

TWELFTH ANNUAL WILLEM C. VIS
INTERNATIONAL COMMERCIAL ARBITRATION MOOT
2004 – 2005

CLAIMANT'S MEMORANDUM



CLAIMANT:

Mediterraneo Confectionary Associates, Inc.
121 Sweet Street
Capitol City
MEDITERRANEO

RESPONDENT:

Equatoriana Commodity Exporters, S.A.
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Port City
EQUATORIANA

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A. List of Abbreviations

| <u>Abbreviation</u> | <u>Full text</u> |
|----------------------------|---|
| Arb Int | Arbitration International |
| Art / Artt | Article / Articles |
| ASA | Swiss Arbitration Association |
| Bd. | Band (Volume) |
| BGH | Bundesgerichtshof (German Supreme Court) |
| BGHZ | Entscheidungen des Deutschen Bundesgerichtshofs in Zivilrechtssachen |
| CCIG | Geneva Chamber of Commerce and Industry |
| CISG | United Nations Convention on Contracts for the International Sale of Goods of 1980 |
| CLOUT | Case Law on UNCITRAL Texts |
| DIS | Deutsche Institution für Schiedsgerichtsbarkeit |
| e.g. | <i>exempli gratia</i> (for example) |
| ECE | Equatoriana Commodity Exporters, S.A. (Respondent and Counter-Claimant) |
| ECJ | European Court of Justice |
| Ed. | Edition |
| EGCMO | Equatoriana Government Cocoa Marketing Organization |
| et alt. | <i>et alteri</i> (and others) |
| et seq. / et seqq. | <i>et sequens / et sequentes</i> (the following page(s) or paragraph(s)) |
| F.D.A. | Food and Drug Administration |
| FS | Festschrift |
| GER | Germany |
| i.e. | <i>id est</i> (that is) |
| IBLJ | International Business Law Journal |
| ICC | International Chamber of Commerce (International Court of Arbitration) |
| Int ALR | International Arbitration Law Review |
| IPRax | Praxis des Internationalen Privat- und Verfahrensrechts |
| IPRspr | Die deutsche Rechtsprechung auf dem Gebiete des internationalen Privatrechts im Jahre |
| ITA | Italy |



| | |
|-----------------------|---|
| LCIA | The London Court of International Arbitration |
| LG | Landgericht (German District Court) |
| LIFFE | London International Financial Futures and Options Exchange |
| MAL | UNCITRAL Model Law on International Commercial Arbitration |
| MCA | Mediterraneo Confectionary Associates, Inc. (Claimant and Counter-Respondent) |
| NYC | New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 |
| No. | Number |
| NYBOT | New York Board of Trade |
| O.R. | Official Records |
| OCA | Oceania Commodity Association |
| OLG | Oberlandesgericht (German Appellate Court) |
| OSLJ | Ohio State Law Journal |
| p. / pp. | page / pages |
| para. / paraa. | paragraph / paragraphs |
| PECL | Principles of European Contract Law |
| QBD | Queen's Bench Division (Civil Court, England) |
| RabelsZ | Rabels Zeitschrift für ausländisches und internationales Privatrecht |
| RIW | Recht der Internationalen Wirtschaft |
| S.T. | Substitute Transaction |
| ULIS | Uniform Law on the International Sale of Goods |
| UN | United Nations |
| UNCITRAL | United Nations Commission on International Trade Law |
| UNIDROIT | <i>Institut International pour l'Unification du Droit Privé</i> |
| USD | United States Dollars |
| w/o | without |
| YB | Yearbook |
| ZfVR | Zeitschrift für Rechtsvergleichung, internationales Privatrecht und Europarecht |



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C. Statement of Facts

§ Conclusion and content of Cocoa Contract 1045

- 1 On **19 Nov 2001** Mediterraneo Confectionary Associates, S.A., the Claimant (hereinafter referred to as MCA), received a phone call from Equatoriana Commodity Exporters, Inc., the Respondent (hereinafter referred to as ECE), offering 400 metric tons of cocoa at a price of USD 1,240.75 per metric ton. MCA accepted. A contract (hereinafter referred to as Cocoa Contract 1045), containing an arbitration clause calling for arbitration under the Arbitration Rules of the Chamber of Commerce and Industry of Geneva (hereinafter referred to as the Geneva Rules) in Vindobona, Danubia, was signed by ECE and MCA on **19 and 23 Nov 2001**. The date for delivery was to be fixed by ECE between **1 Jan and 28 Feb 2002** for actual delivery between **1 Mar and 31 May 2002**.

§ Embargo and non-fulfillment of Cocoa Contract 1045 by ECE

- 2 On **24 Feb 2002** ECE informed MCA that the Equatoriana Government Cocoa Marketing Organization (hereinafter referred to as the EGCMO) had imposed an export ban (hereinafter referred to as the Embargo) on cocoa from Equatoriana and that ECE would not be able to deliver as promised. On **5 Mar 2002**, MCA replied that ECE could deliver cocoa from any country, as Cocoa Contract 1045 was not specifically for Equatorianese cocoa and that the cocoa would be needed later that year. If ECE did not deliver by then, MCA would purchase the cocoa elsewhere and hold ECE liable for damages. ECE did not reply. On **18 May 2002**, ECE delivered 100 metric tons which the EGCMO had released. ECE announced that the 300 metric tons outstanding would be delivered in the very near future. Until **August 2002**, MCA inquired on several occasions as to the delivery of the cocoa outstanding. On **15 Aug 2002**, MCA informed ECE of its urgent need to receive the cocoa and reiterated that the cocoa would be purchased elsewhere if ECE did not deliver shortly. Again ECE did not reply.

§ Substitute transaction made by MCA, avoidance of contract and damages

- 3 On **24 Oct 2002** MCA made a substitute transaction for 300 metric tons of cocoa at the then current market price of USD 2,205.26 per metric ton. On **25 Oct 2002**, MCA informed ECE of the substitute transaction and thereby terminated Cocoa Contract 1045 implicitly. On **11 Nov 2002** MCA demanded USD 289,353 damages as announced on **25 Oct 2002**. The Embargo was lifted on **12 Nov 2002**. On **15 Nov 2002** MCA, in an abundance of caution, explicitly declared that Cocoa Contract 1045 was avoided.



§ **Conclusion and content of Sugar Contract 2212**

4 In **Nov 2003**, ECE sold 2,500 metric tons of sugar to MCA for a total price of USD 385,805. The contract (hereinafter referred to as Sugar Contract 2212) was signed on **20 and 21 Nov 2003**. It contained an arbitration clause calling for arbitration under the Rules of Arbitration of the Oceania Commodity Association (hereinafter referred to as OCA) in Port Hope, Oceania. A dispute arose regarding the quality of the delivered sugar and the payment of the contract price.

§ **Claim and counterclaim, objection to jurisdiction of the Arbitral Tribunal**

5 On **5 Jul 2004** MCA filed a claim to the Chamber of Commerce and Industry of Geneva (hereinafter referred to as CCIG) concerning the dispute arising out of Cocoa Contract 1045. MCA was informed on **16 Jul 2004** by the CCIG that an amended version of the Swiss Rules of International Arbitration (hereinafter referred to as the Swiss Rules), would be applied to the arbitration proceedings although it came into force only on **1 Aug 2004**. This amendment would allow arbitration under the Swiss Rules to be conducted outside of Switzerland. In its answer to the claim, on **10 Aug 2004** ECE filed a counterclaim concerning the dispute arising out of Sugar Contract 2212 which it based on Art 21(5) Swiss Rules. MCA objected to the application of Art 21(5) and the jurisdiction of the presiding arbitral tribunal (hereinafter referred to as the Arbitral Tribunal) in its answer to the counterclaim dated **31 Aug 2004**.

D. Statement of Purpose

6 Based on the above facts, MCA will demonstrate

- § that ECE is not exempted from paying damages under Art 79 CISG;
- § that ECE was in fundamental breach of Cocoa Contract 1045 under Art 25 CISG;
- § that MCA rightfully avoided Cocoa Contract 1045 on 25 Oct 2002;
- § that MCA was justified in making a substitute transaction;
- § that MCA is therefore entitled to claim the difference between the contract price and the price for the substitute transaction, i.e. USD 289,353, as damages;
- § that the Arbitral Tribunal does not have jurisdiction over the counterclaim arising out of Sugar Contract 2212; and
- § that, should the Arbitral Tribunal find that it has jurisdiction, the counterclaim would be limited to a set-off defense.



E. Claim

1. The Embargo does not excuse ECE from paying damages under Article 79 CISG.

7 In the following, MCA will demonstrate that ECE has breached Cocoa Contract 1045. ECE must therefore pay damages, as the Embargo did not make the fulfillment of the contract impossible. MCA will demonstrate that Cocoa Contract 1045 was in fact not specifically for cocoa of Equatorianese origin. Therefore ECE could have delivered any cocoa of similar quality.

1.1 As Cocoa Contract 1045 was not for Equatorianese cocoa, the Embargo did not prevent ECE from fulfilling the contract.

8 According to Cocoa Contract 1045 (Claimant's Exhibit No. 2) ECE was obliged to set the delivery date in the course of January and February 2002 for delivery of 400 metric tons of cocoa during the months of March to May 2002.

9 Pursuant to Art 33(b) CISG, if a period of time is fixed by or determinable from the contract, the seller must deliver at any time within that period. By 31 May 2002, only 100 metric tons of cocoa had been delivered and ECE had not set a delivery date for, let alone delivered the remaining 300 metric tons of cocoa. This constitutes a breach of contract under Art 33(b) CISG for which ECE is liable. The Embargo does not exempt ECE from this liability.

10 Generally, under the CISG, contracting parties are required to perform all their obligations under the contract and are therefore "*liable for any objective failure to perform, regardless of the reasons for the failure*" (*Schlechtriem in Schlechtriem*², Art 79, para. 6, p. 603). No subjective fault is needed for a party to be liable for the damage arising from its conduct (*Tallon in Bianca/Bonell*, Art 79, section 1.1, p. 573). A party can only be exempted from paying damages in very special circumstances, such as an impediment impossible to avoid or overcome by all reasonable measures [**paraa. 26 et seqq.**].

11 Governmental embargoes are usually considered to be such impediments (*Magnus in Honsell*, Art 79, para. 12, p. 988), but only if the embargo makes the delivery of the goods impossible. In the present case, ECE failed to deliver 300 metric tons of cocoa. Even though



the Embargo might have had an effect on ECE's ability to deliver Equatorianese cocoa, i.e. prevented ECE from obtaining the goods from its usual source, the Embargo did not make the delivery of cocoa impossible. ECE could still have fulfilled Cocoa Contract 1045 by delivering cocoa of similar quality from another country.

1.1.1 Cocoa Contract 1045 did not contain an explicit agreement requiring the cocoa to be of Equatorianese origin.

12 Cocoa Contract 1045 was for “400 metric tons net of cocoa beans” (Claimant's Exhibit No. 2). No specific place of origin was agreed upon or even mentioned either in the written contract or in the preceding phone call (see confirmation of phone call in Claimant's Exhibit No. 1). Also, no specific usages or trade terms have been explicitly agreed on.

1.1.2 Cocoa Contract 1045 did not contain an implicit agreement requiring the cocoa to be of Equatorianese origin.

13 To determine if a contract contains an implicit agreement calls for careful consideration of two aspects under Art 8 CISG. These are:

§ Objective intent

14 The intent of the parties, as expressed in the contract, has to be interpreted from an objective point of view (*Schmidt-Kessel* in *Schlechtriem*⁴, Art 8, para. 10, p. 167). In other words, one must consider the impression an objective observer would have after analyzing the terms and circumstances of the contract. In the present case, special consideration has to be given to (a) the relation between the agreed price and the average market price, (b) the use of the NYBOT standard form of cocoa contracts, and (c) the positive and negative effects a specification of origin would have caused.

15 (a) The price of the cocoa in Cocoa Contract 1045 equals the average basic market price for cocoa for the month of November 2001 when the contract was signed (see Respondent's Exhibit No. 3) and corresponds to the price for lowest quality cocoa in Group C of the NYBOT (Respondent's Exhibit No. 1) and Group 5 of the LIFFE (Respondent's Exhibit No. 2). This leads to the conclusion that Cocoa Contract 1045 was for cocoa coming from a



country in one of the specified groups (hereinafter together referred to as Lowest Quality Groups). This fact is not only undisputed, but also stated by ECE itself in its Statement of Defense (Problem, p. 26).

- 16** However, contrary to ECE's statement that the Lowest Quality Groups contain cocoa from Equatoriana and from almost no other source (Problem, p. 26), there are at least six other countries that produce cocoa of said quality. The Growths listed in Group C of the NYBOT are those of Bolivia, Haiti, Indonesia-Sulawesi, Malaysia, Para (Brazil), Peru and Sanchez (Domenican Republic). All these Growths, except Malaysia which is in Group 4 of the LIFFE, are also included in Group 5 of the LIFFE. There were a multitude of suppliers from whom cocoa could have been purchased (Procedural Order No. 2, para. 25). Consequently the fact that Cocoa Contract 1045 was for cocoa of the Lowest Quality Groups does not constitute a reason to assume that the cocoa had to come from Equatoriana. On the contrary, ECE could have delivered cocoa from any of the countries listed in the Lowest Quality Groups to fulfill its contractual obligation.
- 17** (b) Cocoa trade under the NYBOT Cocoa Rules is primarily conducted with regard to groups of quality and not to specific places of origin (Respondent's Exhibit No. 1). Therefore, unless otherwise stated by the parties, a contract refers to cocoa belonging to said groups of quality, regardless of the place of origin. This is further supported by the fact that, according to the NYBOT Contract Specifications for Cocoa Futures and Options (published at <http://www.nybot.com/specs/cc.htm>), the NYBOT standard form of contracts "*calls for delivery of any kind of cocoa bean - the growth of any country or clime, including new or yet unknown growths*". As the contracting parties, i.e. MCA and ECE, (hereinafter referred to as the Parties) used the NYBOT standard form of contracts for Cocoa Contract 1045 and as the contract did not specify Equatorianese cocoa, it was for "*any kind of cocoa bean*".
- 18** (c) Finally, contracting for cocoa of a specific place of origin was not in the interest of MCA, as this would have imposed an unnecessary limitation without obvious gain for either of the Parties. Such a limitation would only have been in MCA's interest if it had brought MCA some advantage, for example if the specific place of origin of the ingredients had resulted in an improvement in image or quality of the products manufactured. This, however, is not the case with MCA's production. The use of lowest quality cocoa shows that MCA's confectionary is not intended for the high quality segment. Advertising the use of high quality



ingredients from a specific place of origin is not unusual but it would be highly unreasonable to specially advertise the use of low quality ingredients. Therefore, specific Equatorianese origin would not have brought any benefit to MCA's business. Consequently, objective interpretation leads to the conclusion that the origin of the cocoa was irrelevant.

§ Subjective intent

19 When interpreting a contract, subjective intent is relevant only if the recipient of the declaration could not have been unaware of it (see Art 8(1) CISG). Even if serious doubts had arisen as to possible differences between ECE's objective and subjective intent, MCA was not obliged to investigate further (see *Witz/Salger/Lorentz*, Art 8, para. 5, p. 98). It may be true that ECE's intent was to sell Equatorianese cocoa. But no grounds existed for MCA to assume that this was in fact the case as no explicit reference was ever made to the place of origin of the cocoa contracted for.

20 According to Art 8(3) CISG, all the circumstances of the case have to be considered when determining the intent of the parties. The CISG explicitly points out the negotiations, the practices and usages [**paraa. 21 et seqq.**], as well as the subsequent behavior of the parties. No detailed negotiations were conducted for Cocoa Contract 1045. The phone call preceding the written contract only gave a brief summary of what would be contained in the contract. In its letters dated 5 Mar 2002 (Claimant's Exhibit No. 4) and 15 Aug 2002 (Claimant's Exhibit No. 7), MCA made it clear to ECE that it did not think that Cocoa Contract 1045 called for delivery of cocoa of a specific origin, i.e. Equatorianese cocoa. However, ECE did not in any of its letters reply to this specific statement, thereby not disputing this fact. Subsequent behavior such as this has to be considered when interpreting the intent of the parties under Art 8(3) CISG.

1.1.3 ECE has not proved the existence of any international trade usages or established practices with regard to the origin of the cocoa.

21 As stated [**para. 20**], in determining whether a contract contains an implicit agreement, thought has to be given to any established practices between the parties and to international trade usages.



§ Practices established between the Parties

- 22 No practices have been established between MCA and ECE as regards the origin of the cocoa. For a practice to be established between the parties, the majority of the past contracts must have been performed in the same special manner to which none of the parties have raised objections (*Junge in Schlechtriem*², Art 9, para. 7, p. 78). It is not disputed that in the past ECE has delivered Equatorianese cocoa. However, the previous contracts did not contain an agreement, or even an understanding on both sides, that the cocoa should be exclusively of Equatorianese origin (Procedural Order No. 2, para. 16). MCA never had any reason to object to the cocoa which was delivered, as it conformed to what was agreed, i.e. cocoa of the Lowest Quality Groups. Objecting to the delivery of Equatorianese cocoa would have been a breach of contract on MCA's part as ECE was left free to choose the place of origin of the cocoa. While it may have been a habit of ECE to deliver Equatorianese cocoa, no practice relating to an agreement on the specific place of origin can be derived from this.
- 23 Also, for a practice to be established, both parties have to have unequivocal trust in the relevance of the practice for similar future business transactions (*Honnold*², Art 9, para. 116, p. 175; see also LG Frankenthal [GER], 17 Apr 1997, 8 O 1995/95). MCA never had a reason to trust in or rely upon the cocoa as coming from a specific place of origin. Since in past contracts no reference was ever made to the Equatorianese origin of the cocoa to be delivered, there was no reason to trust in the existence of a practice concerning the place of origin of the cocoa. If ECE were to claim such practices, the burden of proof would be on it.

§ International trade usages

- 24 ECE has neither claimed nor proved the existence of any international trade usages. No international trade usages with respect to the place of origin are known to MCA. If any such usages existed, it would have been for ECE to prove their existence.

- 25 **Conclusion:** Interpretation of Cocoa Contract 1045 shows that there was neither an explicit nor an implicit agreement as regards the specific origin of the cocoa. ECE could therefore have delivered cocoa from any country in the Lowest Quality Groups.



1.2 Alternatively, should the Arbitral Tribunal find that Cocoa Contract 1045 was indeed for Equatorianese cocoa, Article 79 CISG still does not exempt ECE from paying damages considering that ECE could have overcome the impediment.

26 If the Arbitral Tribunal finds that Cocoa Contract 1045 was in fact for Equatorianese cocoa, the Embargo does not exempt ECE from paying damages under Art 79 CISG as ECE did not take all reasonable measures to overcome it. Exemptions are very rarely granted (see *Winship*, *RabelsZ* [2004] 68, p. 503; so far, only in five cases) and only serve as a last resort. MCA will show that ECE should have asked for an exemption from the Embargo and provided MCA with a commercially reasonable substitute.

1.2.1 In order to overcome the alleged impediment, ECE should have requested an exemption from the Embargo of the EGCMO, especially towards its end.

27 Art 79 CISG imposes upon the seller the obligation to undertake all reasonable measures to overcome an impediment. In its letter dated 15 Aug 2002 (Claimant's Exhibit No. 7) MCA had clearly stated that the timely receipt of the remaining 300 metric tons of cocoa was of prime importance to it as it was running low on stock. ECE did not attempt to ask the EGCMO for an exemption from the Embargo. Even if requests by other exporters had been rejected, an attempt by ECE would have been reasonable. Especially towards the end of the Embargo the EGCMO might have agreed to an exemption, as it possibly already had plans to lift the Embargo shortly.

1.2.2 ECE should have delivered cocoa from another country as a commercially reasonable substitute.

28 In order to be exempted, ECE would have had to offer a "*commercially reasonable substitute*" (*Stoll/Gruber in Schlechtriem*⁴, Art 79, para. 23, p. 758). Such a substitute can be required if it can fulfill the purpose of the contract (*Stoll/Gruber in Schlechtriem*⁴, Art 79, para. 23, p. 758) and if it leads to complete or approximate fulfillment of the contract (*Magnus in Staudinger*¹³, Art 79, para. 34, p. 696). Minor deviations from the goods initially owed are reasonable as long as the substitute can fulfill the contract's goal. Even if Cocoa Contract 1045 had been for Equatorianese cocoa, ECE could have provided MCA with any cocoa of the Lowest Quality Groups as a reasonable substitute, especially as such cocoa was



widely available on the market and MCA itself was able to purchase the substitute goods. The obligation to offer such a substitute depends on the extent to which the other party is affected by the non-fulfillment (*Achilles*, Art 79, para. 8, p. 239). ECE could not have been unaware of the fact that MCA would have had to halt its production [para. 42] if it had not received the cocoa in time [see table para. 42]. Because of this impending serious disruption and the fact that delivery of cocoa from another country would have been only a minor deviation, easy to achieve and still serve MCA's purpose, there was a definite obligation on ECE's part to deliver such a substitute.

- 29 The duty to offer a substitute cannot be extended so far as to modify the contractual obligation unilaterally (*Tallon in Bianca/Bonell*, Art 79, section 2.6.5, p. 582). This limitation serves as a protection for the injured party that should not be forced to accept anything as a substitute. However, MCA was in no need of such protection as it had stated on several occasions (Claimant's Exhibit No. 4; Claimant's Exhibit No. 7) that it was willing to accept any cocoa of the Lowest Quality Groups. On the other hand, the seller cannot be compelled to deliver whatsoever the buyer requires. However, requiring ECE to deliver cocoa of Lowest Quality Groups as a substitute was reasonable, since such cocoa was widely available on the market. ECE, a commodity trader, could certainly have purchased such cocoa without difficulty. The costs incurred by the party in breach in delivering such a substitute are irrelevant. Even greatly increased expenses do not make the provision of the substitute commercially unreasonable (OLG Hamburg [GER], 28 Feb 1997, 1 U 167/95). Thus ECE would have even been obliged to deliver cocoa of a higher quality group.

- 30 **Conclusion:** Even if the Arbitral Tribunal finds that Cocoa Contract 1045 was indeed for Equatorianese cocoa, ECE is not exempted from paying damages. ECE should have overcome the alleged impediment by asking for an exemption or delivering cocoa from a different country as a commercially reasonable substitute.

- 31 **Answer to Procedural Order No. 1, Question 1: Cocoa Contract 1045 was not for Equatorianese cocoa. ECE could have fulfilled the contract by supplying MCA with any cocoa of the Lowest Quality Groups. Therefore, ECE is not exempted from paying damages under Art 79 CISG.**



2. MCA is entitled to claim damages for partial non-delivery.

32 ECE was, under Cocoa Contract 1045, obliged to deliver 400 metric tons of cocoa of the Lowest Quality Groups by 31 May 2002 [paraa. 8 *et seq.*]. Only 100 metric tons were delivered (18 May 2002). The remaining 300 metric tons were never delivered. This partial non-delivery constitutes a breach of contract by ECE under Art 33 CISG.

33 According to Art 45 CISG, when the seller is in breach of contract, the buyer can make use of the remedies under Articles 46 to 52 CISG and can claim damages under Articles 74 to 77 CISG. Under Art 75 CISG the buyer can claim damages if he has bought goods in replacement and declared avoidance of the contract. Under Art 49(1)(a) CISG, fundamental breach is a prerequisite for avoidance. In cases of delay, when the injured party intends to declare avoidance of the contract, Art 49(1)(b) CISG requires that the injured party sets an additional period of time before avoidance can be declared, as delay as such does not automatically amount to fundamental breach. However, in certain cases delay alone can amount to a fundamental breach and consequently no additional period of time has to be fixed by the injured party (*Müller-Chen in Schlechtriem*⁴, Art. 49, para. 5, p. 550).

34 MCA will show that the breach of contract by ECE must be considered fundamental under Art 25 CISG for several reasons, and that any one of these reasons alone would suffice for a fundamental breach to exist. Also, MCA will demonstrate that it avoided Cocoa Contract 1045 implicitly on 25 Oct 2002 and is thus entitled to claim damages under Art 75 CISG.

2.1 MCA has rightfully and effectively avoided Cocoa Contract 1045 under Articles 25, 26 and 49 CISG.

2.1.1 ECE committed a fundamental breach of Cocoa Contract 1045 under Article 25 CISG.

35 Art 25 CISG defines a fundamental breach as “*a breach of a contractual obligation which results in such detriment to the other party as to substantially deprive it of what it was entitled to expect under the contract*”. The monetary value of the contract, the monetary harm caused by the breach and the extent to which the breach interferes with other activities of the injured party are all factors to be taken into account when defining the extent of the detriment



(*Secretariat Commentary*, Art 23, O.R., p. 26). The interference with other activities of the injured party is of special importance in the case at hand. The following section will show that ECE's breach of contract was fundamental.

2.1.1.1 The delay in delivery by ECE caused MCA substantial detriment.

- 36 A delay in performance can amount to a fundamental breach if it causes substantial detriment (*Secretariat Commentary*, Art 43, O.R., p. 39-40). In this case, several different factors caused MCA substantial detriment. Although either of these factors amounts by itself to fundamental breach, in this case the fundamental breach consists of a combination of these factors.

§ Unreasonable delay in delivery

- 37 An unreasonable delay in delivery can amount to substantial detriment (*Müller-Chen in Schlechtriem*⁴, Art 49, para. 5, p. 550). At the time of avoidance of Cocoa Contract 1045, there was already a delay in delivery of over five months. This delay is certainly unreasonable. In case-law, a delay of just two months has been considered unreasonable (Pretura circondoriale de Parma [ITA], 24 Nov 1989, 77/89; see also ICC Award No. 8128, 1995). A delay in delivery of over 5 months is especially unreasonable for commodities readily available on the market. Cocoa was available as "*there were a multitude of suppliers from whom the cocoa could have been purchased*" (Procedural Order No. 2, para. 25).

§ Uncertainty with regard to the delivery and the delivery date

- 38 Substantial detriment can also be caused when the seller promises the buyer again and again to deliver at a later time and thereby makes him wait for an unreasonably long period of time (*Müller-Chen in Schlechtriem*⁴, Art 49, para. 5, p. 550). ECE led MCA to believe that delivery would be made within a reasonable period of time. First in its letter dated 7 May 2002 (Claimant's Exhibit No. 6) ECE stated that it was looking forward to shipping the remaining 300 metric tons "*in the very near future*". This was repeated in telephone calls during the months of June and July (see Problem, p. 3). ECE's conduct caused MCA substantial detriment as it repeatedly led MCA to believe that the cocoa would be delivered "*soon*". ECE never had grounds for this assumption.



39 ECE was, according to Cocoa Contract 1045, obliged to set a date for delivery. Good faith in contractual relationships required that ECE keep MCA up-to-date as to any circumstances affecting delivery. ECE should therefore have kept MCA informed on the status of the Embargo. If ECE were aware of the rumors concerning the end of the Embargo, it should have informed MCA thereof. This would not have constituted a burden for ECE, and would on the other hand have been of great advantage to MCA. Knowing about the status of the Embargo would have allowed MCA to adapt better to the inconvenience imposed on it by ECE's breach of contract.

§ MCA had special interest in timely delivery and made time of the essence

40 Delay can amount to a fundamental breach if the buyer has a special interest in the delivery date, e.g. a contract for seasonal goods or a contract where time is explicitly made of the essence (*Schlechtriem in Schlechtriem*², Art 25, para. 18, p. 182). Such interest needs to be recognizable by the seller when the contract is concluded (OLG Düsseldorf [GER], 24 Apr 1997, 6 U 87/96). In this case, time was not explicitly made of the essence when the contract was concluded, but afterwards it was made of the essence implicitly. As an exception to the rule that a contract can only be modified by both parties' consent (Art 29 CISG), the delivery date can unilaterally be made essential by the buyer, even after the conclusion of the contract, by setting an additional period of time pursuant to Art 47 CISG (*Honnold*, Art 49, para. 305, p. 385). MCA did not set ECE a specific deadline for the additional period as required by Art 47 CISG. However, in its letter dated 15 Aug 2002 MCA implicitly made time of the essence (Claimant's Exhibit No. 7) by unambiguously stating that it was running low on supplies and that it would have to purchase elsewhere if ECE did not deliver promptly. As ECE could not have been unaware of MCA's need to receive the cocoa soon, the further delay in delivery after 15 Aug 2002 constitutes a fundamental breach.

41 To hold the lack of a specific deadline against MCA would contradict the principle of good faith in contractual relationships. MCA showed this good faith by not setting a narrow period of time during which ECE had to deliver the remaining 300 metric tons of cocoa. On the contrary, MCA tried to give ECE the longest possible period for delivery without endangering its own production. MCA thereby wanted to maintain their good business relationship (Claimant's Exhibit No. 8). At the same time MCA made clear that it was in



urgent need of the cocoa. Although MCA's statement of urgency lacks a specific deadline, MCA has made time of the essence in a manner close to setting an additional period of time under Art 47 CISG. Thus, the continuing delay by ECE amounts to substantial detriment.

§ Loss of interest by MCA

42 MCA lost interest in the delivery of ECE's cocoa when it became clear that it would not arrive in time to ensure MCA's continuous production. Delay can cause substantial detriment when it causes the buyer to lose interest in the performance (*Graffi*, IBLJ [2003] 3, p. 339). The prerequisite for this is that the seller knew or must have known of the buyer's special interest (*Schlechtriem in Schlechtriem*⁴, Art 25, para. 14, p. 314). The continuous production constituted MCA's interest in the contract. As MCA and ECE had been doing business together for a long time, it must have been clear to ECE that MCA as a confectionary producer would need the cocoa not just for resale but for its own production. Therefore, ECE must also have known that MCA would run out of stock if it did not receive the cocoa shortly. The following table shows that MCA would have had to stop production in mid-November if it had not made the substitute transaction on 24 Oct 2002. Because of the possibility of a halt in production, MCA lost interest in delivery as of that date.

| Table of Production and Stocks* | | | |
|---------------------------------|--|-------------------|------------|
| Date | Action taken | Cocoa in Stock ** | |
| | | w/o S.T. | with S.T. |
| 24 Oct 2002 | Substitute transaction | 100 | |
| 7 Nov 2002 | Estimated arrival of substitute cocoa | 42 | |
| 12 Nov 2002 | Lifting of the Embargo | 21 | 321 |
| 13 Nov 2002 | Earliest possible delivery for shipment | 17 | 317 |
| 17 Nov 2002 | Cessation of production without substitute delivery | 0 | 300 |
| 27 Nov 2002 | <i>Earliest estimated arrival of ECE's cocoa</i> | 300 | 559 |

*Approximate figures, calculated on the basis of an average yearly requirement (see procedural order No. 2, para. 24) of 1,500 metric tons of cocoa (4.11 metric tons per day). Two weeks are estimated for shipment.

** In metric tons. After 7 Nov 2002, the figures on the left side represent the amount of cocoa that would have been in stock without the substitute transaction and the figures on the right side the amount including the substitute transaction.

43 By the time of the substitute transaction, on 24 Oct 2002, MCA had slightly more than 100 metric tons in stock. MCA would only have been able to uphold its production at a regular



level for less than a month, i.e. until mid-November. On 24 Oct 2002, the delay in delivery had already lasted over 5 months. MCA had no reason to believe that ECE would deliver the 300 metric tons outstanding before mid-November.

- 44 The Embargo was lifted on 12 Nov 2002, which MCA could not anticipate when the substitute transaction was made on 24 Oct 2002. Even if MCA had known about this, it was unlikely that ECE's delivery would have arrived in time to secure MCA's continuous production. MCA would have needed the cocoa before 17 Nov 2002. Even if the cocoa had been shipped immediately after the Embargo was lifted on 12 Nov 2002, it is doubtful that the cocoa would have arrived by 17 Nov 2002, i.e. within five days.

2.1.1.2 The fundamental breach was foreseeable to ECE.

- 45 Art 25 CISG requires the breach and its consequences to be foreseeable. According to this requirement, a breach is considered fundamental only if the party in breach did foresee or a reasonable person of the same kind in the same circumstances would have foreseen such a result.
- 46 ECE and MCA had been doing business together for a long time. It must therefore have been foreseeable to ECE (a) that MCA would run out of supplies if the delivery were delayed by over 5 months, (b) that the longer the uncertainty lasted in which MCA had to act, the higher the possibility of substantial detriment became, (c) that delivery soon after MCA's notice dated 15 Aug 2002 would be necessary and extending the delay further would result in substantial detriment and (d) that MCA would eventually lose interest in the contract if the goods were not delivered in time to ensure its continuous production.

- 47 **Conclusion:** ECE's delay in delivery of over 5 months caused MCA substantial detriment for several reasons. The unreasonable delay in delivery, the uncertainty with regard to the delivery date, MCA's interest in timely delivery and MCA's loss of interest, all separately and together amount to substantial detriment. The detriments caused by the delay were also foreseeable to ECE. Therefore ECE's delay amounted to a fundamental breach of Cocoa Contract 1045 under Art 25 CISG.



2.1.2 MCA was entitled to avoid Cocoa Contract 1045 under Article 49(1)(a) CISG.

48 The remedy of avoidance is granted to the injured party that can no longer be expected to continue the contract (UNCITRAL Digest, Art 49, para. 2). According to Article 49(1)(a) CISG, the buyer may declare the contract avoided if the failure by the seller to perform any of its obligations under the contract or the Convention amounts to a fundamental breach. ECE's delay amounted to a fundamental breach [paraa. 35 *et seqq.*]. Therefore, MCA was entitled to avoid the contract when it became clear that the delay would be detrimental.

49 **Conclusion:** ECE's breach of contract amounted to a fundamental breach. MCA was therefore entitled to avoid the contract under Article 49(1)(a) CISG.

2.1.3 MCA declared Cocoa Contract 1045 avoided by notice to ECE on 25 Oct 2002 pursuant to Article 26 CISG.

50 Pursuant to Art 26 CISG, an explicit or implicit notice of avoidance must be given to the other party (*Karollus in Honsell*, Art 26, para. 12, p. 282; *et alt.*). There are no further formal requirements (*Leser in Schlechtriem*², Art 26, para. 8, p. 188). MCA's notice about the substitute transaction, dated 25 Oct 2002, implied that delivery was no longer needed (Claimant's Exhibit No. 8). ECE could not have understood this in any other way as MCA had notified ECE several times of the necessity of receiving the cocoa shortly. The first notice was sent on 5 Mar 2002, stating "*although we are not under immediate pressure to receive the contracted cocoa, we will be later this year*" (Claimant's Exhibit No. 4). A second notice was sent on 15 Aug 2002, stating "*our stocks are lower than we are comfortable with*" (Claimant's Exhibit No. 7) and emphasized by the warning that MCA would purchase the cocoa elsewhere if it were not delivered soon. Thus, it must have been clear to ECE that the information about the substitute transaction implied the avoidance of the contract.

51 **Conclusion:** MCA implicitly notified ECE of the avoidance on 25 Oct 2002. Taking into account that MCA had, on several occasions, drawn ECE's attention to the fact that it would soon be in urgent need of the cocoa, ECE could not have misunderstood the implicit declaration of avoidance.



2.1.4 Alternatively, if the Arbitral Tribunal finds that Cocoa Contract 1045 was not implicitly avoided on 25 Oct 2002, it was avoided explicitly on 15 Nov 2002.

52 ECE interpreted the requirements for avoidance in a formalistic way by insisting on an explicit notice of avoidance (Claimant's Exhibit No. 10). Only as a precaution MCA issued an explicit notice of avoidance on 15 Nov 2002 (Claimant's Exhibit No. 11).

53 **Answer to Procedural Order No. 1, Question 2: Taking into account all circumstances, ECE committed a fundamental breach of contract by exceeding the initial delivery period by almost 5 months. MCA was therefore entitled to avoid the contract and implicitly did so on 25 Oct 2002. Consequently MCA is entitled to claim damages under Art 75 CISG.**

3. MCA is entitled to claim damages in the amount of USD 289,353.

54 MCA will demonstrate that as a consequence of ECE's delay in delivery, it had to purchase cocoa elsewhere to avoid running out of supplies [see table para. 42]. As a result, MCA incurred additional costs of USD 289,353, which it is entitled to claim as damages.

55 Under the CISG damages can be claimed under Artt 74, 75 and 76. Under Art 74 CISG the injured party can claim damages whether or not the contract has been avoided. However, when the contract has been avoided and a substitute transaction has been made, damages are calculated under Art 75 CISG. If the substitute transaction has not been made in a reasonable manner and in a reasonable time after avoidance, damages are calculated under Art 76 CISG (*Chengwei*, Non-Performance, section 15.3.2). Firstly, MCA will show that it is entitled to claim damages in the amount of USD 289,353 pursuant to Art 75 CISG. Secondly, and only if the Arbitral Tribunal finds that MCA cannot rely on Art 75 CISG, MCA will show that it is entitled to claim the same amount as damages under Art 76 CISG. Thirdly, if the Arbitral Tribunal finds that avoidance was not declared until 15 Nov 2002, MCA will show that the damage suffered as a result of ECE's breach of contract amounts to USD 289,353 even under Art 74 CISG. Finally, MCA will show that it has taken all reasonable measures to mitigate losses under Art 77 CISG.



3.1 As a result of the substitute transaction, MCA has incurred losses of USD 289,353. MCA is entitled to claim damages for this loss under Article 75 CISG.

56 MCA rightfully avoided Cocoa Contract 1045 on 25 Oct 2002 [**para. 50**]. As a rule under Art 75 CISG, avoidance has to be declared before the substitute transaction is made. This is considered a measure protecting the counter-party's interests, e.g. from price speculations by the other party. MCA will show that ECE's interests were in no way endangered by the fact that the substitute transaction was made before avoidance [**paraa. 58 et seq.**]. The substitute transaction was justified as it was made in a reasonable manner, at a reasonable time and for a reasonable price, pursuant to Art 75 CISG [**paraa. 60 et seq.**].

57 Concrete calculation of damages is the primary method under the CISG (*Stoll in Schlechtriem*, Art 75, para. 1, p. 573). Accordingly, MCA's losses consist of the difference in price between that specified in Cocoa Contract 1045 (USD 372,225) and that paid for the substitute cocoa (USD 661,578), i.e. USD 289,353. MCA claims this amount as damages.

3.1.1 MCA was entitled to make a substitute transaction before avoidance of Cocoa Contract 1045.

58 Pursuant to Art 75 CISG a contract has to be avoided before a substitute transaction can be made. However in order to preserve good faith in international transactions, in cases where it is certain that the seller will definitely not perform his obligations, an exception should be made to this requirement (*Stoll in Schlechtriem*², Art 75, para. 5, p.575; OLG Hamburg [GER], 28 Feb 1997, 1 U 167/95). In the present case, though it was not certain that ECE would never perform, it was certain that it would not perform by 25 Oct 2002, i.e. the day when the contract was avoided. ECE had showed in past correspondence (Claimant's Exhibit No. 3 and Claimant's Exhibit No. 6) that it was not willing to deliver anything but Equatorianese cocoa, which was prevented by the Embargo.

59 Avoidance is normally required before a substitute transaction is made in order to (a) inform the party in breach that performance is no longer needed and (b) to prevent price speculations by the buyer at the expense of the seller (*Schönle in Honsell*, Art 75, para. 20, p. 957). MCA declared the contract avoided one day after the substitute transaction was made. However, this did not impair ECE's interests in any way, as (a) ECE was informed immediately after



the substitute transaction was made that delivery is no longer needed and (b) the prices for cocoa remained the same throughout the month of October. MCA therefore did not endanger ECE's interests by making the substitute transaction shortly before declaring avoidance.

3.1.2 The substitute transaction was rightfully made on 24 Oct 2002.

60 A substitute transaction is considered reasonable when (a) the date of the substitute transaction is reasonable, when it is (b) made at a reasonable price and (c) in a reasonable manner (see *Knapp in Bianca/Bonell*, Art 75, section 2.4, p. 550; *et alt.*). As shown above [paraa. 58 *et seq.*] (a) the date of the substitute transaction was reasonable. MCA did its utmost to purchase the cocoa at the lowest possible price. MCA bought the substitute goods at the current market price (Respondent's Exhibit No. 3) and therefore (b) the price was reasonable. The price being reasonable MCA is entitled to claim compensation even for the less favorable price (see *Stoll in Schlechtriem*², Art. 75, para. 9, p. 576). MCA concluded its contract with Oceania Produce Ltd. on similar terms as Cocoa Contract 1045 and purchased "the same type and quality" (*Stoll in Schlechtriem*², Art. 75, para. 7, p. 576). Therefore (c) the substitute transaction was made in a reasonable manner. In addition to this, the amount purchased was reasonable, as MCA had no reason to believe that ECE would deliver the remaining 300 metric tons of cocoa shortly. Buying less than 300 metric tons might have resulted in a shortage of supplies only a short time later [see table para. 42] as well as in additional transactions which would have entailed additional shipping costs. Also, the price of the cocoa was affected neither by the amount purchased nor the date of the purchase. Therefore buying 300 metric tons of cocoa was reasonable as regards date, price and manner.

61 It must be foreseeable for the promisor that the promisee will compensate himself for non-performance by means of a substitute transaction (*Stoll in Schlechtriem*², Art 75, para. 9, p. 576). This was the case as ECE was explicitly informed by MCA that MCA would purchase the cocoa elsewhere if it ran out of stock (Claimant's Exhibit No. 7).

3.2 Alternatively, MCA is entitled to claim damages in the amount of USD 289,353 under Article 76 CISG.

62 If the Arbitral Tribunal finds that MCA's actions in making the substitute transaction before declaring the contract avoided were not reasonable, damages can still be claimed under Art



76 CISG because the goods contracted for have a market price (OLG Hamburg [GER], 4 Jul 1997, 1 U 143/95 and 410 O 21/95). In such a case, damages are calculated as though no substitute transaction had taken place (*Chengwei*, Non-Performance, section 15.2.3). Under Art 76, the calculation of damages must be made according to the market price on the day of avoidance (*Secretariat Commentary*, Article 71, O.R., p. 60; see also *Sutton*, OSLJ [1989], p. 737-752).

63 As MCA avoided Cocoa Contract 1045 on 25 Oct 2002, damages are to be calculated according to the market price of that day. The prices shown in the chart from the International Cocoa Organization (Respondent's Exhibit No. 3) for any given month represent the market price for cocoa purchased on any given day during that month (Procedural Order No. 2, para. 25). Thus the price of the cocoa in question was the same on 24 and 25 Oct 2002. Therefore no matter whether the substitute transaction was made shortly before or after avoidance, and whether the damages are calculated according to Art 75 CISG or Art 76 CISG, MCA is entitled to USD 289,353 as damages.

3.3 Alternatively, if the Arbitral Tribunal finds that avoidance was not effected until 15 Nov 2002, damages still amount to USD 289,353 under Article 74 CISG.

64 If the Arbitral Tribunal finds that MCA did not avoid the contract until 15 Nov 2002, MCA is still entitled to claim damages in the amount of USD 289,353 under Art 74 CISG. Art 74 CISG applies whether the contract has been avoided or not. It establishes the rule for the measurement of damages whenever and to the extent that Artt 75 and 76 CISG are not applicable (*Chengwei*, Non-Performance, section 15.1) and contains the principle of full compensation for all disadvantages suffered. Those disadvantages are established by comparing the situation in which MCA finds itself as a result of ECE's breach, with the fictitious situation without such a breach (see *Stoll in Schlechtriem*², Art 74, para. 2, p. 553).

65 The loss suffered by the promisee, in this case MCA, needs to be objectively foreseeable for the other party at the time of the conclusion of the contract. In assessing this foreseeability, the usual or intended use of the goods by the buyer should be the decisive factor (*Slechtriem*, Uniform Sales Law, p. 97). From the long business relationship between ECE and MCA, ECE should have known that MCA, a small purchaser (Procedural Order No. 2, para. 29), uses the cocoa for the production of confectionary. ECE should have been aware at



the time of the conclusion of Cocoa Contract 1045 that if ECE were unable to deliver, MCA would eventually run out of stock. Furthermore, ECE could foresee that if delivery were delayed by as much as five months, MCA would have to purchase elsewhere to continue its production. The burden of proof concerning the non-existence of foreseeability under Art 74 CISG is on the seller (OLG Zweibrücken [GER], 31 Mar 1998, 8 O 1995/95), i.e. on ECE.

- 66** There are four preconditions for claiming damages under Art 74 CISG: (a) a breach of contract by the seller, (b) a loss suffered by the other party, (c) causality between (a) and (b) (*Knapp in Bianca/Bonell*, Art 74, section 2.4, p. 540) and (d) foreseeability of the loss at the time of the conclusion of the contract. ECE was in breach of contract [**para. 32**] and as a result MCA suffered losses in the amount of USD 289,353 [**para. 57**]. The loss resulting directly from non-performance can be considered a typical form of loss and is generally regarded as foreseeable. The amount of such loss depends primarily on general factors, such as market conditions. The general factors may change after the conclusion of the contract, but those changes are part of the contractual risk assumed by the promisor. Thus ECE cannot invoke the fact that after the conclusion of Cocoa Contract 1045 there has been an unusually large rise in the market price of the goods (see *Stoll in Schlechtriem*², Art 74, para. 38, p. 569).
- 67** Any costs resulting from reasonable efforts to mitigate losses may be compensated for under Art 74 CISG (OLG Köln [GER], 8 Jan 1997, 27 U 58/96), especially a substitute transaction to prevent loss of profit (*Stoll/Gruber in Schlechtriem*⁴, Art 74, para. 16, p. 701). In the case at hand, the loss is the result of the rise in market prices which is reflected in the higher price of the substitute transaction. This substitute transaction was, as will be shown [**para. 69**], a reasonable measure to mitigate losses. Therefore ECE is liable to pay damages in the amount of the difference in prices between that specified in Cocoa Contract 1045 (USD 372,225) and that paid for the substitute cocoa (USD 661,578), i.e. USD 289,353.

- 68** **Conclusion:** Under Art 75 CISG, MCA is entitled to claim USD 289,353 as damages as a consequence of the necessary substitute transaction made on 24 Oct 2002. Alternatively, MCA can claim the same amount under Art 76 CISG. Finally, if the Arbitral Tribunal finds that Cocoa Contract 1045 has not been avoided until 15 Nov 2002, MCA is entitled to claim this amount under Art 74 CISG.



3.4 MCA has taken all reasonable measures to mitigate losses under Article 77 CISG.

69 Art 77 CISG requires the injured party to take all measures that are reasonable in the circumstances to mitigate losses, including loss of profit, resulting from the breach. The substitute transaction was MCA's method of mitigating losses. Further waiting would not only have resulted in loss of profit, but also in the cost of halting and restarting production, carrying costs of an unproductive working force without production and possibly even the payment of damages to MCA's customers. By acting as it did, MCA not only mitigated its losses but also complied with its duty to counteract imminent loss (see *Stoll* in *Schlechtriem*², Art. 77, para. 1, p. 585). It was reasonable to buy 300 metric tons of cocoa in order to mitigate losses. Not knowing of the imminent cessation of the Embargo, it would not have been reasonable to purchase a smaller amount as (a) 300 metric tons was the amount of cocoa missing from Cocoa Contract 1045, and (b) MCA had no reason to rely on the possibility that ECE would deliver the cocoa before MCA ran out of supplies. Purchasing a smaller amount could have resulted in higher transaction costs [para. 60].

70 **Conclusion:** MCA made the substitute transaction to comply with its obligation to mitigate losses under Art 77 CISG. By doing this, MCA maintained its right to claim damages.

71 **Answer to Procedural Order No. 1, Question 3: As a result of the substitute transaction which MCA rightfully made on 24 Oct 2002, it incurred losses of USD 289,353. MCA is entitled to claim this amount as damages, especially as it mitigated losses by means of the substitute transaction.**



F. Counterclaim

4. The Arbitral Tribunal does not have jurisdiction over the claim arising out of Sugar Contract 2212.

72 MCA respectfully requests the Arbitral Tribunal to find that it does not have jurisdiction over the counterclaim arising out of Sugar Contract 2212. It will demonstrate that ECE's counterclaim cannot be decided on by this Arbitral Tribunal, as it is an independent action in its own right [paraa. 73 *et seqq.*]. Consequently, MCA's consent is necessary to give the Arbitral Tribunal jurisdiction over this claim. However, MCA did not consent to this [paraa. 77 *et seqq.*]. Art 21(5) Swiss Rules can provide no basis for ECE's counterclaim. In any event, MCA objected to Art 21(5). Nor is there any basis for ECE's counterclaim outside of this provision even if it is reduced to a set-off defense [paraa. 82 *et seqq.*]. If the Arbitral Tribunal does not agree to the exclusion of Art 21(5), MCA will show that the Geneva Rules ought to be applied. Under these rules there is no basis for the jurisdiction of the Arbitral Tribunal to consider disputes out of Sugar Contract 2212 [paraa. 98 *et seqq.*]. Finally, it will be argued that an award made by the Arbitral Tribunal on the counterclaim could be subject to challenge in Danubia and may be unenforceable in NYC-States [paraa. 106 *et seqq.*].

4.1 The counterclaim raised by ECE constitutes an independent action in its own right and therefore cannot be heard in the current proceedings.

73 MCA's claim concerns Cocoa Contract 1045. In its Statement of Defense ECE raised a counterclaim arising from Sugar Contract 2212 (Problem, p. 28). Each contract is governed by its own arbitration clause [para. 78]. ECE is attempting to join these two unrelated cases in these arbitration proceedings by filing a counterclaim. A counterclaim is a separate claim by means of which the respondent seeks to obtain a separate judgment (ECJ, 13 Jul 1995, C-341/93). Since the counterclaim does not come within the scope of the arbitration clause of Cocoa Contract 1045, the Arbitral Tribunal may not exercise jurisdiction over it without explicit consent of both parties (see *Redfern/Hunter*³, para 6-59, p. 310; *Schlosser*², para 671, p. 498). This approach is taken by the majority of leading international commercial arbitration rules, as the following comparison demonstrates:



74 Art 19 of the UNCITRAL Arbitration Rules stipulates that “*the respondent may make a counterclaim arising out of the same contract or rely on a claim arising out of the same contract for the purpose of a set-off defense*”. Art 3(2) of the International Arbitration Rules of the American Arbitration Association states that “*a respondent may make counterclaims or assert set-offs as to any claim covered by the agreement to arbitrate*”. Art 7a of the Rules on Arbitration and Conciliation of the Vienna International Arbitration Centre states that “*Claims by the Defendant against the Claimant that are based on the same arbitration agreement can be raised as counterclaims*”. Art 19(1) of the Commercial Arbitration Rules of the Japan Commercial Arbitration Association states that the respondent may “*submit a counterclaim that is related to the claimant's claim(s) and covered by the same arbitration agreement*”. The Arbitration Rules of the International Chamber of Commerce (hereinafter referred to as ICC), do not contain a provision explicitly dealing with counterclaim and set-off. But it is understood that counterclaims raised in ICC proceedings have to be covered by the same arbitration clause as the main claim (*Derains/Schwartz*, p. 72).

75 Neither the arbitration agreement in Cocoa Contract 1045, nor in Sugar Contract 2212, provides a basis for this Arbitral Tribunal to decide on ECE's counterclaim [para. 73]. Thus this unrelated counterclaim can only be considered if MCA expressly consented to admit it. Since MCA did not consent thereto it cannot be considered by the Arbitral Tribunal [paraa. 79 et seq.].

76 **Conclusion:** ECE's counterclaim arises out of a different contract than the main claim. MCA did not consent to include the counterclaim in the current proceedings. Therefore it cannot be considered by the Arbitral Tribunal.

**4.2 An arbitral tribunal's jurisdiction is derived solely from the consent of the parties.
There was no consent to include the counterclaim in the current proceedings.**

77 The consent of MCA and ECE expressed in the arbitration agreements of Cocoa Contract 1045 and Sugar Contract 2212 is not to be ignored. To hold otherwise would be a denial of the very nature of arbitration. Since arbitration is a private and voluntary method of dispute-settlement, it necessarily has its foundations in the agreement of the parties. The arbitrators derive their powers solely from this agreement (*Fouchard/Gaillard/Goldmann*,



para. 7, p. 9). Consequently, the agreement of the parties is essential in determining the scope of the arbitral tribunals' jurisdiction (*Redfern/Hunter*³, para. 1-09, p. 6).

4.2.1 Disputes out of both Sugar Contract 2212 and Cocoa Contract 1045 must be resolved according to their respective arbitration agreements.

78 In Sugar Contract 2212 the Parties expressly agreed on arbitration in accordance with the Arbitration Rules of the OCA (hereinafter referred to as the OCA Rules). Port Hope, Oceania was chosen as the place of arbitration. By contrast, Cocoa Contract 1045 provides for arbitration according to the Geneva Rules. The chosen place was Vindobona, Danubia. Both arbitration agreements only allow disputes arising out of the respective contractual relationship to be decided by the respective arbitral tribunal. In the absence of an agreement of the parties providing otherwise, these arbitration agreements must be adhered to. Not to do so would be to disregard the consensual nature of arbitration. No agreement providing otherwise exists in the case at hand.

4.2.2 The arbitration clause in Cocoa Contract 1045 was not amended by the Parties.

79 The effect of an arbitration agreement is that it obliges the parties to submit the disputes it covers to arbitration under defined terms. This is an expression of the most widely accepted rule of international contract law - *pacta sunt servanda*, i.e. contracts must be adhered to (*Fouchard/Gaillard/Goldmann*, para. 627, p. 382). This rule also applies to arbitration agreements. Thus the consent given to an arbitration agreement cannot be unilaterally withdrawn by one of the parties (*Redfern/Hunter*³, para. 1-09, p. 7). An arbitration agreement can only be altered by consent and in observation of the applicable formal requirements. The MAL, the *lex arbitri* in the pending arbitration proceedings, requires an arbitration agreement to be in writing, according to its Art 7(1). The writing requirement also applies to amendments to the original agreement (*Schütze/Tscherning/Wais*², para. 73, p. 38). Consequently, if additional disputes are submitted to the arbitral tribunal, even during the arbitral proceedings, the writing requirement must be met (*Holtzmann/Neuhaus*, p. 261). ECE and MCA did not validly change their arbitration agreement contained in Cocoa Contract 1045.



80 Under Art 7(2) MAL the writing requirement would also be met by an exchange of statement of claim and defense, in which the existence of an arbitration agreement is alleged by one of the parties and not denied by the other. The same applies to counterclaim and defense to such counterclaim, according to Art 2(f) MAL. By presenting the dispute arising out of Sugar Contract 2212 as a counterclaim to the main action, ECE made an offer to extend the terms of the arbitration agreement in Cocoa Contract 1045. In its answer to the counterclaim MCA refused that offer [**para. 99**]. Thus, the original scope of the arbitration agreement in Cocoa Contract 1045 remains unchanged, and does not include disputes arising out of Sugar Contract 2212.

81 **Conclusion:** The essence of private arbitration is that the consent of the parties defines the scope of jurisdiction of an arbitral tribunal. The arbitration agreements in Cocoa Contract 1045 and Sugar Contract 2212 must not be ignored. They were not later amended. ECE's offer in the counterclaim to extend the arbitration agreement in Cocoa Contract 1045 was rejected by MCA. Thus the Arbitral Tribunal cannot decide on the merits of the counterclaim.

4.3 Art 21(5) Swiss Rules is no valid basis for the Arbitral Tribunal to decide on the counterclaim or set-off.

82 ECE relies on Art 21(5) Swiss Rules as the basis for the Arbitral Tribunal's jurisdiction to decide on the merits of the counterclaim. MCA will show that the counterclaim cannot be based on Art 21(5) because this provision only provides for set-off defense. If at all the counterclaim could only be considered as a set-off defense [**para. 83**]. Even a set-off defense would not be admissible in the current proceedings, because it arises out of a different legal relationship and would thus require consent [**paraa. 84 et seqq.**].

4.3.1 Art 21(5) provides no basis for ECE's counterclaim as it only refers to set-off.

83 ECE raises a counterclaim (see Problem, p. 28) on the basis of Art 21(5) of the Swiss Rules. Art 21(5) only permits the admissibility of set-off defenses – and not counterclaims, which are not governed by the arbitration agreement (*Peter*, ASA Special Series [2004] 22, p. 9). Set-off defense and counterclaim have to be sharply distinguished (*Berger*, Arb Int [1999], p. 59). Set-off constitutes a mere defense. It can therefore only be used “*as a shield not as a*



sword" (Stooke v. Taylor [1880] 5 QBD 569). ECE, however, requests the Arbitral Tribunal in its counterclaim to find that "*MCA is obliged to pay the full contract price of USD 385,805*" (Problem, p. 29) under Sugar Contract 2212. The relief requested by ECE shows its intention to take the initiative and attack, and not just defend itself against the claim raised by MCA (USD 289,353 (Problem, p. 5)). Whereas set-off is a mere defense, a counterclaim is an action of its own. ECE's action constitutes a counterclaim since the contract price claimed is higher than the damages sought by MCA. Because of the fundamental differences between counterclaim and set-off, a counterclaim cannot simply be treated as a set-off defense. The wording of Art 21(5) is unambiguous; it only provides a basis for a set-off defense. Therefore, ECE's counterclaim cannot be based on Art 21(5) and could, at the most, only be considered as a set-off defense. Should the Arbitral Tribunal find that it has jurisdiction over the counterclaim on the grounds of Art 21(5), any recovery made would be limited to a set-off against the recovery awarded to MCA out of Cocoa Contract 1045.

4.3.2 Even a set-off would not be permissible under Art 21(5) without the consent of the parties.

84 Even if the counterclaim were reduced to a set-off by the Arbitral Tribunal it would still not be admissible. Decisions on both set-off and counterclaim have the effect of *res judicata*, i.e. both pleas result in a final decision that cannot be changed. Therefore disputes arising out of other contracts or not covered by the arbitration agreement may not be introduced into arbitral proceedings through the backdoor of set-off. Otherwise even unforeseeable conflicts which the parties never agreed to arbitrate would be included. Thus the same strict standards for admissibility should apply, i.e. either the set-off should be covered by the same arbitration agreement or by parties' explicit consent. This will be shown below [**paraa. 85 et seqq.**]. MCA will also demonstrate that the necessity of these requirements cannot be overruled by Art 21(5) Swiss Rules [**paraa. 94 et seqq.**].

4.3.2.1 A set-off defense raised by ECE would be outside the scope of the arbitration agreement in Cocoa Contract 1045.

85 There is no basis for ECE to raise a set-off defense outside the scope of the arbitration agreement contained in Cocoa Contract 1045. The separate intents of the parties [**paraa. 86 et seqq.**] at the moment of the conclusion of the arbitration agreement covering the main claim



on the one hand, and the arbitration agreement covering the set-off defense on the other, has to be determined (*Berger*, Arb Int [1999], p. 74; see also *Reiner*, FS Hempel [1997], p. 121). Further, general principles governing the admissibility of set-off have to be applied, since the *lex arbitri*, in this case the MAL, does not contain a provision explicitly dealing with set-off defense [**paraa. 89 et seqq.**].

§ Intent of the Parties in Sugar Contract 2212

86 In interpreting the intent of the parties, the choice of the place of arbitration and the choice of the *lex arbitri* therein must be considered. A change of the place of arbitration is only allowable in very limited circumstances, e.g. if it is to be feared that equal justice will otherwise not be granted (*The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 [1972]). There are no such exceptional circumstances in this case.

87 Moreover the parties chose OCA as a specialized arbitration institution for Sugar Contract 2212. The parties' decision was based on legal, economic and practical considerations which cannot be ignored. The main question in dispute under Sugar Contract 2212 is whether the sugar was fit for human consumption at the time of delivery, i.e. before the risk passed to MCA. The OCA, as a specialized institution, has the ideal infrastructure and experience to take evidence and evaluate the facts at hand.

§ Intent of the Parties in Cocoa Contract 1045

88 For Cocoa Contract 1045 the Parties deliberately chose the Geneva Rules, and not the Arbitration Rules of the Zurich Chamber of Commerce (hereinafter referred to as the Zurich Rules). The Geneva Rules do not contain a provision similar to Art 21(5) Swiss Rules, whereas Art 27 Zurich Rules does contain such a provision.

§ Procedural admissibility of set-off

89 A comparative analysis of Swiss, German, French and English law shows that a set-off defense which is not connected to the main claim and which is disputed, should either be inadmissible or in any case not be considered by the arbitral tribunal dealing with the main claim (see *Wagner*, IPRax [1999], p. 75). The extensive admissibility of set-off defenses, as



provided for in the Zurich Rules and the Swiss Rules, neither represents the general perception of the admissibility of set-off defenses in Switzerland nor are they in harmony with the concepts in other European countries (*Bucher*, p.138; see also *Bucher Juristentag*, p. 1). In Swiss doctrine it is even argued that implementing a provision similar to Art 21(5) Swiss Rules into the Swiss Procedural Code was in breach of the Swiss Constitution (*Bucher, Juristentag*, p. 1).

- 90** An extensive discussion on the principles applying to set-off is to be found in German legal literature and court rulings. It is held that in court proceedings the defendant cannot raise a set-off defense which is subject to an arbitration agreement, because the arbitration agreement includes a procedural prohibition of set-off (BGH [GER], 22 Nov 1962, VII ZR 264/61, see also *Schütze/Tscherning/Wais*², para 55, p. 29). From this, the opinion was developed that an arbitral tribunal has no jurisdiction to decide on a set-off defense which is subject to a different arbitration agreement (*Lionnet*², p. 311; *Schlosser*², para. 399, p. 300). Otherwise the defendant would have the opportunity to avoid the agreed arbitral tribunal by simply raising a set-off defense (*Lionnet*², p. 311). Only if the claim raised as a set-off is undisputed or has already been ascertained with *res judicata* effect, is it held to be admissible (*Berger, Arb Int* [1999], p. 77). In this case, the claim raised by ECE was disputed by MCA and thus may not even be admitted as a set-off.
- 91** Also in common-law jurisdictions a set-off defense would not be admissible in the current proceedings. Under English law for instance an arbitral tribunal has no jurisdiction to decide on the set-off plea outside the scope of the arbitration agreement and the respondent can only request to stay the arbitral proceedings (*Baumann*, p. 57). Also the US-Iran Claims Tribunal has repeatedly emphasized that, despite the distinct procedural nature, a set-off has to meet the same jurisdictional standards as a counterclaim; i.e. the set-off has to be within the jurisdiction of the arbitral tribunal (Iran – U.S. Claims Tribunal, 16 Apr 1986, Case No. 65 (221-65-1); see also *van Hof*, p. 133). Danubia, the place of arbitration, is a common-law country. MCA is a corporation organized under the laws of Mediterraneo which is also a common-law country (see Procedural Order No. 2). Art 21(5) clearly conflicts with the common-law perception in the sense that it allows set-off defenses outside the scope of the arbitration agreement. This shows the surprising character this provision has for MCA and that it should not be applied to the current proceedings without MCA's explicit consent [para. 96].



92 It has been suggested that a set-off defense based on a closely connected contract, i.e. the contracts form a single economic unit, should be admissible without consent (ICC Award No. 5971). However, Sugar Contract 2212 and Cocoa Contract 1045 are not closely related. The agreements were intended to have an independent and separate existence. There is no economic or temporal linkage between the two contracts.

93 It follows that the admissibility of a set-off defense subject to a different arbitration agreement without consent of the parties is limited to exceptional cases in international commercial arbitration. None of these rare exceptions exist in the case at hand. Therefore ECE's counterclaim, even taken as a set-off, is inadmissible without consent of the Parties.

4.3.2.2 Art 21(5) is an entirely unexpected and exceptional provision which cannot be applied without the explicit consent of both Parties.

94 Set-off is an issue which most arbitration laws and institutional rules are silent upon. This is because of its complexity and disputed legal nature. Even the drafters of the MAL, in order to avoid additional intricate problems, refrained from tackling the issue of set-off (*Berger, Arb Int* [1999], p. 53).

95 When MCA was first informed about the application of the Swiss Rules (Problem, p. 19), no reference was made to the introduction of Art 21(5) and its possible far-reaching effects. In contrast, the attention of the Parties was drawn to the new rules concerning the Expedited Procedure and their application (Problem, p. 21). Whereas the Expedited Procedure affects both parties in the same way, Art 21(5) strengthens the position of ECE, while prejudicing MCA.

96 Where the parties refer to arbitration rules, these form part of the arbitration agreement without being explicitly listed (*Berger, p. 345*). The same applies if contracting parties make reference to standard contract forms which then form part of their agreement. In both cases the parties implement a set of rules by way of reference, trusting that they are an appropriate legal framework for the contract they are concluding. In many European countries standard contract forms are subject to judicial control as regards surprising, unfair or exceptional provisions. Because of the above-mentioned similarities, arbitration rules should be under



comparable control (*Aden*², para. 15, p. 78; *Maier*, para. 58, p. 84). With regard to surprising, unfair or exceptional provisions, it must be assessed whether a given consent covers a provision that would not ordinarily be included in such a context. Art 21(5) constitutes a surprising and exceptional provision, as it has a very expansive approach to the admissibility of set-off defenses. This is both new in comparison to the Geneva Rules and drastically extends the original arbitration agreement. An arbitration agreement must refer to disputes arising out of a defined legal relationship. Art 21(5) threatens this fundamental principle by opening up the arbitration clause of the parties to unforeseeable conflicts arising out of unpredictable legal relationships. It thereby jeopardizes the validity of the arbitration agreement. Even if MCA had agreed on Art 21 (5) which it did not [para. 99], this would not be sufficient without additional consent for each new claim to be introduced. There was no such additional consent by MCA.

97 **Conclusion:** Art 21(5) Swiss Rules only applies to set-off defenses. ECE's counterclaim thus has to be dismissed and ECE's assertions could, at the most, be considered as a set-off defense. Nevertheless, even a set-off defense by ECE would be inadmissible. This is because it is outside the scope of the arbitration agreement in Cocoa Contract 1045 and MCA did not consent to include it. Art 21(5) Swiss Rules cannot serve as a basis to allow such an extension. Its application would require explicit consent which was not given by MCA. Even if MCA had agreed on the application of the Swiss Rules without any objection to Art 21(5), an explicit consent to the new claim arising out of Sugar Contract 2212 introduced as a set-off would be necessary.

4.4 Art 21(5) Swiss Rules must not be applied. Should the Tribunal not agree to the exclusion of Art 21(5), MCA rejects the application of the Swiss Rules as a whole.

98 The Swiss Rules were presented to MCA as the successor of the Geneva Rules. However, they contain in Art 21(5) a completely new feature. The statement of claim was filed to the CCIG on 5 Jul 2004. Although the Swiss Rules were in force as of 1 Jan 2004 they are not automatically applicable to the case at hand, despite their Art 1(3) [para. 101 *et seqq.*]. MCA's consent to the application of the Swiss Rules was conditional upon the non-applicability of Art 21(5) Swiss Rules (see Problem, p. 41). In order to avoid falling back on



the Geneva Rules or MAL as enacted in Danubia, MCA requests the exclusion of the provision it objected to. Otherwise MCA must reject the Swiss Rules in their entirety.

4.4.1 MCA has objected to the application of Art 21(5).

99 According to Art 21(3) Swiss Rules, any plea as to the jurisdiction of an arbitral tribunal over a counterclaim must be raised no later than in the reply to the counterclaim. The question whether Art 21(5) is applicable to the current proceedings comes within the scope of this article. In its answer to the counterclaim on 21 Aug 2004 (Problem, p. 40), MCA expressly objected to the application of Art 21(5). Therefore, MCA has pleaded in due time against its application and against the jurisdiction of the Arbitral Tribunal to decide on the counterclaim.

4.4.2 The Swiss Rules as a whole are not applicable in the absence of MCA's consent.

100 MCA only consented to the Swiss Rules on the condition that Art 21(5) would not be applicable [para. 78]. In the event that the Arbitral Tribunal finds that the Swiss Rules are to be applied in their entirety, that condition is not met and thus MCA's prior consent to the Swiss Rules (Problem, p. 41) no longer stands. A lack of consent to a substantial point, such as Art 21(5), must not be disregarded. Therefore there is no valid basis for the application of the Swiss Rules as a whole.

4.4.2.1 The Swiss Rules are substantially different from the Geneva Rules.

101 This case does not automatically fall under the scope of the Swiss Rules. The Swiss Rules are not the direct successor of the Geneva Rules. Rather they harmonize a number of differing Swiss cantonal arbitral regimes. This new set of rules was implemented by the various Swiss Chambers of Commerce and Industry by an inter-institutional agreement. However this decision of the six chambers in question cannot have any influence or effect on the parties involved (see *Fouchard/Gaillard/Goldmann*, para. 320, p. 157), i.e. in this case MCA and ECE concerning Cocoa Contract 1045, without the consent of those parties.

102 There is a general tendency to accept the fact that an institution may need to revise its rules from time to time in order to bring them up-to-date (*Redfern/Hunter*³, para 1-88, p. 49). However, it can be seen from the amendments to the ICC Rules, that changes concerning



substantial issues are subject to much dispute (ICC Award No. 2671 of 1976). To clarify this matter the 1998 amendment to the ICC Rules inserted in Art 6(1) the principle that the version to be applied should be the one in effect on the date of the commencement of arbitration, unless otherwise stated by the parties. However, this “*deeming*” provision cannot definitively determine the intent of the parties (*Craig*, ICC arbitration, p. 143). Such an assumption would have a retroactive effect on parties’ agreements, fundamentally infringing party autonomy. In general the opinion is that in unclear situations the will of the parties must be understood to comprise only the version of the rules as known to them upon agreement (*Schlosser*², para. 631, p. 473).

103 Art 1(3) Swiss Rules imposes its rules in effect on notice of arbitration unless otherwise agreed. By incorporating the model clause of the Geneva Rules in Cocoa Contract 1045, ECE and MCA agreed to those rules in effect on the date of signature of that contract, 19 and 23 Nov 2001. Thus, if the rules applicable to the pending proceedings are questionable, simple objection, as articulated by MCA (Problem, p. 41) [**paraa. 79 et seq.**], must be sufficient to exclude the application of the Swiss Rules. This approach is also taken in the Geneva Rules. Art 1(2) Geneva Rules stipulates that a simple objection by one of the parties is sufficient to prevent the application of the amended rules. Finally taking into account the substantial differences between the Geneva Rules and the Swiss Rules, it is clear that MCA cannot be held to have endorsed the Swiss Rules and justifiably so.

4.4.2.2 At the time of submission of the claim the Swiss Rules were in conflict with the arbitration clause.

104 Should the Arbitral Tribunal find that applicable rules are those which apply to the agreement at the date of submission, the Geneva Rules are the rules which should govern these proceedings. MCA filed its statement of claim on 5 Jul 2004. The Swiss Rules entered into force on 1 Jan 2004, but were amended on 6 Jul 2004 on a very important point: Art 1(2) previously stated that the place of arbitration had to be within Switzerland. After the amendment it allowed the place of arbitration to be also outside of Switzerland. This amendment came into force on 1 Aug 2004, i.e. only after the statement of claim had been filed. This means that at the time of submission the Swiss Rules were not applicable, because the arbitration clause in Cocoa Contract 1045 calls for Vindobona, Danubia, as the place of arbitration. The decision of the Special Committee of the Swiss Chambers retroactively



declaring the amended provision to be applicable cannot cure the previous non-conformity. The Special Committee was formed to govern arbitral proceedings under the Swiss Rules and derives no power from the arbitration agreement in Cocoa Contract 1045. Thus the Geneva Rules should apply to the current proceedings. These rules remain in existence unamended and in common use for domestic arbitration in Switzerland. They do not contain a provision similar to Art 21(5) Swiss Rules. Thus, neither counterclaim nor set-off is admissible without consent of the Parties.

105 Conclusion: Art 21(5) Swiss Rules has not been accepted by MCA, and is thus not applicable. If the Swiss Rules cannot be applied without Art 21(5), the Geneva Rules must govern the current proceedings. Under these Rules neither counterclaim nor set-off subject to a different arbitration agreement are admissible without the consent of the parties. MCA did not give such consent.

4.5 An arbitral award rendered on the basis of Art 21(5) Swiss Rules could be subject to challenge in the courts of Danubia and may be unenforceable under the NYC.

106 Should the alleged claim arising out of Sugar Contract 2212 be considered in the final award, this would be incompatible with the MAL as enacted in the place of arbitration, Danubia, and also with the NYC. Danubia, Oceania, Equatoriana and Mediterraneo – likely places for the enforcement of the award – are all parties to the NYC and are bound by its provisions. It is in the interest of the parties and the Arbitral Tribunal to render an award that will not give rise to challenge and will be enforceable in NYC-States.

4.5.1 The competence of the Arbitral Tribunal to rule on its own jurisdiction regarding Sugar Contract 2212 is of a provisional nature and is subject to further court review.

107 An arbitral tribunal is competent to rule on its own jurisdiction according to Art 21(1) Swiss Rules and Art 16(1) MAL. Such decision is, however, only preliminary and subject to court review. If the Arbitral Tribunal in this case renders a separate award on the jurisdictional issue, this may be subject to appeal before the Danubian courts according to Art 16(3) MAL.



If the Arbitral Tribunal incorporates its decision on jurisdiction in the final award, the whole award may be set aside in Danubian courts according to Art 34 MAL.

4.5.2 An award made on a claim arising from an unrelated contract can be set aside under Art 34 MAL. Moreover enforcement may be refused under Art V NYC.

- 108** MCA reserves the right to challenge an award that also decides on the counterclaim or admits a set-off defense. According to Art 34 MAL, which is worded in accordance with Art V NYC, arbitral awards may be subject to judicial review and set aside on the grounds listed therein. The following grounds could be a basis for such a challenge:
- 109** Art 34(2)(a)(i) MAL – There is no valid agreement that entitles the present Arbitral Tribunal to decide upon the alleged counterclaim arising out of Sugar Contract 2212 [**paraa. 82 et seqq.**]. The agreement stipulating arbitration under the Geneva Rules would be overruled and the Swiss Rules enforced by the CCIG. If the original agreement were to be changed, the writing requirements of Art 7 MAL & Art II(2) NYC would have had to be met (*Schwab/Walter*⁶, para. 1, p. 547).
- 110** Art 34(2)(a)(iii) MAL – The Arbitral Tribunal would be exceeding its authority if it decided on the merits of the counterclaim, because it did not fall within the terms of the arbitration agreement in Cocoa Contract 1045. MCA never agreed to any extension of its submission to arbitration (*Fouchard/Gaillard/Goldmann*, para. 1700, p. 988).
- 111** Art 34(2)(a)(iv) MAL – MCA only agreed on the Geneva Rules and was not subjected to the Swiss Rules at the time the arbitration proceedings started. It only accepted the Swiss Rules under the exclusion of Art 21(5). This means that the application of any other procedure would not conform with the agreement of the parties (*Holtzmann/Neuhaus*, p. 917). A ground for challenge was held to exist where the change of rules was of serious prejudice to a party (OLG Schleswig [GER], 30 Mar 2000, 16 SchH 05/99). In this case, MCA's right to object was reduced and the scope of authority of the Arbitral Tribunal was extended to an unconnected contract, here the counterclaim, by the application of the Swiss Rules.
- 112** Art V NYC governs the refusal of recognition and enforcement of arbitral awards. As it was the model for Art 34 MAL, the relevant arguments given above apply correspondingly. On



these grounds an award based on Art 21(5) Swiss Rules would be unenforceable. Given the weight of each of these reasons an award which includes Sugar Contract 2212 in these proceedings could be challenged in, and set aside by, Danubian courts.

113 Conclusion: An award deciding also on the counterclaim raised by ECE infringes Art 34 MAL and Art V NYC. Thus it would not be upheld or enforced in courts to whose review it may be subjected.

114 Answer to Procedural Order No. 1, Question 4: Jurisdiction over ECE's counterclaim must be refused by the Arbitral Tribunal. This independent claim neither falls within the scope of the arbitration agreement in Cocoa Contract 1045, nor have the Parties since the conclusion of the arbitration agreement consented to the inclusion of this claim. By bringing the counterclaim, ECE was merely offering to extend the Parties' previous agreement. However MCA never accepted this offer. Further, MCA never consented to a set-off defense and the set-off cannot be imposed on MCA by Art 21(5) Swiss Rules, as these do not apply to the current proceedings. Moreover, Art 21(5) Swiss Rules can only be applied to a set-off defense. Should the Arbitral Tribunal find that it has jurisdiction over Sugar Contract 2212 under Art 21(5) Swiss Rules, it would be limited to a set-off defense.

G. Plea

- 115** For all of the above reasons, MCA respectfully requests the Arbitral Tribunal
1. to order ECE to pay MCA damages in the amount of USD 289,353;
 2. to declare that it does not have jurisdiction over the counterclaim arising out of Sugar Contract 2212;
 3. alternatively, if the Arbitral Tribunal finds that it has jurisdiction over the counterclaim,
 - 3.1 to render an interim award on its jurisdiction regarding the counterclaim;
 - 3.2 to render a partial award concerning the claim;
 - 3.3 to consider the assertions of ECE as a set-off defense and not as a counterclaim.