechanism of settlement of disputes within ICC is referred to: no guidance was given as to which of conciliation or arbitration mechanism had been agreed upon . . .

[Defendant No. 1] further refers to legal authors who indicate that a clear expression of intent, not only to arbitrate but also to have the arbitration take place under the ICC Rules, is required. [Defendant No. 1] also refers to the ICC Model Clause and to article II of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards to conclude that article 14.2 contains no express reference to arbitration as a mode of settlement of disputes . . .

[Defendant No. 1] adds that, contrary to Claimant's allegations, there exists no common will of the parties for arbitration under the provisions of the Credit Agreement since "there is no explicit or even implicit expression by the parties of their consent on that issue" . . . It contends that the parties' consent should have been given in writing and that the wording should have been precise and exact on the real intention of the parties, *i.e.* no ambiguity and no doubt about the parties' intention. It concludes that article 14.2 does not respond to any of these requirements and no provision of article 14.2 leads to the conclusion that the real intention of the parties was to solve their dispute by way of arbitration . . .

[Defendant No. 1] adds that it is to [Claimant] to prove the existence of an arbitration agreement and to demonstrate that the proper interpretation to be given to the provisions of said article 14.2 is such that it should be deemed to establish the common will of the parties to arbitrate . . . [Defendant No. 1] contends that, in the instant case, there is no fact, even *prima facie* evidence, that it could operate in a way to suggest a reversal of the burden of proof . . .

Alternatively, should the Tribunal decide to interpret the provisions of article 14.2 of the Credit Agreement as constituting an arbitration agreement, [Defendant No. 1] contends that article 14 of the Credit Agreement contains pathological elements:

- an ambiguity results from the fact that it is not specified whether the dispute shall be settled by ICC Rules of Conciliation or Arbitration;
- while article 14.2 provides for the submission of any dispute between the parties to the ICC, article 14.3 reserves the right of [Claimant] to start any legal proceeding for the protection of its right in the courts of [country Y];
- the parties have combined submission of their dispute to the ICC and to a state jurisdiction. Article 15(1)(5) of the Credit Agreement provides that said Agreement once signed "shall constitute legally valid and binding obligations, and that if necessary the Bank [[Claimant]] could enforce judicially the said obligation in [country Y]" . . .

[Defendant No. 1] contends that, in view of this ambiguity, judicial proceedings should prevail as an incontestable proceeding left for the parties to settle their dispute. It further refers to the legal opinion dated . . . whereby judicial proceeding should be considered as the main way of resolving disputes provided by the parties . . .

[Defendant No. 2]'s position

[Defendant No. 2] contends that article 14.2 does not constitute an arbitration agreement, and alternatively that there exists no valid arbitration agreement capable of extension:

- on the burden of proof:

[Defendant No. 2] claims on the basis of a principle recently reconfirmed by an ICC Arbitral Tribunal sitting in Zurich, that the burden of proof "for the scope and reach of an arbitration

clause is incumbent on the party which intends to rely on it (here: on Claimant)". Claimant has not discharged its burden of proof according to [Defendant No. 2] . . .

[Defendant No. 2] alleges that article 14.2 of the Credit Agreement "does not refer at all to arbitration as a mode of settlement", and since there exist two mechanisms of settlement of disputes at the ICC, *i.e.* conciliation and arbitration, article 14.2 of the Credit Agreement does not provide a clear guidance as to what mechanism is referred to . . .

[Defendant No. 2] contends that [Claimant] has failed to discharge its burden of proof as to the validity of the arbitration agreement and that its reasoning is based on a chain of wrong assumptions and confusions since it confuses two mechanisms of settlement of disputes, *i.e.* direct negotiation, on the one hand, and conciliation, which requires the intervention of a third person, on the other hand. [Claimant] thus allegedly implicitly admits that article 14.2 provides for conciliation as a referral of settlement of disputes . . .

Finally, [Defendant No. 2] contends that [Claimant] ignores article 14.3 of the Credit Agreement which provides for the jurisdiction for [the courts of country Y] while giving "no explanation of how its interpretation could be reconciled with the express wording of article 14.3" . . .

- on the arbitration agreement:

[Defendant No. 2] maintains that article 14.2 lacks the fundamental elements of an arbitration agreement, *i.e.* the intention to arbitrate the dispute, since in the absence of such an intention "no valid and binding agreement comes into existence". [Defendant No. 2] refers to Craig, Park and Paulsson in their Commentary on the ICC Arbitration Rules stating that "if the parties want arbitration, they should say so clearly" (Part II, p. 90), and contends that the word "arbitration" appears neither in the title, nor in the wording of article 14.2, nor anywhere else in the Credit Agreement.

It adds that "the absence of any reference to arbitration as the mode of settlement of dispute is not at all remedied by the fact that article 14.2 provides that the dispute 'will be submitted to the International Chamber of Commerce for settlement under their rules and regulations, in Paris'" since the ICC is engaged in settlement of disputes by conciliation as well as by arbitration, as demonstrated by the existence of two separate sets of rules, and accordingly any inference in favour of arbitration is absolutely impossible . . .

It adds that, when compared with the ICC Model Clause, the absence of the words "arbitration" and "finally" is "of paramount importance as they affect the validity of article 14.2 as an arbitration agreement and its binding character" . . .

[Defendant No. 2] further contends that, according to the rules of interpretation of both *Unidroit* principles and French scholars, an ambiguous clause has to be interpreted against the drafter, *i.e.* against [Claimant] . . .

Moreover, [Defendant No. 2] contends that the wording of article 15.1.5 of the Credit Agreement, which provides only "[...] that if necessary the Bank could enforce judicially the said obligations in [country Y]", shows the parties' intention of no settlement other than a judicial one in [country Y] . . .

[Claimant]'s position

[Claimant] contends that, in article 14.2, the parties "intended to solve their dispute by mutual agreement in order to avoid litigation. Should mutual agreement not be possible, (either reached by direct negotiation between the parties, or by conciliation by a third person), the clause foresees a solution which is compulsive for the parties, that is, it conclusively resolves a dispute arisen. Such method is arbitration." . . .

It alleges that [Defendant No. 1] and [Defendant No. 2]'s interpretation, *i.e.* converting this clause into a conciliation clause, negotiation or any other alternative method, would only tend to "perpetuate the actual situation, that is their non payment of the outstanding amounts" . . .

Accordingly, the only possible method in order to solve the dispute in an ICC Rules frame which would be final and compulsory for the parties is arbitration . . .

As to the rules of interpretation (Unidroit principles and jurisprudence and legal scholars) mentioned by [Defendant No. 2] in order to interpret article 14.2, [Claimant] alleges that should the Contract be interpreted as being of an onerous character, the doubt should be resolved in favour of the reciprocity of interest. In this case, reciprocal interest of all parties were best protected in an international arena, avoiding a party being involved in a litigation in the territory of the other party . . .

Additionally, [Claimant] alleges that should the parties have intended to submit their litigation to [the courts of country X or country Y], they would have stated so clearly; on the contrary, article 14.3 reserves only to [Claimant] the right to claim before [a court of country Y]. Besides, should the parties have intended to solve their disputes before [the courts of country Y], they would have selected [the law of country Y] instead of [the law of country X] in the Credit Agreement and would have expressly so provided in the Letter of Guarantee instead of only referring to the terms and conditions of the Credit Agreement . . .

Discussion of the Arbitral Tribunal

The Tribunal notes that article 14.2 of the Credit Agreement provides that the "parties to the Agreement" were to submit their dispute "to the International Chamber of Commerce for settlement under their Rules and Regulations, in Paris". Accordingly, it is clear to the Tribunal that the parties' will, failing a settlement by mutual consent, was that the dispute be settled before the ICC according to the "Rules and Regulations" of the ICC.

The Tribunal also notes that the terms "arbitration" or "arbitrator" or "Arbitral Tribunal" are not set forth under article 14 "Law and Jurisdiction" of the Credit Agreement. However, the Tribunal considers that arbitration agreements which do not include the word "arbitration" may still be deemed as constituting an arbitration agreement if the interpretation of the Contract shows that such was the parties' intent.

The Tribunal further notes that the principles of interpretation of an arbitration agreement lead the Tribunal (i) to look for the parties' real intent, taking *inter alia* into account the consequences which they have reasonably and legitimately contemplated, and (ii) to give effect to the parties' intent. This approach falls in line with the Unidroit Principles on International Contracts, article 4.5 of which providing that "[c]ontract terms shall be interpreted so as to give effect to all the terms rather than to deprive some of them of effect". Applying a similar reasoning, article 1.6(2) of Unidroit Principles states that "[i]ssues within the scope of these Principles but not expressly settled by them are as far as possible to be settled in accordance with their underlying general principles". There are several ICC awards which have decided that the appreciation of the validity and effectiveness of an arbitration agreement goes beyond the requirements of a strict literal interpretation. On the contrary, when the parties insert an arbitration agreement in their contract, one should presume that their intent was to establish an effective machinery for the settlement of disputes contemplated in the arbitration clause (see *inter alia* ICC award no. 2321 rendered in 1974 in JDI 1975, p. 938; award rendered in ICC case no. 1434 in 1975 in JDI 1976, p. 978 and award rendered in ICC case no. 5103 in 1988 in JDI 1988, p. 1206).

In the present case, [Claimant], a party [from country X], executed the Credit Agreement with [Defendant No. 1], a party [from country Y], for the purpose of financing an international

project in [country Y]. Both the Bank ([Claimant]) and the Borrower ([Defendant No. 1]) were perfectly aware of the importance of ICC for the settlement of disputes and of the fact that should their dispute be submitted to the ICC for settlement under its "Rules and Regulations", the normal process of settlement is then arbitration under the Rules of Arbitration.

As to the alternative mentioned by Respondents between conciliation and arbitration, the Tribunal confirms that the *normal* procedure of settlement of dispute is arbitration. A survey of ICC's practice clearly shows that arbitration is by far the prevailing method of settlement before the ICC: in 1997, there were 452 arbitration cases, as compared with 8 conciliations (433 arbitrations in 1996, as compared with 11 conciliations). (See ICC International Court of Arbitration Bulletin, May 1997, p. 6 and May 1998, p. 4.) Accordingly, on the basis of the principle of effectiveness, article 14.2 can only be construed as referring to arbitration. Furthermore, conciliation, even as considered as prerequisite to arbitration, requires the consent of all parties. By filing a request for arbitration, [Claimant], as Claimant, is deemed to have renounced any preliminary step for conciliation.

Defendants have pointed out the apparent contradiction between article 14.2 of the Credit Agreement [the arbitration agreement] and its articles 14.3 and 15.1.5. Article 14.3 provides that "the Bank ([Claimant]) reserves the right to start in the courts of [country Y], any legal proceeding that may be required for the protection of its rights", thus enunciating clearly the parties' intent to leave open an option to the Claimant only (*i.e.* [Claimant]) between the recourse to arbitration or to the state jurisdictions. Article 15.1.5 ("[...] if necessary the Bank could enforce judicially the said obligations in [country Y]") emphasizes a similar intent of the parties to also leave such an option open.

Accordingly, the Tribunal's decision is that the parties' intention was that their dispute be settled through arbitration under ICC Rules of Arbitration.

Final Award in Case 9797

July 2000

Original in English

Place of arbitration: Geneva, Switzerland

1998 ICC Rules of Arbitration

The parties to this dispute were all members of a worldwide business group. Claimants were firms comprising one business unit (X) within the group, whilst Respondents were other firms constituting another business unit (Y) within the group, plus an umbrella entity (Z) created to coordinate the practice of its partners and their member firms, which included those of X and Y. Coordination between member firms was achieved by way of agreements, known as MFIFAs (Member Firm Interfirm Agreements), designed to ensure the provision of uniform, high quality services to clients with interests in more than one country. Such cooperation enabled member firms to benefit from technological expertise developed by other member firms, in return for which payments or contributions to costs might be required. Over time, as the skills and services offered by each unit evolved, they began to overlap, causing conflict between X and Y. Attempts were made to define the responsibilities of each business unit so as to avoid competition, but they proved

unsuccessful. Failing a satisfactory solution, Claimants initiated arbitration proceedings, accusing Y of breaching their MFIFAs by encroaching on X's area of practice, of disrupting Claimants' business opportunities, of misappropriating X's name and goodwill, causing marketplace confusion, poaching X's personnel and trading on X's credentials and expertise. It further accused Z of breaching its obligations under the MFIFAs by failing in its duty to coordinate practice, by allowing Y to compete with X, by failing to enforce the mutual obligations between the member firms of X and Y and by failing to regulate the use of the group name. Y accused X of engaging in inequitable conduct and breaching its obligations to the Y member firms, notably by trading on their credentials and expertise, acting in bad faith and refusing to cooperate with Y member firms. In examining certain of these claims and the remedies to be granted, the sole arbitrator referred to the *Unidroit Principles* (articles 1.7, 4.1, 5.4, 7.3, 7.4).

Applicable law

The Tribunal found that the Member Firm Interfirm Agreements (MFIFAs) entered into between [Z] and the [group] member firms, together with the [Z] Articles and Bylaws are the relevant rules of law chosen by the parties to govern the present arbitration; in interpreting the provisions of the MFIFAs the arbitrator is not bound to apply the substantive law of any jurisdiction but shall be guided by the policies and considerations set forth in the Preamble to the MFIFAs and the Articles and Bylaws of [Z]; if the MFIFAs and the [Z] Articles and Bylaws are silent or do not provide guidelines for a decision, the Tribunal shall, pursuant to article 17(1) of the ICC Rules, apply the rules of law it deems appropriate; those rules of law shall be the general principles of law and the general principles of equity commonly accepted by the legal systems of most countries.

The Unidroit Principles of International Contracts are a reliable source of international commercial law in international arbitration for they "contain in essence a restatement of those "*principes directeurs*" that have enjoyed universal acceptance and, moreover, are at the heart of those most fundamental notions which have consistently been applied in arbitral practice."¹

With regard to X's claim that Y member firms disrupted its business opportunities, poached its personnel, traded on its credentials and expertise, misappropriated its name and member firms' goodwill and caused marketplace confusion.

The [X] member firms additionally accuse the Respondent member firms of breaching their obligations under the MFIFAs on the counts described above.

The [Y] member firms deny both the factual and contractual basis of Claimants' allegations and challenge some assertions of the [X] member firms.

In the Tribunal's view, only a few situations described by Claimants can be categorized as a breach under the MFIFAs.

There are ten uncontested events prior to this arbitration of [Y] member firms' partners or personnel misleading [X] clients in order to sell their own services and 18 situations of [Y] member firms bidding on [X] member firms' existing clients for jobs similar to those performed by Claimants for such clients.

Claimants have also produced evidence of an incident involving a [Y] member firm hiring away an [X] member firm's employee. The former [X] employee later solicited work to the same client he had assisted while serving with the [X] member firm in spite of the [Y] member firm's assurance that such situation would not occur.

The MFIFAs contain no provision explicitly prohibiting that conduct, but the contractual agreements among the parties forbid the [group] member firms to engage in uncooperative acts to benefit themselves at the expense of other member firms. Such acts are contrary to the member firms' implicit obligation to cooperate and to pursue their professional practice in accordance with the principle of good faith and fair dealing inherent to international contracts.²

On five other occasions [Y] member firms traded on Claimants' credentials and expertise, citing as [the group]'s qualifications and skills exclusively belonging to [X] member firms. That conduct is also contrary to the member firms' obligation to act in accordance with the principles of good faith and fair dealing.

With regard to X's claim that Z failed to coordinate the practices of the member firms

'Claimants accuse [Z] of disregarding "its core function to assure that the basic purpose of the 1989 restructuring is met and to act as the *coordinator* of all Member Firms and the implementer of guidelines and policies to ensure compatibility among and the harmonious operation of all Member Firms". (emphasis provided in text)

The [X] member firms' contention rests on one basic assumption: [Z] has the obligation to coordinate the member firms' practices. [Z] answers that with minor exceptions, the MFIFAs do not impose an obligation on [Z] to coordinate.

In the Tribunal's view, the language of the [group] organizational documents is not in accordance with [Z]'s interpretation.

Member firms coordination is the cornerstone of the MFIFAs; it is the means to ensure that the [group]'s cooperative goals are achieved. If adequate coordination were not well-founded and properly ensured in an organization such as the [group] – comprised of more than one hundred member firms worldwide – cooperation would be seriously impaired.

By entering into an MFIFA, a member firm appoints [Z] to arrange for the coordination of its professional practice on an international basis with that of the other member firms . . . and legitimately expects its professional practice to be coordinated with that of the other member firms. Conversely, [Z] accepts such appointment and the responsibilities inherent to the coordinating function.

Furthermore, one of [Z]'s guiding principles is that the members firms' practices shall be correlated and coordinated on an international basis . . .

In summary, the explicit MFIFA provisions, interpreted in light of the purposes and policies set forth in the Preamble thereto and in the [Z] Articles and Bylaws, demonstrate that [Z]'s essential obligation is to coordinate the [group] member firms' diverse professional practices subject to the purposes and policies set forth in the Preamble to the MFIFAs and in article 3 of the [Z] Articles. Indeed, since its creation in 1977, [Z]'s purpose has been the coordination of its member firms on an international basis . . .

Those coordinating duties include specific functions, among others, developing compatible policies and professional standards for the member firms; developing annual operating plans to ensure the effective coordination of the member firms' practices and determining the appropriate scope of practice for the members firms.

The Tribunal finds that the wording of these purposes, policies and functions indicates that [Z] must exercise its best efforts³ to ensure cooperation, coordination and compatibility among the member firms' practices.

² Unidroit Principles of International Commercial Contracts, article 1.7.

³ Unidroit Principles of International Commercial Contracts article 5.4(2). "To the extent that an obligation of a party involves a duty of best efforts in the performance of an activity, that party is bound to make such efforts as would be made by a reasonable person of the same kind in the same circumstances."

...
 [Z] neglected to address the scope of practice conflict, even after the Board of Partners and Mr ... had admitted that the status quo was unacceptable and unsustainable.

On these grounds, the Tribunal finds [Z] did not make its best efforts to ensure coordination, cooperation and compatibility among the practices of the [Y] and [X] member firms, because it failed to take any course of action when the scope of service conflict surfaced and extended; and because it failed to develop the annual operating plans required to coordinate the practices of all the [group] member firms.

...
 [Z]'s neglectful conduct is a breach of its obligations to coordinate the practices of the [X] with those of the [Y] member firms, to develop compatible policies and professional standards for member firms and to develop annual operating plans to assure the effective coordination of the member firms' practices ...

[Z] contends that any such breaches are not sufficiently material to warrant termination. "The Unidroit factors – says [Z] – make it clear that there has been no material, fundamental breach."

The Unidroit criteria cited by [Z] proclaim:

"In determining whether a failure to perform an obligation amounts to a fundamental non-performance regard shall be had, in particular, to whether

- a. the non-performance substantially deprives the aggrieved party of what it was entitled to expect under the contract unless the other party did not foresee and could not reasonably have foreseen such result;
- b. strict compliance with the obligation which has not been performed is of essence under the contract;
- c. the non-performance is intentional or reckless;
- d. the non-performance gives the aggrieved party reason to believe that it cannot rely on the other party's future performance;
- e. the non-performing party will suffer disproportionate loss as a result of the preparation or performance if the contract is terminated."

Several prior findings made in this award must be considered in assessing [Z]'s conduct in the light of the Unidroit criteria: ...

In light of the above findings, [Z]'s conduct amounts to a fundamental non-performance of its obligations under the MFIFAs.

First, [Z] failed to coordinate all the [group] member firms, particularly by neglecting two of its critical functions: to develop annual operating plans for all the member firms' practices and to make its best efforts to address and resolve the scope of service issue.

[Z]'s failure to exercise its best efforts to coordinate the member firms' practices substantially deprived Claimants of the cooperation they were entitled to expect under the MFIFAs.

[Z]'s negligence led the [Y] and [X] member firms to behave essentially as two separate global partnerships, amid the internal tensions and disputes between them. Thus, as events unfolded, the benefits for Claimants under their MFIFAs became increasingly unrelated to their association with the [Y] member firms.

By any count, the [X] member firms have been substantially deprived of the cooperative benefits which the contractual bonds with the [Y] member firms were supposed to provide. In fact, the agreements between the [Y] and [X] member firms grew to be highly detrimental for Claimants, insofar as the [X] member firms have been obliged to make massive transfer payments without receiving cooperation in return.

That kind of arrangement could not have been the result expected by the [X] member firms or the result any reasonable party would expect from a contractual relationship.'

Second, strict compliance by [Z] [with] its obligation to coordinate the practices of the [X] and the [Y] member firms is of the essence of the MFIFAs.

As stated above, coordination among the member firms' practices provides the means to ensure the cooperative goals set forth in the Preamble thereto are achieved. If the member firms are not adequately coordinated, cooperation among them is seriously impaired.

Also, by entering into an MFIFA, each [X] member firm appointed [Z] to provide such coordination and legitimately expected its professional practice to be coordinated with that of the other member firms, including the [Y] member firms.

Third, [Z]'s non-performance gives Claimants reason to believe that they cannot rely on [Z]'s future performance.

[Z] failed to coordinate the practices of the [Y] and [X] member firms despite Mr. . . . and the business unit leaders' admittance that the scope of service issues needed to be addressed. [Z] equally failed to define an overall operating framework for all the member firms and to comply with its obligations albeit its Board of Partners declared fifteen months prior to the initiation of this arbitration that the status quo was unacceptable.

Nothing indicates that the [X] member firms can rely on [Z]'s future performance of its obligations, particularly in light of the internal division among most of its leaders along business units lines.

Fourth, Respondents will not suffer a disproportionate loss as a result of the preparation or performance if Claimants' MFIFAs are terminated.

[Z] cannot possibly suffer any harm from the termination of its contractual relationship with the [X] member firms because [Z] is an instrumentality for the purpose of coordinating the member firms' professional practice. In fact, [Z] is only paid for the services rendered to the member firms as long as Claimants' MFIFAs remain in force. . . .

Moreover, the [Y] member firms' past performance to the [X] member firms has been more than compensated by the significant amounts received from the [X] member firms as transfer payments.

Respondents' reliance on paragraph 17.2 of the MFIFAs to determine the damages suffered as a result of Claimants' departure from the [group] is unfounded. The MFIFAs explicitly state that those liquidated damages are to be presumed as a valid measure of actual damages suffered by the party entitled to payment. Among them are the increased costs of establishing a relationship with other suitable practice entities or those associated with the inability to establish such replacement relationships, and the related decrease in revenues.

Respondents have neither right to termination payments nor the apparent need to establish new relationships with other suitable practice entities. The [X] and [Y] member firms virtually operate as two separate global partnerships . . .'

With regard to X's alleged refusal to cooperate with Y

'The Respondent member firms accuse Claimants of systematically failing to cooperate since the early 1990s, by refusing to team with them and declining to share resources including common support structures and personnel.

The Tribunal found eleven instances, prior to this filing of this arbitration, of [X] member firms acting uncooperatively by, *inter alia*, halting previous joint industry studies; excluding [Y] member firms from engagements for clients introduced by [Y] partners to [X] member firms; excluding [Y] personnel previously committed to work on certain [X] member firm engagements and backing out of joint proposals with [Y] member firms.

That conduct is contrary to the member firms' implied obligation to cooperate under the MFIFAs and to the explicit obligation to pursue their professional practice with respect to one another in accordance with the principle of good faith and fair dealing, inherent to international contracts.⁴

Nevertheless, the events portrayed by the [Y] member firms are not a material breach of the MFIFAs, particularly if those events are placed in the context of a long-standing relationship involving thousands of potentially conflicting situations.

Contrary to the Respondent member firms' assertion, the Tribunal found no documentary support showing that Claimants had issued a "directive" forbidding the [X] member firms to cooperate with the [Y] member firms.⁵

With regard to remedies

(i) Claimants' release from its obligations under the MFIFAs

'While [Z] breached its obligations to the [X] member firms under Claimants' MFIFAs and was responsible for a fundamental non-performance thereunder, Claimants did not engage in inequitable conduct or breach their contractual or fiduciary obligations.

It is a well established rule of law that a fundamental breach of a contract gives the aggrieved party the right to terminate the contractual relationship. This general rule is reflected in the MFIFAs which provide that the effect of a material breach thereto entitles the wronged party to terminate its MFIFA . . .

Under the Unidroit Principles of International Commercial Contracts, a party may terminate a contract when the failure of the other party to perform an obligation under the contract amounts to a fundamental non-performance. The consequence of termination is to release the parties from their obligation to effect and to receive further performance.⁵

On account of [Z]'s fundamental non-performance, the [X] member firms' MFIFAs are terminated. Consequently, Claimants are released from all their obligations to [Z] and the [Y] member firms under the MFIFAs as of the date the present award is notified to the parties.⁷

(ii) damages or compensation

'Claimants seek an award of US\$. . . for damages caused to the [X] brand and reputation, originated in marketplace confusion caused by [Y]. Those damages stem from the time Claimants devoted to clarifying existing or prospective clients' perceptions; from lost accounts; from the cost of developing a new logo and identity; increased advertising and marketing communications; and from reputation effects on brand image and equity.

⁴

Unidroit Principles of International Commercial Contracts, article 1.7

⁵

Unidroit Principles of International Commercial Contracts, articles 7.3.1(1) and 7.3.5(1).

The Tribunal found that the [Y] member firms did not breach their obligations under the MFIFAs by causing confusion in the marketplace. For this reason, the [X] member firms cannot claim any harm from the alleged breach and are not entitled to any compensation (article 7.4.2 of the Unidroit Principles).

[Z] on the other hand, breached its material obligations under the MFIFAs by failing to coordinate the practices of the [X] and [Y] member firms. However, [Z] was not under the duty to coordinate the practices of the member firms by drawing clear distinctions among the member firms' marketplace images. Thus, none of the damages alleged by Claimants are a consequence of [Z]'s non-performance.

Claimants also seek restitution of the transfer payments made to the [Y] member firms since 1994, including the transfer payments placed in escrow, plus interest thereon.

The Tribunal has ruled that Claimants' MFIFAs are terminated as of the date this Award is notified to the parties.

Under general principles of law, upon termination of the contract either party may claim restitution of whatever it has supplied, provided that such party concurrently makes restitution of whatever it has received (see article 7.3.6(1) of the Unidroit Principles). Thus, restitution necessarily entails that both parties return what they have received under the contract.

Performance of Claimants' MFIFAs has extended over a period of more than ten years. During that time and even after 1994, Claimants have received several benefits from their association with the [Y] member firms, e.g. the use of the [group] name and client referrals by the [Y] member firms. Albeit these benefits have decreased in the course of time, they are by no means immaterial.

Restitution of the benefits received by Claimants is impossible. In fact, the [X] member firms do not even offer to do so.

If the Tribunal were to grant the restitution of transfer payments made by Claimants, they would be unjustly enriched.

The Tribunal shall not grant Claimants the restitution they requested.⁶

(iii) use of common technology

The next question is what determination should the Tribunal make in case all the member firms which jointly developed and collectively own [group] Technology depart the [group]. Neither the MFIFAs, nor any other [group] governing document known to the Tribunal provide an answer. Therefore, the general principles of law are the appropriate rules to decide this matter.

Under general principles of law, contracts must be interpreted according to the common intention of the parties.⁶ If the intention cannot be established, the contract should be interpreted in light of the meaning reasonable persons of the same kind as the parties would give to it in the same circumstances.⁷

It would not be reasonable to hold – and reasonable persons of the same kind as the parties to this arbitration could not possibly claim – that the member firms not paying for or participating in the development of [group] Technology are common owners of such technology or that the entities which funded and developed it are bound to forfeit their rights to those who have no title thereto.

⁶ Unidroit Principles of International Commercial Contracts, article 4.1(1) and Principles of European Contract Law, article 5:101(1).

⁷ Unidroit Principles of International Commercial Contracts, article 4.1(2) and article 5:101(3) of the Principles of European Contract Law substantially contains the same provision.

Equity would not dictate a different solution. Indeed, the Tribunal found that the Respondent member firms established a broad-based . . . practice that competes with Claimants' activities. For this reason, it would be unfair to compel the [Y] member firms to surrender their technology which would capacitate the competing [Y] member firms in Claimants' core activities.

The final question is what disposition should the Tribunal make in connection with [group] Technology, if any, jointly developed and commonly owned by [X] and [Y] member firms.

The Tribunal has found no evidence among the myriad of documents submitted in this arbitration, of the extent to which any [group] Technology was jointly developed by member firms from both business units. In any case, that Technology must remain within the [Y] member firms as provided in paragraph 17.2(D) of the MFIFAs.'

Partial and Final Awards in Case 9875

January 1999 (partial), March 2000 (final)

Original in English

Place of arbitration: Brussels, Belgium

1998 ICC Rules of Arbitration

*In 1983, Claimant, a French company, was given an exclusive licence to manufacture, sell and distribute Respondent's products in Europe. A similar agreement was made at the same time between Respondent and an American firm (X) for the North American market. Respondent retained exclusive distribution in Asia for itself and gave Claimant and Respondent non-exclusive rights for other countries. The licence agreement between Claimant and Respondent provided for an exception to exclusivity in order to allow the products bought by Original Equipment Manufacturers in the territory of one exclusive licensee to be distributed in another licensee's exclusive territory. In 1996, Respondent entered into a new agreement with X and submitted a new draft contract to Claimant, which was never executed. Claimant contended that the new contract between Respondent and X infringed its exclusivity in Europe, as Europe had been omitted in a clause defining limitations upon the extent of X's distribution. The arbitral tribunal therefore had to decide whether the second contract between Respondent and X was to be deemed to violate the exclusivity in the European market granted to Claimant in its original agreement with Respondent. In its partial award, the arbitral tribunal decided that *lex mercatoria* should be applied to the merits of the case, noting that the *Unidroit Principles* were a reflection of the rules of law and usages of international trade. In its final majority award, the tribunal referred to the rules of interpretation contained in article 4 of the *Unidroit Principles* and the practice of good faith and fair dealing expressed in article 1.7.*

Partial Award

'Applicable Rules of Law'

The Agreements between the parties do not include provisions concerning the rules of law applicable to their contractual relationship.

Claimant argues French law should be applicable. The choice of Brussels, a place with no substantial link with the dispute, cannot lead to the application of Belgian law. The most appropriate law should be determined through the "méthode de la voie directe", involving the examination of different factors. The place of the characteristic performance, in a licence agreement, is often considered as that of the licensor; however, the issues submitted to this tribunal are wider than questions related to the Defendant's industrial property rights. The "proper law of the contract" can only be French law, for several reasons. France is the country from which all operations included in the territorial exclusivity were conducted; it is the country where the formulas and know-how allegedly misappropriated by Defendant were developed; it is in France that the consequences of the breach of the licence contracts were felt and the ensuing prejudice must be compensated.

While agreeing with Claimant that Belgian law should not govern the issue, Defendant considers Japanese law should apply, not French law. In the absence of a common intent of the parties, Japanese international private law applies the law of the place where the contract was executed, that is Japan in this case. Under French international private law, the 1980 Rome Convention would apply. Article 4 of that Convention provides that in the absence of an express choice, the agreement "shall be governed by the law of the country with which it is most closely connected", it being "presumed that the contract is most closely connected with the country where the party who is to effect the performance which is characteristic of the contract has, at the time of conclusion of this contract, his ... central administration". The characteristic performance, in a licence contract, is that of the licensor, *i.e.* [Defendant], which would also lead to the application of Japanese law. Refuting some of Claimants' arguments, Defendant points out that the territory of the licence agreements was not limited to France, that the choice of the law of the place where the alleged prejudice was suffered might be relevant in a tort case, but not in a contractual dispute and that the alleged breaches (conclusion of the second [X] agreement, registration of patents in Japan and the United States) have no link to France.

According to article 17(1) of the ICC Rules, in the absence of an agreement between the parties upon the rules to be applied to the merits of the case, "... the Arbitral Tribunal shall apply the rules of law which it determines to be appropriate". Article 17(2) adds: "In all cases the Arbitral Tribunal shall take into account the provisions of the contract and the relevant trade usages."

The provisions of the contract are not decisive. It contains references to France and other European and non-European countries as well as to Japan. The Sales Territory described in Exhibit II covers "All countries of the world, other than Canada, USA, Mexico and Asian countries east of Iran, except French Territories". The licence is granted for patents held by Japanese companies (Exhibit III). Technical assistance will be provided by the Defendant at the Claimant's factory in France (art. 4) or at the Defendant's offices and production facilities in Japan (art. 5). The Claimant has agreed to pay royalties in Japanese currency (art. 6). An important provision, much at the centre of this dispute, deals with improvements invented by the Claimant, normally in its premises in France (art. 9).

The tribunal does not consider the neutral choice of Brussels as the seat of the arbitration to imply a choice of Belgian law as the law applicable to the contract.

In licence agreements, the appropriate law is sometimes considered to be that of the country where the licensor is located (in this case, Japan), assuming the most characteristic performance of such contracts would be that of the licensor. However this is not an absolute rule. For example, the law of the licensee is sometimes preferred. The Rome Convention of 1980 also provides that the link to the characteristic performance can be discarded when such characteristic performance cannot be determined or when circumstances indicate that the contract is more closely connected with another country (art. 4) (cf. J. M. Mousseron, J. Raynard, R. Fabre and J. L. Pierre, *Droit du commerce international*, 1997, no. 136 *et seq.*).

In this case, part of the issues deal with the way the Defendant handled technical improvements invented and transferred to the former by the Claimant, casting doubts on a solution that would exclusively consider the licensor's transfer of technology to the licensee as the most characteristic performance of the contract. Insofar as the licensee's own performance can be considered as characteristic of the contract, this would lead to the application of French law. Another significant factor consists in the geographical scope of the rights licensed to the Claimant, which do not exclusively lead to French law, but would eliminate Japanese law.

The arbitral tribunal considers that the difficulties to find decisive factors qualifying either Japanese or French law as applicable to the contract reveal the inadequacy of the choice of a domestic legal system to govern a case like this. A contract concluded between Japanese and French companies concerning a licence to manufacture products and to sell them in various parts of the world is not appropriately governed by the national law of one of the parties, failing agreement on such a choice.

The most appropriate "rules of law" to be applied to the merits of this case are those of the *lex mercatoria*, that is the rules of law and usages of international trade which have been gradually elaborated by different sources such as the operators of international trade themselves, their associations, the decisions of international arbitral tribunals and some institutions like Unidroit and its recently published Principles of International Commercial Contracts.

Nevertheless the tribunal will take into account any relevant national laws concerning intellectual property rights issues raised during this procedure.'

Final Award

Interpretation principles

[1] Since the main problem here is one of interpretation, the tribunal has invited the parties to express their views of the principles to be applied under the *lex mercatoria*, which the partial award of January . . . 1999 declared to be applicable to the case.

[Claimant] refers to two provisions of the Unidroit Principles of International Commercial Contracts. According to article 4.1(1): "A contract shall be interpreted according to the common intention of the parties." Article 4.3 states that in applying article 4.1 . . . "regard shall be had to all the circumstances, including (a) preliminary negotiations between the parties; (b) practices which the parties have established between themselves; (c) the conduct of the parties subsequent to the conclusion of the contract; (d) the nature and the purpose of the contract; (e) the meaning commonly given to terms and expressions in the trade concerned; (f) usages". Such principles correspond to jurisprudence and arbitral practice. [Claimant] claims its interpretation of article 2 e of the second [X] contract is confirmed by the parties' common intention and subsequent conduct.

[Defendant] also invokes art. 4.3 of the Unidroit Principles, but additionally refers to art. 4.4 ("Terms and expressions shall be interpreted in the light of the whole contract or statement in which they appear.") and 4.5 ("Contract terms shall be interpreted so as to give effect to all the terms rather than to deprive some of them of effect."), as well as to art. 8 b of the Vienna Convention on Contracts for the International Sale of Goods ("In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties."). More generally, the *lex mercatoria* invites the tribunal to take into account

elements such as, *inter alia*, the principle of good faith, the rule of effectiveness, the reference to the contract as a whole and the behaviour of the parties. ...

[2] The tribunal considers the parties have rightly identified the interpretation principles to be applied, with one exception. It does not think [Respondent]'s reference to the rule of effectiveness (as expressed in art. 4.5 of the Unidroit Principles) is relevant in this case. Art. 2 e of the second [X] agreement would have effect under either interpretation submitted. Otherwise, the dominant principle is to consider the intention of the parties, which can be determined having regard to all the circumstances. Of particular importance in this case are on one side the contractual set-up as a whole, and on the other side the conduct of the parties subsequent (but also previous) to the conclusion of the contracts. ...

(a) Intention of the parties

[3] In the interpretation of art. 2 e of the second [X] contract, the intention of the parties should first be determined in the full context of the whole contractual set-up between [Defendant] and its two licensees, as it was organized in 1983 and as it may have evolved in 1996. The contractual relationships between [Defendant] and [Claimant] on one side, and between [Defendant] and [X] on the other side, should not be analyzed separately. The system set up in 1983 reflected [Defendant]'s worldwide planning with two licensees, each of the three participants receiving its own exclusive territory and agreeing to engage in a regular exchange of know-how. The main issue is to determine whether [Defendant]'s and [Claimant]'s intention, in 1996, was to allow [X] to enter the European market though this would be in violation of [Defendant]'s obligations towards [Claimant] under their still applicable 1983 agreement. In this respect, the controversial provision of article 2 e of the second [X] contract cannot be read by itself, nor even only in connection with art. 1 of the same agreement. The two 1983 contracts and the 1996 contract and draft contract have to be fully compared in their sensitive provisions.

The alleged violations of [Claimant]'s European territory came through direct ... and indirect ... sales by [X]. The relevant issue is not whether such sales occurred, but whether the second [X] contract permitted them.

Direct and indirect sales have to be distinguished.

Direct sales

[4] ...

As far as direct sales are concerned, the 1996 (draft) contracts are not different in their principles from the 1983 agreements: each contract protects the other licensee's territory. The second [X] contract does not contain any provision which would amount to a violation of [Defendant]'s obligations towards [Claimant].

Indirect sales

[5] Indirect sales are another matter. Apart from the OEM exceptions mentioned above, they were not explicitly referred to in the 1983 agreements. They were certainly permitted for each partner in its exclusive or non-exclusive territory. Were they permitted or prohibited in each other's territories?

The tribunal believes that in the absence of any explicit prohibition, such sales are not allowed outside one's territory. "Each party must act in accordance with good faith and fair dealing in international trade." (Unidroit Principles, art. 1.7) It would be contrary to this principle to do indirectly what the contract prevents from doing directly. Good faith prevents from selling to an entity which one knows or should reasonably know intends to resell in another licensee's territory. (This is an obligation towards the licensor, not towards the other licensee.)

This interpretation is confirmed by the OEM exceptions, which would not be necessary if indirect sales were freely permitted.

[6] Significantly, the 1996 (draft) contracts introduce specific provisions concerning indirect sales: . . .

[7] Remarkable differences from the 1983 agreements are apparent. Indirect sales are now subject to express provisions, in [Defendant]'s contractual relationships with both its licensees. With [Claimant], the prohibition which formerly derived from the good faith principle is now stated in the contract, and made applicable to the American and Asian markets. Between [Defendant] and [X], on the contrary, there is reciprocal prohibition of indirect sales in each other's territories, but Europe is significantly omitted.

It is also relevant to note that while the 1983 [Claimant] contract stated that "[b]oth [Defendant] and its US Licensee(s) are restricted from selling directly to the European market even to the European subsidiary or agent of an OEM located in their own respective countries" (art. 1), such provision was omitted in the 1996 draft contract.

Obviously, as far as indirect sales are concerned, the 1996 (draft) agreements are no longer identical. Considering the parties' legal expertise, the tribunal believes this new contractual set-up is not the result of bad drafting but of a deliberate intent, at least on [X]'s side, to alter the symmetry between [Claimant] and [X]'s positions on the world markets. Either [Defendant] shared that intent, or it can be reproached with oversight of [Claimant]'s interests when negotiating the second [X] contract.

(b) Parties' conduct

This interpretation is confirmed by the parties' respective conduct before and after the execution of that contract.

[8] The fact that the 2½-year-long renegotiation of the [X] agreement was not disclosed to [Claimant] is in itself probably no breach of [Defendant]'s contractual obligations towards [Claimant]. However, the tribunal finds it surprising as the three firms had been working together for many years on the basis of a worldwide cooperation and met regularly to exchange information. . . . Considering the significant modifications which were to appear in the 1996 contracts concerning indirect sales, this discretion suggests that [Defendant] was indeed playing a new game with [X] it did not want to reveal to its other licensee. . . .

[9] . . . [X]'s conduct after the conclusion of its second contract with [Defendant] casts some light on the American licensee's intentions. . . . [An internal memorandum] demonstrates [X]'s preoccupation with entering the European market and [X]'s conviction that they were able to do it through indirect sales.

[10] Such conviction is confirmed by . . . [X]'s . . . letter to [Defendant]: "[X] needs to offer products and services in Europe to remain competitive with . . . Today, we are accessing Europe through sales channels consistent with our . . . agreement" (emphasis added).

[11] [Respondent] argues that [X] was referring to the OEM exceptions, which permitted some indirect sales into each other's territories. . . . The tribunal does not follow this restrictive interpretation in a context where [X] proclaims its "intent to open up territories between [Claimant] and [X] in Europe" and its need "to offer products and services in Europe to remain competitive . . .".

Conclusion

[12] The tribunal concludes that by entering into a contract that opened [X]'s door for indirect sales in Europe, [Defendant] breached the exclusive licence it had granted to [Claimant] by article 1 of their 1983 contract.'

Partial Award in Case 10022

October 2000

Original in English

Place of arbitration: Vilnius, Lithuania

1998 ICC Rules of Arbitration

The parties entered into agreements aimed at developing Respondent into an efficient cement producer with a firm position in the export market. Claimant accused Respondent of violating the text and spirit of their agreements. After presenting the parties' claims, the Arbitral Tribunal discussed the question of the applicable law, which led it to make reference to the Unidroit Principles. No further reference was made to the Principles or "relevant trade usages" later in the award.

Applicable law

'[1] According to article 17 of the Rules, the primary source of the law applicable to the merits of the dispute is determined by the will of the parties. In article 5 of the Export Company Agreement, as well as in article 4 of the AEER [Agreement on Exclusive Export Rights, Upgrading of the Plant and Delivery of Cement], the parties have agreed that: "This agreement is governed by Lithuanian law." This choice of law clause has been interpreted as providing that Lithuanian law is to govern both the formation of the contract and the rights and duties of the parties arising from the contract as well. Throughout the proceedings the choice of Lithuanian law has not been disputed by the parties. (Claimant has expressly confirmed that the applicable law is Lithuanian and Respondents have impliedly confirmed this choice by invoking the provisions of the respective Lithuanian laws and arguing their applicability.)

[2] In its closing arguments Claimant has expressed the view that it is legitimate to look to the Unidroit Principles of International Commercial Contracts and the Principles of European Contract Law as a source of usage, customs and practice and that they are to be relied on when interpretation of the law is necessary in order to determine the parties' rights and obligations. Article 17 of the Rules confirms reliance on trade usage: "In all cases the Arbitral Tribunal shall take account of the provisions of the contract and the relevant trade usages." Both sets of principles represent the latest codification of international commercial trade usages. However, unless expressly incorporated by agreement between the parties, which they are not, they are not of mandatory but only of persuasive nature. Therefore, when necessary the Tribunal refers in this Award to "the relevant trade usages" and such reference includes, but is not limited to, the Unidroit Principles and Principles of European Contract Law.'

Final Award in Case 10114

March 2000

Original in English

Place of arbitration: Stockholm, Sweden

1998 ICC Rules of Arbitration

The parties entered into an agreement whereby Claimant, a Chinese company, was to provide and organize after-sales services for vehicles delivered by Respondent, an East European car manufacturer. The agreement laid down certain criteria which had to be met by the provider of the after-sales service. For its part, Respondent was to make periodical payments of assistance and to provide spare parts at the most competitive prices for the Chinese market. Three such payments were made. During the second year of the agreement, Respondent was informed that the agreement had been transferred from Claimant to a company registered in another Chinese city. This led Respondent to announce its intention to cancel the agreement. After unsuccessful negotiations, Respondent requested Claimant to cease its activities under the agreement and declared the agreement terminated due to breach of contract by Claimant. Claimant initiated arbitration proceedings in which it alleged various breaches of the agreement between the parties, such as failure to supply spare parts at the lowest ex-works prices, failure to abide by the exclusivity undertakings and failure to pay assistance fees. It claimed outstanding payments, compensation for harm suffered as a result of Respondent's breaches, and punitive damages. Respondent dismissed these claims, alleging in its turn that Claimant had no capacity to perform the agreement, that the agreement had been transferred without its consent and that Claimant had failed to meet several of the criteria laid down in the after-sales service agreement. It considered itself entitled not only to withhold and then cease payment of the assistance fees but also to request repayment of those fees already paid. In addition it claimed for loss of profit due to reduced sales, loss of goodwill and various costs and unpaid invoices. Following the parties' wishes, the Arbitral Tribunal decided that, in addition to Chinese law, the *Unidroit Principles* would be applicable, as a reflection of international practices. It subsequently referred to international trade principles when ruling on punitive damages, although without explicitly naming the *Unidroit Principles*.

Applicable law

The parties' positions

'Claimant holds Chinese law applicable as substantive law governing the contractual relations of the Parties, but is of the opinion that "international practices" have to be applied extensively. Claimant refers specifically to the *Unidroit Principles* of 1994. Claimant is of the opinion that the Convention on the International Sale of Goods ("CISG") is only applicable as to the contractual obligations referring to the sale of goods.'

'Respondent holds Chinese substantive law as applicable to the extent CISG, *Unidroit* or general principles of international trade law do not prevail over or complete the Chinese law.'

The Arbitral Tribunal's decision

'The Agreement No. 245 does not contain a choice-of-law clause. But both Parties presume that Chinese law is applicable. This joint presumption has to be regarded as an agreement on the application of Chinese law as governing the merits of the dispute. This choice of law – even if only made during the arbitration (see Redfern Hunter, *Law and Practice of International Commercial Arbitration*, 3rd ed., 1999, 2-26) – is valid according to article 17(1) ICC Rules.

CISG is a part of Chinese law. This convention is therefore applicable as part of Chinese law in a dispute between a Chinese entity and one from another country that, like China, has acceded to the CISG. However, the Arbitral Tribunal need not go further into this issue as the claims raised by the Parties do not concern issues that fall within the scope of CISG, as CISG regulates only claims resulting from non-performance, late performance or bad performance of a sales contract and none of these claims have been raised.

The Parties are jointly of the opinion that international practices, especially the Unidroit Principles, shall also apply. The Unidroit Principles (see Blessing, *Regulation in Arbitration Rules on Choice of Law*, 1996, p. 391; Derains/Schwartz, *A Guide to the New ICC Rules of Arbitration*, 1998, p. 218 ss.) are rules of law in the sense of article 17(1) ICC Rules.

The Arbitral Tribunal therefore decides, that the Chinese law and international practices including Unidroit Principles are applicable to the merits of the dispute.'

With respect to punitive damages, requested by Claimant.

'The concept of punitive damages is not known in Chinese contract law. Chinese law knows only specific performance, liquidated damages and compensatory damages as remedies for breach of contract, see Zhao, in: Wang/Mo, *Chinese Law*, 1999, p. 244 ss.

The FECL [1985 Chinese law on foreign economic contracts] defines compensatory damages as the actual loss resulting from the breach, which may include the expectation interests from the performance of the contract. However, such damages must not exceed the loss that was foreseeable by the breaching party at the time the contract was made.

Claimant has not given any proof that Chinese law grants damages that go beyond compensatory damages. The Arbitral Tribunal has not found any international trade principle authorizing the award of punitive damages. Punitive damages are in some jurisdictions even regarded as contrary to public policy, *i.e.* in German law (see Federal Supreme Court, Judgment of June 4, 1992, BGHZ 118, p. 312 ss.) and Switzerland (see Dörig, *Anerkennung und Vollstreckung US-amerikanischer Entscheidungen in der Schweiz*, 1998, p. 356 ss.).

In a situation where some of the important trading nations regard punitive damages as contrary to public policy, it is obvious that there is no international trade practice favouring punitive damages.

The Arbitral Tribunal therefore dismisses the claim for punitive damages.'

Final Award in Case 10335

October 2000

Original in English

Place of arbitration: Paris, France

1998 ICC Rules of Arbitration

Claimants, two Greek companies, and Respondent No. 1, a French company, submitted a joint offer (their second, the first having been unsuccessful) for the purchase of shares in a company (X) listed on the Athens stock exchange. Their offer was accompanied by a first demand bank guarantee. Following the acceptance of this offer, Claimants and Respondent No. 2 entered into a shareholders' agreement, according to which Respondent No. 1 was to transfer the shares it would purchase in the Greek company to Respondent No. 2 and Claimants, each receiving a specified percentage of shares and being responsible for their payment. Subsequently, a share purchase agreement was concluded between Respondent No. 1 and Claimants, as buyers, and the Greek state entity responsible for

selling the shares (seller). Respondent No. 1 refused to pay its share of the purchase price on the ground that the conditions precedent had not been met. As the purchase price was thus not paid in time, the seller rescinded the share purchase agreement and called the bank guarantee. The guarantor in turn demanded that Claimants and Respondent No. 1 pay their share of the credit risk to which they had subscribed. Claimants initiated arbitration proceedings, contending that the shareholders' agreement covered both the acquisition of the shares and their subsequent distribution between the parties and that both Respondents were liable for payment. They sought compensation for having had to pay their share of the guarantee. The terms of reference stated that the sole arbitrator would apply Greek law, in accordance with the arbitration clause in the shareholders' agreement, and that the law applicable to any matters not covered by the shareholders' agreement would be determined pursuant to article 17 of the ICC Rules of Arbitration. The first question examined by the arbitrator – which led him to make reference to the *Unidroit Principles* – was whether the shareholders' agreement was applicable to the acquisition of shares from the seller and whether, under this agreement, Respondent No. 2 had an obligation to pay the seller.

'Claimants assert a right ex articles 383, 385 Greek Civil Code (C.C.) to be compensated for damages resulting from delayed and ultimately non-performance of [Respondent No. 2]'s obligation to pay its share of the purchase price to [the seller].

The Shareholders' Agreement . . . , after identifying the Parties to it, introduces on little more than one typed page to its history and business background.

The clause cited by Claimants and Respondents as a possible source of an obligation which may have been breached, reads as follows:

1. Payment Responsibility

Each Party shall be solely responsible for the payment of the purchase price of the shares which correspond to its participation.

In order to support the Claimants' claim two questions would have to be answered in the affirmative: (1) Is the Shareholders' Agreement at all applicable to the acquisition of shares from [the seller]? (2) Does the Shareholders' Agreement create an obligation, on the part of Respondent No. 2, to pay its part of the purchase price to [the seller]?

In both respects, Claimants have made affirmative assertions while Respondents have denied both.

It is submitted that the language of the provision as such does neither permit to answer the question as to the Agreement's sphere of application nor does it indicate to whom the purchase price corresponding to each Party's quota shall be paid. As the sphere of application, of course, will only be revealed if one looks at the Agreement in its entirety, I shall first turn to the second question.

The obligee of the obligation to pay, *i.e.* the recipient of the payment for which responsibility is described is not named at all. Taking a grammatical approach to interpreting clause 1, the salient features are rather the word "solely" as well as the emphasis on responsibility for the payment of those shares "which correspond to its [*i.e.* the Party's] participation". "Solely" having the meaning of "alone" or "only", taken together with the last five words of the clause therefore, suggests that the provision's gist is to limit and circumscribe each Party's obligation rather than imposing any such obligation.

Claimants from the very outset have drawn the Arbitrator's attention to the fact that, for the purposes of interpreting a declaration of will and, for that matter, a contract, the two arguably most important provisions of the Greek Civil Code (C.C.) are articles 173 and 200. They read:

Article 173

When interpreting a declaration of will the true intention shall be sought without sticking to (the literal meaning of) the words.

and

Article 200

Contracts shall be interpreted according to the requirements of good faith taking into account business usages.

(Translation by C. Taliadoros, Greek Civil Code, 1982).

Both provisions are well known as common heritage of and fundamental to most civil-law systems, and in particular to the civil codes of the so-called germanic legal family. For example, §§ 133, 157 of the German Civil Code are identical. § 914 of the Austrian Civil Code and article 18 Swiss Law of Obligations enshrine the same principle. Modern international commercial law is evolving in the same direction (cf. for example, articles 1.7, 1.8, 4.1 - 4.3 of the Unidroit Principles of International Commercial Contracts).

Both Claimants and Respondents agree that the *telos* of the provisions quoted is to strike a balance between a subjective and an objective approach to determine what the "true" meaning is, when the parties to a contract, at a later stage, find themselves in disagreement. They have quoted Greek authorities and I find confirmation in this respect in Symeonides, "The General Principles of the Civil Law" in: Kerameus/Kozyris (eds.), *Introduction to Greek Law*, 2d ed. (Deventer/Boston, 1993) pp. 53, 68.

Claimants and Respondents, at least initially, further agreed that articles 173, 200 apply when there are doubts and the need to clarify and, in particular, gaps and ambiguities in the exchange of declarations and the wordings of a contractual provision. Only recently Claimants, citing two older supreme court cases and two writers, have put forward the theory that all declarations of will (and not only ambiguous or incomplete ones) are subject to interpretation . . . and, moreover and citing two high court decisions, that the judge "has an unlimited freedom to evaluate all the elements presented to him (either written or not) and draw conclusions, using the common sense rules, as well as his experience and common knowledge" . . . Respondents contest this analysis, citing both doctrinal writings and case law, including three supreme court cases . . .

I do not see an irreconcilable contrast of theory. Of course, all declarations are, logically speaking, subject to interpretation. But it is equally clear that interpreting an unambiguous term or phrase will necessarily result in identifying that unambiguous meaning. By the same token, no judge or arbitrator will ever disregard the letter of a contract nor will he hold that there is a lacuna where the parties have merely agreed (to his eyes and with hindsight) on an "unjust" allocation of risks. Finally, it appears safe to say that, however far the theory of "supplementing", "gap-filling" or "integrating" interpretation may be stretched, never will it reach beyond the substantive boundaries of the contract giving, for example, to one party something which that party may have tried, but was unable, to obtain in the negotiation process. The freedom of the judge or arbitrator may be unlimited in a procedural sense, but it is undoubtedly limited by the law and the parties' freedom to determine the content of their contracts, cfr. art. 361 Greek Civil Code.

Finally, Claimants . . . and Respondents . . . agree on the elements interpretation will draw on, namely the document in its entirety, surrounding facts, related documents, negotiations, interests of the parties, purposes of the agreement and custom.

Turning now to the document in its entirety, the analysis of the text will at the same time be aimed at understanding its clause 1 and the Agreements' sphere of application.

The Shareholders' Agreement's Preamble, after describing the target ([X]) and the (anticipated) successful outcome of the bidding process as well as Respondent No. 2's and Claimants' respective quota in the shares to be acquired from [the seller], turns to the next stage, the (anticipated) internal and final division of the shares. The bid and this second stage are clearly distinguished.

After setting out the (internally and not vis-à-vis [the seller]) envisaged allotment of the shares among Respondent No. 2 and Claimants, the Preamble defines the end of the entire transaction ("For the purpose of achieving the above shares allocation") as well as the means to be employed ("the Parties hereto and [Respondent No. 1], undertake..."). Only thereafter does the document set out the agreement proper: "In view of the above, (emphasis added; *i.e.* the final allotment) and of the impending acquisition of the shares (emphasis added), the Parties agree as follows" (emphasis added).

It is undisputed among the Parties to this arbitration that the technique to be employed for the acquisition of the shares for [the seller] was to be a reverse leveraged buyout... It is equally undisputed that this was the very purpose to bring in the "vehicle"... *i.e.* Respondent No. 2. Lastly, it is undisputed that [the seller] would not have agreed to substitute Respondent No. 2 for the successful official (co-)bidder, Respondent No. 1. All this is reflected in the Agreement's Preamble which distinguishes (1) acquisition from [the seller] (by Respondent No. 1 and Claimants), (2) re-allotment for purposes of the financing scheme and the restructuring of the future group, (3) relationship of the eventual shareholders (Respondent No. 2 and Claimants) subsequent to the acquisition and to the intermediate stage of re-allotting the [X] shares.

Neither the written submissions nor the testimony given by Messrs... suggest that any of the Parties to this arbitration, at the time of signing of the Shareholders' Agreement, expected Respondent No. 2 to step into the shoes of Respondent No. 1 vis-à-vis [the seller] and to actually acquire the [X] shares.

To conclude, the text of the Agreement's Preamble, while alluding to the acquisition of the shares (and in this sense "applicable" to that first stage of the transaction), does not support the theory that Respondent No. 2 was under an obligation vis-à-vis Claimants to acquire and to pay the purchase price for those shares.

Turning now to outside elements for the Shareholders' Agreement's proper construction, related documents might be of assistance. The first one coming to mind, and indeed cited by Claimants in their brief dated..., is the Cooperation Agreement, signed on... and regulating the relationship of the same Parties with regard to their first bid... However, that bid was unsuccessful and rejected by [the seller]. The Shareholders' Agreement in question here and signed after the second bid had been successful, provides in its clause 12:

This agreement included the complete agreement of the Parties hereto as to its subject matter and supersedes to any prior written or oral agreement between the Parties which are hereby declared null and void.

Therefore, the Cooperation Agreement, while certainly a predecessor in the history of the transaction, cannot provide guidance as to the interpretation of the Shareholders' Agreement which is in dispute in this arbitration. In any event, it does not support the Claimants' theory. On the contrary, although the Shareholders' Agreement was signed prior to the completion of the acquisition..., the Parties to it apparently deliberately dropped a clause contained in the (superseded) Cooperation Agreement which provides that:

The parties agree... to use their best endeavours in order to succeed in the final bid and acquire the Shares...

At a later stage, a new draft Cooperation Agreement... contained a clause 1 identical to the previous one. However, this draft remained unexecuted.

The testimony given by Claimants' witness . . . corroborates the result that the parties, during the negotiations of what was to become the Agreement signed, had decided to cover only their post-acquisition relationship.

Counsel for Respondents: "There were things that you decided not to regulate, which if you were to make another agreement of this sort now you might decide to regulate?"

[Claimants' witness]: "...Of course, since I have the knowledge now, I would regulate it". And: "... I would ask [Respondent No. 1] for the money."

Shareholders' agreements are highly negotiated made-to-measure documents. Consequently, custom as one of the accepted tools for interpreting declarations of will is not of assistance. The interests of the parties being entirely subjective (and in the case at hand in open conflict) and the negotiations and the purpose of the contract being reflected in the history from the various drafts to the Agreement executed on . . . the ways to discover the meaning of clause 1 asserted by Claimants are thus exhausted.

To sum up, neither does clause 1, to the best of my understanding, establish an obligation for Respondent No. 2 to pay for its share of the purchase price to [the seller] nor does it say that completion of the share purchase is owed to the Claimants.

To my eyes and according to my experience, with similar transactions, the Respondents' interpretation of clause 1, namely that it refers to and limits the responsibility of Respondent No. 2 and Claimants to pay [Respondent No. 1] in consideration for the (second-stage) re-allotment of the [X] shares, is highly plausible. But Respondents do not have to prove that. Claimants had the burden of proof for the facts in support of their claim and they have been unable to discharge it as far as the alleged breach of clause 1 is concerned.

Final Award in Case 10346

December 2000

Original in Spanish

Place of arbitration: Barranquilla, Colombia

1998 ICC Rules of Arbitration

Claimant and Respondent, both Colombian companies, entered into a contract pursuant to which Claimant was to sell electrical energy to Respondent so that the latter could ensure the public supply of electricity in a part of Colombia. However, the agreement remained unperformed. Claimant attributed responsibility for this to Respondent's failure to cooperate in registering the agreement and to the transfer of Respondent's assets to a third party, as part of its privatization. Claimant initiated arbitration proceedings in which it sought confirmation that the agreement between the parties was valid and that Respondent was in breach of contract, entitling Claimant to damages and the agreement to be terminated. Respondent rejected these claims, alleging in turn that the agreement was null and void. It raised a number of other objections, including the ineffectiveness of the contract, due its not having been registered, and force majeure, due to the imposed

transfer of its assets. In examining these claims and defences, the arbitral tribunal applied Colombian law, as provided in the parties' contract, as well as the provisions of the contract and relevant trade usages, as required by article 17(2), ICC Rules of Arbitration. In support of its conclusions, it referred to articles 1.7, 5.3, 7.3 and 7.4 of the *Unidroit Principles*.

With respect to Respondent's plea of unenforceability of the contract

'C - Issue no. 3

This is covered in point V (2) (c) (iii) of the Terms of Reference and requests the Tribunal to examine and decide the following:

To reject the allegation of absolute nullity of the contract, including addendum no. 1 and addendum no. 2, if it finds as proven and therefore accepts one or more of the remaining defence pleas put forward by Respondent, that is to say the pleas of "unenforceability of the contract due to lack of registration with the Sistema de Información Comercial - SIC [Commercial Information System]"; "defence of unperformed contract" and "force majeure".

2. Having set out the above, the Tribunal states the following with regard to the first plea, that is to say the plea of "unenforceability of the contract due to lack of registration with the Sistema de Información Comercial - SIC":

(a) Aside from the allegation of breach of contract put forward by [Claimant] due to Respondent's unwillingness to execute the documentation required for the registration of the contract, which is a matter that, whilst connected with this one, relates to another issue, [Respondent] has denied the allegations contained in the claim, relying on a fact which is fully established in the proceedings, namely that the contract was not registered in the SIC. As a result the task of the Tribunal is to decide whether this circumstance legally exonerates Respondent from the allegations of Claimant regarding Respondent's performance of its contractual obligations.

(b) The first point to specify is that it is not the contract which is enforceable or unenforceable, but rather the obligations generated by it, in order then to distinguish between the validity of the contract and the enforceability of the services provided for in it.

Registration of a contract in the SIC is clearly a prerequisite in order for its ultimate effects – supply of the energy; billing, fixing of the price, payment, etc. – can come into play. In other words, until the contract is registered the services provided for in it cannot be enforced. In that sense the final efficacy of the contract is pending and is subject to a condition whose performance, in this case, depended on positive joint action by the parties: the amendment of the corresponding terms of the agreement, in view of the position taken by the director of the SIC.

Such registration is, therefore, an administrative requirement which relates to regulation of the electricity service and is not, we repeat, a formality *ad substantium actus* as Defendant alleges. The contract is made upon fulfilment of the substantive requirements for such type of contract and, in the event that it is a state contract, with the formal requirements corresponding to such category of contracts. Registration is not an essential part or prerequisite of validity, nor even a procedure to publicize the contract, but rather, and we repeat, an administrative requirement for its enforcement.

This being the case, Respondent is obviously confused between validity of a contract and enforceability of its obligations and between prerequisites for validity and conditional nature of the performance of the services provided for in it.

(c) In addition to the above, that is how the parties must have understood it, particularly Respondent who drafted its text, in view of the fact that the contract only makes reference to the obligation to register it in clause 18 when, in an impersonal way, it provides: "This contract shall be deemed to be perfected by the duly legalized signatures of the parties, but to be enforceable it requires registration with the SIC."

The above terminology, leaving aside for the moment any reference to clause 16.5 of the contract, implies that the registration with the SIC was a joint task of the parties, in line with article 871 of the Commercial Code (*Código de Comercio*) and, by its nature, with the so-called "duty to collaborate" which is a rule of conduct that is clearly a "responsibility" which is discharged by the performance of the necessary acts, and whose omission, depending on the circumstances, may simply mean that the party concerned cannot attribute to the other party the adverse consequences of the omission and, therefore, claim breaches against that party which are only attributable to the party concerned itself. It may even amount to a breach of the duty of good faith, a source of liability, by preventing the performance of the services and the attaining of the purpose of the contract, that is to say by causing its frustration to the detriment of the other party.

In relation to this duty and responsibility, article 5.3 of the "Principles of International Commercial Contracts" prepared by the International Institute for the Unification of Private Law, "Unidroit", characterizes the "duty of collaboration" as follows: "Each party shall cooperate with the other party when such co-operation may reasonably be expected for the performance of that party's obligations" and the text comments as follows:

A contract is not merely a meeting point for conflicting interests but must also, to a certain extent, be viewed as a common project in which each party must cooperate. This view is clearly related to the principle of good faith and fair dealing (art. 1.7) which permeates the law of contract, as well as to the obligation to mitigate harm in the event of non-performance (art. 7.4.8).

The duty of co-operation must of course be confined within certain limits (the provision refers to reasonable expectations), so as not to upset the allocation of duties in the performance of the contract. Although the principal concern of the provision is the duty not to hinder the other party's performance, there may also be circumstances which call for more active cooperation.¹

The Council of State (*Consejo de Estado*), Chamber for Administrative Disputes, Section 3, in its judgment of 9 March 2000 (case no. 11447 – *Aseguradora del Valle S.A. and Seguros Comerciales Bolívar S.A. v. Empresas Publicas de Pereira*), made the following comments on duty and responsibility:

... it must be remembered that in state contracts too the duties imposed on the parties have to be observed. They include the duty to act with sagacity, which means with reasonable diligence when assuming commitments and fixing remuneration according to the circumstances of the stipulated services; and the duty of clarity by which a party to a contract must ensure that the other party knows, and must itself know, the details and circumstances which make up the agreement: the duty to provide information in order to give and receive all the elements which lead to greater clarity and purity in the agreements reached. It is therefore not viable to take account either of dishonest conduct, which is prohibited by the *nemo auditur* rule, or of contrary conduct whereby one party seeks to use audacious behaviour as a way of obtaining unfair advantages, either over the other contracting party, or over third parties which, as happens in public contracts, are taking part as bidders.

(d) It therefore follows from the above that at the root of the relationship between the parties was the unquestionable and clear duty, in the first instance by reason of their own interest, but at the same time by reason of a real obligation towards the other party, to do

¹ Ministry of Justice and Law, *Unidroit Principios sobre los Contratos Comerciales Internacionales* (Bogotá: Imprenta Nacional de Colombia, 1997) at 142. [The English version of the Unidroit Principles has been used here and below, wherever Unidroit texts are quoted from this publication of the Colombian Ministry of Justice.]

everything in their power to adjust the provisions of the contract to the requirements of the resolutions of the CREG [*Comisión de Regulación de Energía y Gas* - Energy and Gas Regulation Commission] and the director of the SIC, on pain of frustrating the purpose of the contract, to their own prejudice, and of being in breach of an obligation which is inherent to the operation of the contract and complementary or ancillary to its express contents, in this case a preliminary or preventative obligation, in view of the fact that if this step is not taken, all possibility of the performance of the contract is blocked, giving rise to the obligation to make full compensation.

As a result we have to investigate what the parties – or the SIC – did or omitted to do in relation to the registration of the contract in order to determine the inherent consequences, that is to say the failure of the defence plea in the event that Respondent failed to act with the required diligence, or the success of the defence plea in the event that (i) the SIC, arbitrarily, and despite the efforts of Respondent (and of Claimant) refused to register the contract; or (ii) only Respondent acted diligently; or (iii) neither of the parties showed any effective inclination to obtain the registration of the contract.

...

(f) The above summary means that one can infer that [Claimant] clearly tried to obtain registration of the contract in the SIC and did everything within its power, in particular proposing amendments to the contract which, whilst safeguarding the parties' positions on the question of "delivery points" for the contracted energy, would have enabled the registration of the contract.

...

(h) The diligent and reasonable attitude of [Claimant], which is supported by the circumstances described above and which is consistent with the principle of preservation of contracts *ut res magis valeat quam pereat* is however in contrast to the attitude of [Respondent] which, apart from agreeing to the request of the director of the SIC to take part in a meeting in order to analyse the obstacles to registration and to execute the Addendum No. 2, extending the "start date" of the contract, given that "the purchaser and the vendor require additional time over and above the start date to study the legal aspects of the contract", took no steps to overcome the difficulties and there is no evidence in the proceedings of any proposal whatsoever other than the very dubious suggestion that it would be flexible in return for the unrestricted acceptance by [Claimant] that "the energy must be supplied at the measuring points at a voltage level of 110 kv, 66 kv and 13.8 kv". As we saw earlier, this interpretation could easily have been wrong and was contrary to the very conduct of Respondent, as revealed in the seven (7) contracts referred to above which, moreover, were assigned to [X], albeit on a short-term basis.

It is therefore neither logical nor reasonable, nor in line with the aforementioned provision of article 871 of the Commercial Code (*Código de Comercio*) or the "duty of collaboration" that none of [Respondent's] many officers and advisers showed any inclination towards an alternative solution, nor put forward any idea, nor prepared any counterproposal to the amendments suggested by [Claimant] in order to obtain the registration of the contract in the SIC and thereby, if its interpretation is finally accepted by the dispute resolution body provided for in the contract, to reap the very important income, savings and benefits for the end-users described by Respondent...

On the contrary, the evidence shows that despite the provisions of its statutes and the "contracting regime", [Respondent] took no effective steps to overcome the problems with the registration of the contract and simply opted to hide behind the observations of the director of the SIC as a reason for washing its hands of the contract, to the point where it

considered itself released from it, by virtue of its desire for it to be null and void as a result of the said deficiencies or non-conformities which it refused to resolve as it could and should have done. Moreover, applying the doctrine of “own acts” [estoppel] this conduct would prevent “one party [Respondent] from relying on its own inconsistency to the detriment of the other [Claimant]”.²

With respect to the alleged breach of contract due to the transfer of Respondent's assets

[1] This being the case, the Tribunal concludes and will declare in the operative part of the Award that the transfer of assets by Respondent which was contained in notarized deed no. 2633 breached clause 10.3 of the contract as the authorization from [Claimant] contemplated in that provision was not obtained.

[2] The next aspect of the issue which is evaluated here concerns the breach of clause 10.2 of the contract as a result of the execution of notarized deed no. 2633 by Respondent.

In this regard the first point which the Tribunal makes is that the part of clause 10.2 which is relevant to this part of the Award is subsection one, which as part of clause 10 of the Contract on “Representations and Warranties; Additional Covenants by the Vendor and the Purchaser”, provides: “Both the vendor and the purchaser shall preserve and maintain in full force and effect their existence and all the state authorizations which are required for the proper performance of their business, including the performance of this contract.”

The aspect of the provision transcribed which concerns this issue is limited to the economic capacity of Respondent, as the change to its existence is a matter which pertains to a different issue. This circumstance in turn means that the following analysis is also conducted by reference to a possible breach by Respondent of clause 2 of the contract by reason of the transfer contained in notarized deed no. 2633 which has already been mentioned several times.

(a) It is clear that in the light of the principle of good faith and fair dealing each party to a contract must, without fail,³ adopt or maintain reasonable measures to ensure that they can perform their respective obligations. This implicit duty is even more rigorous where, as in this case, there is a specific provision, that is to say the part of clause 10.2 with which this part of the Award deals, which, moreover, is a rule which was proposed as a mandatory requirement by [Respondent].⁴

Whether failure to register the contract constituted a breach of contract

“E - Issue No. 6

This corresponds to point V (2) (c) (vi) of the Terms of Reference, that is to say:

Whether Respondent was or was not unwilling to execute the documentation required for the registration of the contract in the SIC, and if it was, whether it breached clauses 16.5 and 16.7 of the contract as a result.

1. The comments made in the analysis of the defence plea of “unenforceability of the contract due to lack of registration with the Sistema de Información Comercial - SIC” mean that one can naturally infer that Respondent will be found to have breached clause 16.5 of the contract which gave contractual force to “the duty of collaboration” when requiring the issue of documents or the performance of acts which were “necessary or desirable to comply with the terms of this contract”, a provision which is complemented by the provision contained in clause 16.7 of the contract in relation to the obligation to replace provisions which

² This formulation corresponds, strictly speaking, to that of Emmanuel Gaillard in “L'interdiction de se contredire au détriment d'autrui comme principe général du droit du commerce international”, cited by Craig, Park and Paulsson, [*International Chamber of Commerce Arbitration* (New York, Oceana Publications Inc. 2000)], page 648, with reference to the doctrine of estoppel which is part of the Anglo-Saxon legal system and is definitely akin to the theory of “own acts”.

³ The commentary in the Unidroit Principles of International Commercial Contracts in relation to principle 1.7 . . . states: “The parties' duty to act in accordance with good faith and fair dealing is of such a fundamental nature that the parties may not contractually exclude or limit it.” (Ministry of Justice and Law, *op. cit.*, p. 55)

prevented the performance of the contract with similar provisions enabling it to be performed, specifically the registration in the SIC.

Having analysed therefore the contractual provisions in question, the Tribunal considers the following to be relevant in relation to each one:

(a) The undertaking to collaborate reflected in clause 16.5 in relation to the registration of the contract in the SIC can be classified as an "obligation to try" (*obligación de medio*) in contrast to "obligations to produce results" (*obligaciones de resultado*). However, this classification does not mean that the first type of obligation, which is an undertaking on the part of the debtor to use all diligence to obtain a result which it cannot guarantee, is transformed into an instrument for reducing liability. As expressed in an arbitral award of 26 April 1998, the "obligation to try" is an obligation:

... in which the duty of the debtor is to conduct itself in such a way as to use all reasonable means within its power - namely knowledge, experience, material resources, diligence - to obtain the result expected by the creditor but without guaranteeing that it will be achieved. In this sense a failure to comply means a failure to use such means, that is to say providing the services without having adequate knowledge or experience, or failing to use the available scientific and technical resources, or failing to exercise ordinary diligence, all of which reflect the coming into existence of fault, that is to say it is an error of conduct which leads to the negative evaluation of the behaviour of the professional.⁴

Therefore, in the light of what has been established in the proceedings with regard to the conduct of Respondent in the matter under analysis, it follows that Claimant has been successful in demonstrating that [Respondent] did not exercise due diligence in relation to the obligation to try to procure the registration of the contract in the SIC, which is equivalent to having proved fault on the part of Respondent. This is one of the connotations of this kind of obligation, in contrast to the general rule on contractual liability where there is a presumption of fault on the part of the debtor in the event of failure to provide the service specified.

(b) As far as clause 16.7 is concerned, the Tribunal notes that the relevant part of the provision for the purposes of this part of the Award is not the inclusion of partial nullity which is contemplated by article 902 of the Commercial Code (*Código de Comercio*), but rather the reference to the amendment of the contract in order to sort out the difficulties involved in its registration and hence its performance, a situation which arose from the clarifications required by the director of the SIC, an official who in turn could be classified as a "state authority" whose interpretation of the contract ought to lead to the corresponding amendments in accordance with clause 16.7.

2. Given these conditions, and without it being necessary to carry out additional investigations, the Tribunal finds, and will so declare, that the conduct of Respondent in relation to the registration of the contract in the SIC was contrary to the obligation to try enshrined in clause 16.5 of the contract and to the positive obligation agreed in clause 16.7 thereof, and it remains only to repeat for the sake of greater clarity in relation to the duty of collaboration, which is central to various parts of the Award, that academic opinion, case law and even legislation itself are paying increasing attention to the duties of correction and fair dealing or, to put it in another way, to the duty to act in accordance with the standards of good faith at all times.

Thus for example article 1175 of the Italian Civil Code, the legislation which the Commercial Code (*Código de Comercio*) took as its model for the subject of obligations and contracts, provides: "The debtor and the creditor must act in accordance with the rules on correctness",

⁴ "Tribunal de Arbitramento Leasing Contra Fiduciaria", *Boletín Jurídico Financiero*, October 1997, pp. 42 and 43.

and article 1.7 of the aforementioned Unidroit Principles of International Commercial Contracts provides: “(1) Each party must act in accordance with good faith and fair dealing in international trade. (2) The Parties may not exclude or limit this duty”,⁵ which translates into the fact that the party, specifically the creditor, who has not acted with the diligence, measures and foresight which are required of him, as the case may be, is not only disqualified from alleging a breach of contract and seeking compensation for damages which, in the event that they have been suffered, would be due to his own fault, but, on a preventative and more direct basis, assumes the consequences of his dishonesty or turpitude and the attendant liability towards the other party where the services provided for in the contract cannot be performed and its purpose has become impossible or has been frustrated due to the lack of the activity (more than collaboration) which it should have shown and which is indispensable in order to achieve the common aim corresponding to the practical or socio-economic function of the contract.

Each party has duties in relation to clarity, precision, information and collaboration so that if a party omits to perform the necessary acts, it assumes exclusive responsibility for the adverse consequences of its inertia or negligence. This is more important and demanding in contracts involving collaboration and in the obligations which presuppose and impose such collaboration, and it may lead to the very extinction of the obligation in the absence of such collaboration by the creditor which prevented, hindered or delayed the exercise by the debtor of his right to release himself from the obligation by means of full performance and to obtain the desired economic result which is the natural consequence of the satisfaction of the reciprocal and common contractual duties and obligations.’

With respect to termination of the contract and damages

‘H - Issues Nos. 9 and 10

The issues, which correspond to point V (2) (c) (ix) and (x) of the Terms of Reference, are closely linked, as the first is a function of the investigations into the contractual breaches by Respondent, whilst the second depends on the outcome of the first.

As a result, and having determined that there was a breach of the contract by [Respondent], the Tribunal considers it appropriate to deal sequentially and jointly with the matters raised, the text of which reads as follows:

In the event that there is an affirmative answer to one or more of points (iv), (v), (vi), (vi) and (vii) above, whether it is appropriate to declare – and the declaration is actually made – that the contract, including addendum no. 1 and addendum no. 2, is terminated due to a breach of contract by Respondent.

and

In the event that the contract, including addendum no. 1 and addendum no. 2, is declared to be terminated for the reason indicated in point (ix) above, that Respondent be ordered to pay compensation for loss and damage and, if it is so ordered, what would be the heads and amounts of such compensation.

1. One of the cornerstones of the legislation on obligations and contracts involving interrelated services, which is based on the interdependent character of the contractual commitments whereby each of the parties is both creditor and debtor of the other – without implying simultaneous performance of the services – is the so-called “tacit resolatory condition” which is enshrined in article 1546 of the Civil Code (*Código Civil*) and article 870 of the Commercial Code (*Código de Comercio*). This means that, in the case of a bilateral contract, a breach by one party enables the other party at its election to request the rescission

or termination of the contract or its performance, in both cases with compensation for loss and damage, which will be compensatory if the choice is to demand the rescission or termination, or will cover the delay if the choice is to require its performance.

Our analysis in relation to the issues corresponding to points (B), (C), (D), (E) and (F) of this chapter shows on the one hand compliance with the requirement to have a valid bilateral contract and on the other the fact that Respondent has committed a definitive breach of its obligations, given that Claimant was ready to comply with its part of the agreement, and furthermore the arguments put forward by [Respondent] in defence of its conduct have no prospect of success . . .

2. Moreover, in accordance with developments in case law and academic thinking,⁶ based on equity, demanding that breaches of contract which mean that the resolutive action is successful have to be serious and material, the Tribunal finds that the breaches committed by [Respondent] merit such a classification from two points of view:

(a) In the first instance, due to the nature of the provisions which were not performed, starting from clauses 16.5 and 16.7 which required the adoption of measures aimed at permitting nothing less than the performance of the contract, and going on to clauses 10.2 and 10.3 which, respectively, required the parties to maintain their legal and economic viability and to request authorization from [Claimant] to dispose of a substantial part of the assets of [Respondent], and the breach of which made it impossible to give effect to the purpose of the contract which is set out in clause 2 thereof.

(b) Secondly, due to the conduct of Respondent which, as has been shown throughout this Award, without justification hindered the solution of the problems which would allow the registration of the contract in the SIC and hence its performance; inadequately carried on its business, which led to the intervention of the public services inspectorate owing to the decrease in its operational capacity; and, finally, erratically and deliberately omitted to request the authorization of [Claimant] to transfer assets and contracts to [X], excluding the contract at issue, so as to place itself in a position where it was totally incapable of meeting its obligations thereunder.

Having proved the breach of contract by Respondent with the characteristics noted above, Claimant had the option of choosing between performance of the contract or its termination, with the consequent damages. [Claimant] unequivocally elected for the first of these options by requesting the termination of the Contract, which it was legally entitled to do for the reasons stated, and this will be addressed in the operative part of the Award.

3. Having discussed the question of the termination of the contract due to its breach by Respondent, it is necessary to consider the consequent compensation for loss and damage that Respondent must pay to [Claimant], which the Tribunal develops as follows:

(a) In the terms of articles 1613 and 1614 of the Civil Code (*Código Civil*), the question of compensation would appear to be resolved merely by applying the concepts of *damnum emergens* and *lucrum cessans*, the first of which means a reduction in net worth (an outlay) and the second a frustrated gain (income not received) or, as the Supreme Court of Justice (*Corte Suprema de Justicia*), Civil Appeals Chamber, in its judgment of 7 May 1968 expressed it:

Damnum emergens relates to the loss of elements of net worth, payments which have been necessary or which will in future be necessary and the advent of liabilities, caused by the facts from which liability is sought to be deduced; whereas *lucrum cessans*, as the expression suggests, consists of all the certain gains which have not been received or remain to be received, based on the same facts. And the claim for compensation has to conform to this classification and adequately place the various heads of damage.

6

Article 7.3.1 of the Unidroit Principles of International Commercial Contract (cf. Ministry of Justice and Law, *op. cit.*, pp 228 and 229) has the following text and commentary:

"1) A party may terminate the contract where the failure of the other party to perform an obligation under the contract amounts to a fundamental non-performance.

(2) In determining whether a failure to perform an obligation amounts to a fundamental non-performance regard shall be had, in particular, to whether

(a) the non-performance substantially deprives the aggrieved party of what it was entitled to expect under the contract unless the other party did not foresee and could not reasonably have foreseen such result;

(b) strict compliance with the obligation which has not been performed is of essence under the contract;

(c) the non-performance is intentional or reckless;

(d) the non-performance gives the aggrieved party reason to believe that it cannot rely on the other party's future performance;

(e) the non-performing party will suffer disproportionate loss as a result of the preparation or performance if the contract is terminated.

(3) In the case of delay the aggrieved party may also terminate the contract if the other party fails to perform before the time allowed it under article 7.1.5 has expired."

"Whether in a case of non-performance by one party the other party should have the right to terminate the contract depends upon the weighing of a number of considerations. On the one hand, performance may be so late or so defective that the aggrieved party cannot use it for its intended purpose, or the behaviour of the non-performing party may in other respects be such that the aggrieved party should be permitted to terminate the contract.

On the other hand, termination will often cause serious detriment to the non-performing party whose expenses in preparing and tendering performance may not be recovered.

For these reasons paragraph (1) of this article provides that an aggrieved party may terminate the contract only if the non-performance of the other party is 'fundamental', i.e. material and not merely of minor importance."

The position is however, as the judgment transcribed above states, that for a loss to be compensated it must be “certain” rather than a “contingent” loss. The latter does not give a right to compensation, a sensitive subject where “unconsolidated losses” are involved and particularly acute when these losses are associated, as in the present case, with situations which did not materialize.

In this respect the Tribunal considers that the classification of damage as certain or as contingent, arising out of situations which were prevented from occurring, constitutes a necessary filter for the determination of the reasonable losses and the Tribunal will deal with this task later, taking as its point of reference the degree of seriousness and the scientific or technical solidity possessed by the prediction of what would have occurred had the harmful event not intervened, and from there go on to quantify the loss which will amount to 100% if there is legal certainty that the situation would have occurred. As Juan Carlos Henao notes:

Nothing of itself is contingent, save for physical or legal impossibilities. Everything is resolved in evidential terms. ... As the Mazeaud brothers say “the probabilities that have been lost are not always the ‘castles in the air’ of Perette and his jug of milk. Sometimes they are real.”⁷

(b) Having set out the aforementioned framework as the reference to evaluate the absence or presence of recoverable losses, the Tribunal also comes up against clause 14.3 of the Contract, the text of which clearly has its origins in the Anglo-Saxon legal systems and makes it necessary to venture into the area of “direct” and “indirect” loss in order precisely to understand the provision, which is consonant with the principle that the reparation for the loss, whilst it has to compensate the aggrieved party, which is a mandatory parameter in the evaluation, cannot impose exaggerated burdens on the liable party.⁸

Thus, as far as direct and indirect losses are concerned, the obligatory starting point is to state that in accordance with article 1616 of the Civil Code (*Código Civil*), absent a contractual provision, the debtor is only liable for direct losses, which means those losses which are a necessary and strict consequence of his unlawful act. In contrast, the debtor does not have any liability if the loss is not a certain and necessary product of his conduct or, in other words, there is no causal relationship, a characteristic which then becomes determinative when classifying a loss as direct.

Therefore what the judge has to evaluate is not the mediate or immediate character of the loss (temporal or spatial proximity) but rather its inevitability or causal nature, so that on the basis of such analysis he can determine the absence or presence of the obligation to compensate.

(c) It is not however enough to denote a loss as direct, as regard must also be had to the distinction between “foreseeable” and “unforeseeable” losses, with compensation being payable in relation to the former but not in relation to the latter, save where the debtor had acted fraudulently.

The distinction between foreseeable and unforeseeable losses in turn presents difficulties and has a limited development in case law, which is why the Tribunal must resort when

Evidently, a party who has already suffered the consequences of non-performance of the contract cannot be required in addition to take time-consuming and costly measures. On the other hand, it would be unreasonable from the economic standpoint to permit an

increase in harm which could have been reduced by the taking of reasonable steps. The steps to be taken by the aggrieved party may be directed either to limiting the extent of the harm, above all when there is a risk of it lasting for a long time if

such steps are not taken (often they will consist in a replacement transaction: see art. 7.4.5), or to avoiding any increase in the initial harm.” (Ministry of Justice and Law, *op. cit.*, pp. 252 and 253)

7

The commentary on article 7.4.3 of the Unidroit Principles of International Commercial Contracts gives the following illustration of the point: “... the owner of a horse which arrives too late to run in a race as a result of delay in transport cannot recover the whole of the prize money, even though the horse was the favourite.” (Ministry of Justice and Law, *op. cit.*, p. 245)

8

Henao, Juan Carlos, *El Daño. Análisis Comparativo de la Responsabilidad ExtraContractual del Estado en Derecho Colombiano y Francés* (Bogotá: Universidad Externado de Colombia, 1996) page 188.

9

This principle, which is firmly rooted in the *lex mercatoria*, is contained in article 7.4.8 of the Unidroit Principles of International Commercial Contracts on the terms and with the explanation set out below:

- “(1) The non-performing party is not liable for harm suffered by the aggrieved party to the extent that the harm could have been reduced by the latter party’s taking reasonable steps.
- (2) The aggrieved party is entitled to recover any expenses reasonably incurred in attempting to reduce the harm.”

“The purpose of this article is to avoid the aggrieved party passively sitting back and waiting to be compensated for harm which it could have avoided or reduced. Any harm which the aggrieved party could have avoided by taking reasonable steps will not be compensated.

characterizing it to the criterion of what is in the contemplation of the parties which is contained in the classic decision in *Hadley v. Baxendale*, which was handed down in 1854 and which said:

... Now we think the proper rule in such a case as the present is this:— Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally i.e. according to the usual course of things, from such breach of contract itself, or such as may be reasonably supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.¹⁰

Thus the judge who follows the “foreseeability” rule mentioned above will have to conduct investigations into the type of losses which ordinarily and reasonably should have been within the contemplation of the party as associated with its breach, in order to decide from there whether or not compensation should be ordered and, if so, the amount of such compensation.¹¹

(d) Thus the Tribunal will proceed to evaluate the figures proved in the proceedings as making up *damnum emergens* and *lucrum cessans* using the following parameters:

- i. Fullness of the compensation, referable to the need to place the aggrieved party in the position it would have been in absent the loss;
 - ii. Certainty of the loss, material in the case of consequential loss (crystallized situation) and legal in the case of loss of profit (contingent situation);
 - iii. Direct character, that is to say resulting exclusively from the cause-effect relationship;
- and
- iv. Foreseeability, referring to the harmful consequences of their actions being within the reasonable contemplation of the Parties.

Finally, on the question of the connotations of having a strict causal relationship and the need for the loss of profit (*lucrum cessans*) claimed by Claimant to have been foreseeable, the Tribunal considers it sufficient to mention, in relation to the first point, that the only reason proved in these proceedings for the frustration of Claimant’s expectations is the inexcusable non-performance of Respondent. And, in terms of the second point, the requirement of “foreseeability” is clearly met as whatever method of analysis is used the loss of profit corresponds, as article 7.4.4 of the Unidroit Principles of International Commercial Contracts¹² states, to “what [Respondent] could have reasonably have contemplated at the time of entering into the contract as the probable consequence of its breach”, or what was “in the contemplation of both parties”, as stated in *Hadley v. Baxendale*.¹³ It is quite clear . . . that the essential objective of [Claimant] in taking part in the public tender and, naturally, in entering into the Contract, was to obtain a return on its investment.

The matters discussed hitherto suffice to conclude that, as will be set out in the operative part of the Award, the Tribunal will order Respondent to pay damages in the sum of US\$. . . , corresponding to Claimant’s loss of profit.¹⁴

¹⁰ Court of Exchequer, 1854, 9 Ex. 341, 156 Eng. Rep. 145.

¹¹ For the Arbitral Tribunal article 7.4.4 of the Unidroit Principles of International Commercial Contracts adopts the rule in *Hadley v. Baxendale* without reservation when it provides:

“The non-performing party is liable only for harm which it foresaw or could reasonably have foreseen at the time of the conclusion of the contract as being likely to result from its non-performance.”

¹² See *supra* note 11.

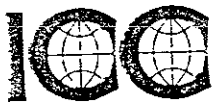
¹³ See 3 (c) above.

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