SIXTEENTH ANNUAL

WILLEM C. VIS INTERNATIONAL COMMERCIAL ARBITRATION MOOT

APRIL 2-9, 2009

Vienna

MEMORADUM FOR RESPONDENT 2

On behalf of

Universal Auto Manufactures, S.A.
47 Industrial Road
Oceanside
Equatoriana
Respondent 2

Against

Mr. Joseph Tisk, Reliable Auto Imports
114 Outer Ring Road
Fortune City
Mediterraneo
Claimant

Alongside

UAM Distributors, Oceania Ltd., 125 Ocean Boulevard, Port City, Oceania
Respondent 1

MASARYK UNIVERSITY

FACULTY OF LAW

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STATEMENT OF FACTS

Claimant	Mr. Joseph Tisk, doing business under the trade name of Reliable Auto Imports, a sole trader car dealer in Mediterraneo.
Respondent 1	UAM Distributors Oceania Ltd., a corporation organized in Oceania.
Respondent 2	Universal Auto Manufacturers, S.A., a corporation organized in Equatoriana.
January 18, 2008	Claimant signs a contract with Respondent 1 to purchase 100 of the Tera cars.
January 23, 2008	Under the payment term in the contract USD 380,000 (50% of the total price) is paid as a deposit.
February 11, 2008	First consignment of 25 cars arrives in Fortune City, Mediterraneo.
February 18, 2008	Cars are available to Claimant. During the journey to the Claimant's showroom the defect on the shipped cars was discovered.
February 21, 2008	The mechanic hired by Claimant inspects ten of the cars to determine the problem.
February 22 – 28, 2008	Claimant communicates with Mr. High (Sales Manager for Respondent 1),Mr. Jones (Chief Engineering Officer for Respondent 2)and Mr. Steiner (Regional Manager for Respondent 2) to solve the problem with defective cars.
February 28, 2008	Mr. Steiner informs Claimant that mechanics will arrive in Mediterraneo within 3 days.
February 29, 2008	Claimant terminates the contract with Respondent 1. He accepts the offer for the Indo cars.
March 9, 2008	Insolvency proceedings are commenced in regard to Respondent 1.
August 15, 2008	Claimant submits his request for arbitration against Respondent 1 and Respondent 2.

INTRODUCTION

I. These arbitration proceedings arise from the contract concluded between Claimant, established car dealer, and Respondent 1, car distributor. The subject-matter of the contract was the purchase of 100 new Tera cars manufactured by Respondent 2. Claimant was willing and able to pay USD 760,000 for whole order. Respondent 2 took neither any part in the negotiations between the contractual parties, nor in final preparations and conclusion of the contract.

II. Respondent 1 delivered first consignment of 25 cars to Claimant pursuant to the contract delivery requirement. After having been in customs for 7 days, Claimant drove them to his showroom on February 18, 2008. It was not before February 22, 2008, when Claimant informed Respondent 1 that there were some defects with the delivered cars. Respondent 1 discussed declared problems with Respondent 2 immediately after he was informed about them. Respondent 2 reacted promptly with the aim to preserve the good reputation of Tera cars without admitting to any liability.

III. Respondent 2 assured Claimant on February 28, 2008, that his technical personnel would arrive in three days in Mediterraneo and they would immediately start repairing the defects. Though the Respondent 2 offered instant assistance at his own expanses, he could not estimate the length of repair before his personnel examined the cars.

IV. Claimant was informed about all steps taken by Respondent 2 to solve the matter as soon as possible. He appreciated these vigorous actions and he did not raise any objections against Respondent's 2 conduct. Contrary to his previous behavior and without any previous objections, Claimant avoided the contract on the very next day February 29, 2008. He did not wait until Respondent's 2 technical personnel could have arrived in Mediterraneo. Claimant must have clearly seen the resolute effort of Respondents that consequently led to fixing the trouble. Nevertheless, he was not willing to contribute by providing necessary time. To the contrary, he avoided contract hastily and submitted the petition to arbitration and claimed the deposit from Respondent 2.

V. Therefore, Respondent 2 respectfully asks the Tribunal to decide that Respondent 2 is not bound by the arbitration clause included in the contract between Claimant and Respondent 1 and further the Tribunal does not have jurisdiction in this dispute due to the insolvency proceedings. Should the Tribunal find otherwise, Respondent 2 suggests the Tribunal holds that there was no fundamental breach in sales contract justifying the avoidance. If decided to the contrary, Respondent 2 cannot be held liable for such breach.

SUMMARY OF ARGUMENT

I. Arbitration clause from the contract between Respondent 1 and Claimant cannot be extended over Respondent 2. (A) Respondent 2 did not show any intention to be bound by this arbitration clause, and (B) the arbitration agreement included in the contract cannot be extended to Respondent 2 because of the principle that contracts may not be concluded to the third party detriment. Furthermore, (C) there is no joint venture between Respondent 1 and Respondent 2, and (D) Respondent 1 and Respondent 2 did not constitute group of companies.

II. The arbitration proceedings cannot be conducted because of the serious effects of the insolvency proceedings of Respondent 1 on it. (A) There is no such public policy that obliges the arbitration tribunal to conduct the arbitration proceedings in current case. (B) Secondly jurisdiction of the Arbitral Tribunal is affected by the insolvency law as a mandatory law that must be taken into consideration by the Tribunal. Moreover, (C) the insolvency proceedings commenced in Oceania could have legal effects in other countries irrespective of the adoption of the Insolvency Model Law. (D) The arbitration agreement is void as a result of reasonable use of Oceanian law to govern the arbitration agreement. Furthermore (E) the dispute as a core insolvency matter is not arbitrable. (F) Finally, if the Arbitral Tribunal rendered award, it would be unenforceable in other countries than Danubia.

III. Respondent 2 is not liable for the breach of contract (A) as potentially binding arbitration agreement as a part of contract does not also imply liability for the breach of main contract due to the doctrine of autonomy of arbitration agreement. Respondent 2 is not subject to liability for the breach of contract through his joint venture interest in Respondent 1 with respect to the legal form of Respondent 1. And besides that, (B) there was a distributor agreement between Respondent 2 and Respondent 1. (C) An agency between Respondent 2 and Respondent 1 has never been established, neither by Respondent's 2 ratification of Respondent's 1 actions nor (D) by Respondent's 1 acting with Respondent's 2 apparent authority nor otherwise.

IV. Claimant could not avoid contract because (A) his ability to avoid the contract was encumbered by Respondent's 2 right to cure. Moreover, (B) there is not a fundamental breach of contract that would substantially deprive Claimant of his contractual expectations. Furthermore, (C) the contract between Claimant and Respondent 1 should have been preserved under the principles of cooperation and saving the contract.

I. RESPONDENT 2 IS NOT BOUND BY THE ARBITRATION CLAUSE IN THE CONTRACT SIGNED BETWEEN CLAIMANT AND RESPONDENT 1

1. **(A)** Respondent 2 is not bound by the arbitration clause from the contract between Respondent 1 and Claimant because Respondent 2 did not show any intention to be bound by this arbitration clause. **(B)** The arbitration agreement included in the contract cannot be extended to Respondent 2 because of the principle that contracts may not be concluded to the third party detriment. **(C)** There is no joint venture between Respondents because the character of the relation between them excludes it and **(D)** there is no group of companies because participation of Respondent 2 in the contract concluded by Respondent 1 and Claimant was insignificant and Respondents never showed any intention to be treated like group of companies.

A. Respondent 2 is not bound by the arbitration clause

2. Considering evidence given, Respondent 2 cannot be bound by the arbitration clause signed by Respondent 1 and Claimant as is stated by Claimant *[Memorandum for Claimant par. 2]*. International arbitration is heralded as a voluntary, flexible and autonomous process to resolve disputes between international parties according to the procedures and laws of their choice *[Livingstone]*.
3. Choice of arbitration process is essential. It is generally known that there are exact rules for creating an arbitration clause: firstly, arbitration clause should be in writing and secondly, it has to be signed by the parties. Signature is proclaimed as a substantial part of process of making an arbitration clause. Normally, parties show their intention to refer all disputes between them to arbitration by signing the arbitration agreement or clause.
4. Undoubtedly, the New York Convention requires explicitly arbitration clause in writing. However, Danubia has adopted *UNCITRAL Model Law* with the 2006 amendments. According *to Art. 7 (Option II) of UNCITRAL Model Law* arbitration clause does not have to be in writing. Arbitration clause is defined as *"an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of defined legal relationship, whether contractual or not" [Art. 7 (Option II) of UNCITRAL Model Law]*. The emphasis lies in the intention of parties to be bound by the arbitration clause. And the point of intention is expressed rightly by signing arbitration

clause which did not happen in this case. There is no arbitration clause between Claimant and Respondent 2.

5. Where the contract contains an arbitration clause, there is a presumption of arbitrability in the sense that *"an order to arbitrate the particular grievance should not be denied unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute" [Laboreres v. Berry Cont.]*. This presumption is balanced, however, by the principle that *"arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit" [Laboreres v. Berry Contr.]*.
6. With reference to Procedural Order No. 2 *[Procedural Order No. 2, points 14, 16],* it cannot be assumed that the acceptance of general conditions in the contract between Respondent 1 and Claimant does automatically imply consent of Respondent 2 to be bound by the arbitration clause. It is important to distinguish "acknowledgement" and "obligation". Respondent 2 was aware of the existence of the arbitration clause between Respondent 1 and Claimant. However, acknowledgement of Respondent 2 cannot be misinterpreted as his intention to be bound by this arbitration clause. Distinguishing between acknowledgement and obligation is fully in accordance with the *doctrine of separation* of arbitration clause and the contract.
7. Analysing the question of agency, the contractual relationship in the case at hand cannot be regarded as an agency. Agency agreement is defined as a contractual relationship where the principal agrees to be bound by the agreements concluded by the agent. However, there must be an express or apparent mandate *[Hanotiau]*. Since the agency is not presumed, it must be proved. Nevertheless, Claimant failed to do so. In addition, the reliable distinctive feature between distributorship and agency is the question of ownership. While agency is based on the fact that principal still owes the goods which agent has in his possession, in distributor relation the owner is distributor himself. As is stated in Procedural Order No. 2, the cars which were in possession of Respondent 1 were owned by Respondent 1 himself *[Procedural Order No. 2 point 20]*. Accordingly, this relationship cannot be qualified as an agency therefore Respondent 2 is not bound by the conduct of Respondent 1.
8. Respondent 2 cannot be bound by the arbitration clause simply because there is no arbitration clause or arbitration agreement between Respondent 2 and Claimant. We do not deny business relationship between Respondent 1 and Respondent 2, but with reference to the doctrine of separation, their relation does not automatically amount to submission to

the arbitration clause. The party autonomy and the freedom of contract are widely recognized and as such it has to be respected and followed by both traders and courts. These principles are also codified in the *Principles of European Contract Law [PECL]*.

B. The arbitration clause could not be extended over Respondent 2

9. Extension of arbitration clause over Respondent 2 would be violation of the basic principle of international trade law and law itself that contracts may not be concluded to the third party detriment. Neither Respondent 2 is not party to the contract concluded between Respondent 1 and Claimant, nor did he show any intention to be bound by the arbitration clause from this contract- Therefore Respondent 2 should be considered as a third party in this case.

10. Accordingly with the *ICC Case No. 5721*, Arbitral Tribunal should consider contractual nature of arbitration agreement and should refuse to extend arbitration clause from aforementioned contract to Respondent 2, otherwise severe detriment would be caused to Respondent 2 which is in contradiction with the principle that contracts may not be concluded to the third party detriment *[Gaillard/Savage 442; ICC Case No. 5721]*.

11. *"Certain elements are almost invariably deemed necessary [for the extension of the arbitration clause]. They include a significant measure of direct control of the subsidiary's activities by the parent or shareholder and the insolvency of the subsidiary" [Gaillard/Savage 285; ICC Award No. 8385]*. Respondent 2, as 10% shareholder *[Procedural Order No. 2, point 12]* in Respondent 1, can hardly be considered as a principal to Respondent 1. In this matter, Respondent 1 cannot be identified with Respondent 2 as single legal person. Respondent 2 cannot enforce any decision without Oceania Partners *[Procedural Order No. 2, point 12]* in Respondent 1 which means that the main shareholder in Respondent 1 is Oceania Partners and not Respondent 2. Therefore Claimant should assert his claim against Oceania Partners and not against Respondent 2.

C. Respondent 1 and Respondent 2 did not constitute joint venture

12. With all due respect, Respondent 2 is afraid that Claimant does not understand the nature of joint venture properly. As Claimant cites, *"a joint venture is a partnership between or among two or more parties whereby each party contributes a portion of its assets, expertise, or activities for the purpose of performing a specific business transaction"*

[Memorandum for Claimant par. 2]. Although this definition is correct, by *"specific business transaction"* is in this case meant the creation of Respondent 1.

13. Respondent 2 does not deny that Respondent 1 was a joint venture between Respondent 2 and Oceania Partners but this does not imply that Respondent 1 still has to be joint venturer for Respondent 1. And in fact, he is not anymore. In the case concerned, joint venture was created just for one single operation and once this operation was performed (Respondent 1 was created), joint venture finished and Respondent 2 has kept just 10% share in Respondent 1 which amounts to the level of his initial investment *[Statement of Claim par. 30]*.
14. The relation between Respondent 1 and Respondent 2 is based on distributor agreement *[Procedural Order No. 2, point 13]*. The character of the relation is even emphasized in the trade name of Respondent 1 – UAM Distributors Ltd *[Statement of Claim par. 4]*. Furthermore, Respondent 2 had 10% share in Respondent 1 and he had just one seat from five in the Governing Board of Respondent 1 with remaining 90% share for Oceania Partners *[Procedural Order No. 2, point 12]*.
15. Liability of Respondent 2 in Respondent 1 was limited by the extent of his investment therefore we could also reasonably assume that power of Respondent 2 to take decisions was limited in the same way. It would be very unwise if the party with as small extent of representation as Respondent 2 could considerably influence decisions concerning the company. This is confirmed directly in the *Procedural Order No. 2* stating that *"10 percent ownership by Respondent 2 did not give it a right to block actions agreed to by a majority of the Governing Board" [Procedural Order No. 2, point 12]*. In practice, this statement means that Respondent 2 did not have the veto right with regard to decisions concerning Respondent 1. In other words, Respondent 2 could be easily outvoted by Oceania Partners.
16. Claimant has not proven the existence of joint venture between Respondent 1 and Respondent 2 satisfactorily. Indeed, Mr. Steiner, Regional Manager of Respondent 2, was quoted in Business News of Equatoriana, Respondent 1 and Respondent 2 *"worked closely together for fifteen years" [Claimant's Exhibit No. 16]*. Nevertheless, Arbitral Tribunal cannot assume anything crucial from this statement. It is euphemism and the connection *"worked closely together"* is very vague so Tribunal could not make any presumptions about the extent of cooperation.

17. As far as question of sharing of profits is concerned, Respondent 2 has of course profit from sale of his cars. Respondent 2 also admits that the profit is the reason why he manufactures automotive products. But it is important to note that the profit of Respondent 2 is not dependent on the profit of Respondent 1 because Respondent 1 must pay for purchased cars according to the agreed conditions in sale contract between Respondent 1 and Respondent 2, irrespective of the fact whether Respondent 1 sells the cars immediately or stores them for months. If Arbitral Tribunal compares possible 10% profit from share in Respondent 1 and 100% profit from selling cars to Respondent 1, it is obvious that contingent 10% profit is insignificant for Respondent 2.
18. It should be emphasized that the principal within Respondent 1 was Oceania Partners with 90% share *[Statement of Claim par. 30]*. Therefore, with all due respect, it is unclear why Claimant tries to assert his claims against Respondent 2 and not against Oceania Partners. It is obvious that between Oceania Partners and Respondent 1 is much stronger relation and it is Oceania Partners who is the pivot.

D. Respondent 1 and Respondent 2 did not constitute group of companies

19. Despite the fact that the group of companies doctrine is worldwide recognized, it is important to mention that it is merely an exception to the rule. "*The basic rule remains that an arbitration agreement is binding only upon parties that are privy to it. A restrictive view prevails: the group of companies doctrine can justify the extension of an arbitration agreement signed by one company to other companies within the same group only in specific and exceptional circumstances" [Kaufmann-Kohler/Stucki 20]*.
20. The leading case in the doctrine of group of companies states special conditions of the case which lead to the exceptional extension of arbitration agreement to the non-signatory party. In the crucial case *Dow Chemical*, the arbitration clause was extend to other companies of the group because "*Dow Chemical Company (USA), exercised absolute control over its subsidiaries having either signed the relevant contracts or, like Dow Chemical France, effectively and individually participated in their conclusion, their performance, and their termination" [Dow Chemical]*. It cannot be spoken about absolute control over Respondent 1 by Respondent 2 because Respondent 2 owned only 10% of Respondent 1 and that is definitely not enough to have dominant influence over important strategies of the company *[Statement of Claim par. 30]*.

21. As far as the question of the participation of Respondent 2 in performance of the contract is concerned, Respondent 2 alleges that there is no evidence of it. "*It is usual that the companies are all involved in various aspects of project and their obligations and responsibilities are interrelated" [Mores 34]*.

22. It cannot be alleged that Respondent 2 shared obligations and responsibilities with Respondent 1. Firstly, such obligation is not implied by the contract between Respondent 1 and Claimant. Secondly, Respondent 2 never accepted any obligations from the contract. On the contrary, Respondent 2 pointed out that he did not admit the liability for the condition of cars. Respondent 2 took part in the performance of the contract only after the problem with cars occurred and always declared that it is only because of his interest in good reputation of these cars.

23. For example, in Swiss law *"[t]he current position ... is that the extension of an arbitration agreement to a non-signatory party can be contemplated only where: (a) it may be inferred from documents that such party was duly represented by one of the signatories (which does not result from the mere existence of a group), (b) there has been subsequent ratification, or (c) circumventing the arbitration agreement would constitute an abuse justifying a piercing of the corporate veil" [Kaufmann-Kohler/Stucki 20]*. Respondent 1 never asserted during the negotiations and signing the contract that he is the representative of Respondent 2. There is no evidence that Claimant could presume that Respondent 1 is acting not only on his own behalf but also as the representative of Respondent 2. Furthermore, nothing shows that Respondent 2 would subsequently ratify the contract. The conditions for piercing of the corporate veil were not met either.

24. *"In sum, as confirmed by the arbitral case law, it is not so much the existence of a group that results in companies within the group being bound by an arbitration agreement which they have not signed, but rather the fact that such a result was the true intention of the parties"* [*Kaufmann-Kohler/Stucki 20]*. Although if Tribunal found that Respondent 1 and Respondent 2 were members of the group of companies, there is no evidence that Respondent 2 took important role in the performance of the contract and therefore it cannot be presumed that it was true intention of both Respondents to be bound by the contract between Claimant and Respondent 1. Moreover, the crucial participation of Respondent 2 in the contract is deeply questionable because Respondent 2 never participated in negotiations of the contract and his name was not even mentioned anywhere in the contract.

25. The role of Respondent 2 in negotiations, performance and termination of the contract was purely passive and therefore it cannot justify the application of the group of companies doctrine in order to extend the arbitration clause to Respondent 2.

II. THE INSOLVENCY LAW OF OCEANIA PREVENTS THE ARBITRATION PROCEEDINGS CONDUCTED IN DANUBIA

26. The insolvency of Respondent 1 significantly affect the arbitration proceedings in Danubia because **(A)** there is no such public policy that obliges the arbitration tribunal to conduct the arbitration proceedings in current case, **(B)** the insolvency law of Oceania must be taken into consideration as an mandatory law affecting the jurisdiction of the arbitration tribunal, **(C)** the insolvency proceedings of Oceania could have legal effects in other countries irrespective of the adoption of the Insolvency Model Law, **(D)** it is reasonable to use Oceanian law to govern the arbitration agreement and therefore **(E)** the dispute is not arbitrable, and **(F)** arbitral award rendered by this Arbitral Tribunal will be unenforceable in other countries.

A. There is no such public policy that obliges the Arbitral Tribunal to conduct the arbitration proceedings in current case

27. Public policy, whether international or domestic, always refers to the national legal rules *[Sheppard 218]*. There is no such international public policy dictating the enforcement of arbitration agreements without any conditions as it is alleged by Claimant *[Memorandum for Claimant par. 14]*. The concept of international public policy must always refer to particular national legal order. However, Claimant does not indicate whose international public policy should include such obligation to conduct the arbitration proceedings in current case.
28. Claimant states that in order to promote international business transactions, countries all over the world have promoted the presumptive validity of international arbitration agreements *[Memorandum of Claimant par. 15]*. However, it must be noted that the insolvency proceedings contradicts this policy and "*the court which has opened the (insolvency) proceedings is exclusively competent to decide disputes arising out of the insolvency or such disputes on which the insolvency has legal effects." [Ancel 276]*.
29. The international public policy is mostly referred as "*forum's state's most basic notions of morality and justice" [Sheppard 227]*. Notwithstanding the differences in various legal

families, countries generally esteem their systems of collective treatments of the debtor's obligations in insolvency proceedings as cohesive legal mean for solving economic crisis of businessmen. "*[Monetary] claims may be pursued only within bankruptcy proceedings in accordance with the provisions of bankruptcy law, meaning in fact that any kind of individual pursuit of ordinary bankruptcy creditors' claims outside the bankruptcy is excluded [Lazic 247]"*. For example, France considers in general the principle of the preclusion of individual action and the principle of equality among creditors as a part of both the domestic and international public policy *[Lazic 254; see also Poudret/Besson/Berti/Ponti 306]*. The same conclusion could be made with regards to German law *[Lazic 256]*. Moreover, Claimant himself recognizes that the centralization of claims against debtor in insolvency proceedings is part of the international public policy *[Memorandum for Claimant par. 19]*.

30. The treatment of current dispute at hand outside of the insolvency proceedings might seriously breach the international public policy of all possible forums of the enforcement of the arbitral award. This award would breach the domestic public policy of Oceania, because these arbitration proceedings ignore its insolvency law. The international public policy of Equatoriana could be considered similar to France or Germany, both belonging to the civil law system *[Procedural Order No. 2 par. 8]*.

31. Moreover, the enforcement of the award in Polaria, as suggested by Claimant *[Memorandum for Claimant par. 19]*, will seriously harm the rights of other creditors of Respondent 1. The general goal of the insolvency proceedings is proportional distribution of debtor's assets. However, if Claimant was fully satisfied from the assets in Polaria, other creditors, who filed their claims to the insolvency proceedings in Oceania, would be satisfied only proportionally from the rest of the assets. Claimant would have unjustifiable advantage thanks to his conduct against other creditors in Oceania. *"Insolvency proceedings affect the interests of all the creditors of the business, and the principle of their equal treatment; they necessarily entail suspension of other legal proceedings and the mandatory jurisdiction of national court*" *[Delvolvé/Rouche/Pointon 45]*. We can presume that such grave infringement of the creditors' equality is contrary to the public policy of Polaria, as it is contrary to the public policy of the most countries.

32. Besides, Danubia, the place of the arbitration proceedings, is a party to the *New York Convention* which states in *Art. II* the general obligation that the arbitration agreement shall be recognized when it is in writing. Still, the arbitration agreement may not be

enforced if it is not null and void, inoperative or incapable of being performed. More than 140 countries *[NYC Status]* acceded to this international convention. In general, the legal orders are willing to enforce the arbitration agreements. However, the presence of abovementioned exceptions precludes the existence of the unbreakable international public policy as was suggested by Claimant.

33. The Arbitral Tribunal in not bound by the public policy to conduct the arbitration proceedings in this case. To the contrary, there is the public policy that prefers the collective treatment of claims against insolvent debtor and it would be seriously hampered by the continuation of this arbitration proceedings.

B. Insolvency law of Oceania must be taken into consideration as mandatory law seriously affecting the jurisdiction of the Arbitral Tribunal

34. The rules of law applicable to the contract are not the only ones that the Arbitral Tribunal must take into consideration when deciding the dispute. Any institution or organ resolving the conflict among the parties must also apply rules arising from other legal orders. These mandatory rules apply irrespectively of the law chosen by the parties to govern their contractual relations *[Barraclough]*.

35. Although application of mandatory rules could raise some doubts and discussions, the application of certain categories of mandatory rules is uncontroversial. One of them is transnational public policy, which "*reflects the fundamental values, the basic ethical standards and the enduring moral consensus of the international business community" [Barraclough]*.

36. The principles of the preclusion of individual action and of equality among creditors in insolvency proceedings are protected around the globe. Significant majority of the most developed countries introduced the collective treatment of the claims against debtor into their legal systems in purpose "*to avoid numerous separate litigations and other proceedings with creditors for the settlement of their claims, but to deal with them in one, collective proceedings instead" [Lazic 246]*. They consider these proceedings as vital to promote their economic development. They are truly part of the transnational public policy. In addition, the arbitral tribunal in ICC Case No. 7563 held that there is a "*…principle that individual proceedings should be suspend in the event of bankruptcy" [Gaillard/Savage 356]*.

37. When deciding on a jurisdiction, the Arbitral Tribunal should take into consideration the

advantages of the centralisation of all the disputes involving a party to a single court e.g. simplification and acceleration of the proceedings as is stated by *Ancel*. However*, "this aim would not be achieved if the parties had a possibility to bring the dispute before another jurisdiction, either a state court or an arbitration tribunal*" *[Ancel 274]*.

38. The rules of the insolvency law also pass the tests used to determine if the mandatory rules apply to a case. Claimant fails to conduct the "special connection" test properly *[Memorandum for Claimant par. 19]*. The three elements of this test are "close connection", "mandatory nature of the laws" and the "application-worthiness" *[Barraclough; Art. 7(1) of Rome Convention]*.

39. Claimant argues that there is not sufficiently close connection between the current contract and the insolvency law of Oceania *[Memorandum for Claimant par. 19]*. However, the *Guliano-Lagarde report* stated that the connection is genuine in the case "*when one party is resident or has his main place of business in that other country"*. Respondent 1 is resident in Oceania and furthermore he conducts his business activities primarily there *[Statement of Claim par. 4, 7]*.

40. Claimant does not conduct the second prong of the test – the mandatory nature of the disputed laws. This omission might be intended and it may imply that Claimant views the insolvency law as mandatory. Notwithstanding this reasoning, Respondent 2 will conduct also this prong to demonstrate the mandatory nature of the disputed law. The *Guliano-Lagarde report* suggested that the existence of similar laws in various countries may determine the mandatory nature of analyzed rules. As we have already shown these rules exist crosswise legal orders *[see par. 29]*.

41. To finally decide, whether to apply the mandatory rules or not, the Arbitral Tribunal should consider the "application-worthiness" of these rules. The commencement of the insolvency proceedings has inevitable and serious impact on all business relations of the party. As will be shown, certain rules and principles of the insolvency law are truly transnational *[see par. 36]*. Furthermore, they represent strong public interest. The interest of the state to protect the equality of creditors and the treatment of the claims in collective proceedings is so strong that it creates a part of the public policy of states. Non-application of mandatory rules would result in the non-enforceability of the arbitral award *[see sub part E]*. The application of the insolvency law of Oceania prescribing the exclusive jurisdiction of the insolvency court of Oceania to treat the Oceanian debtor in insolvency do not create any doubts on the side of the Arbitral Tribunal. By ruling of no-competence to deal with this

case, the Arbitral Tribunal will affirm the worldwide acceptance of the special status of the insolvency law and promotes the consistency of the legal rules of international commercial relations.

C. The insolvency proceedings of Oceania could have legal effects in other countries irrespective of the adoption of the Insolvency Model Law

42. It is necessary to emphasize, contrary to the statement of Claimant *[Memorandum for Claimant par. 26],* that the *Insolvency Model Law* does not provide unified international solution for the cross-border insolvency scenarios. The aim of the proposal is the harmonization, not the unification of the legal standards across the globe *[GA Resolution No. 52/158]*. Therefore the rules provided in the document do not prevent *per se* domestic insolvency rules to be applied. The *Insolvency Model Law* is aimed at promoting the harmonized cooperation among nations in order to support international trade *[Insolvency Model Law, Preamble sub. a), b); guide par. 90]*. As a result, this proposition is not drafted in the way that would forestall the rules of Oceania to be applied in the subject-matter presented, if Arbitrators find them reasonable.

43. According to Claimant, Oceania insolvency courts are not entitled to exercise jurisdiction over this matter and insolvency representative of Respondent 1 cannot void the arbitration clause because Oceania and Danubia have not adopted the *Insolvency Model Law [Memorandum for Claimant par. 26]*. But as it was stated before, these rules have their field of application much larger than only among the signatory countries.

44. More importantly, Respondent 2 must oppose the allegations of Claimant insisting on thoughts that the failure of the state to become "signatory" to the *Insolvency Model Law* automatically prevents insolvency representative to appear before the Tribunal *[Memorandum for Claimant par. 13, 27]*. As was stated, the model laws are not international treaties that might be directly applicable and as such could exclude other rules. It is simply the proposal of the international committee which can be adopted fully or partially by the states. The *Insolvency Model Law* is a legislative text that forms the basis of a recommendation to states for incorporation into their national law *[The Insolvency Service par. 7]*. Consequently, there is no need for Oceania to be the "signatory" to the model law as the sole way how an insolvency representative could be granted the right to appear before the court or the arbitral tribunal.

45. Additionally, Respondent 2 does not accept the claim that the *Insolvency Model Law* itself

forbids such presence of the insolvency representative. Claimant asserts the right to appear does not exist according to the draft notes *[Memorandum for Claimant par. 27]*. However, the draft notes set down "*[i]n States that have not adopted the Model Law, that right of direct access might be limited by formal requirements or by domestic law*" *[UNCITRAL draft notes par. 75]*. It is clear that the right to access the foreign tribunal is not limited by failure to enact *Insolvency Model Law*; it is just not as simple as it could be when proposed piece of legislation was enacted.

46. Should Respondent 2 admit Claimant's allegations, Respondent 1 could not be the party to the arbitration proceedings, because the representative would not have been allowed the access to any tribunal. Thus, this result would dispose of the principle of fairness which is peculiar to international arbitration and render it involuntarily *ex parte* proceedings. As long as the principle of due process is one of the leading values of the arbitration *[Rubino-Sammartano 141*], such result would be contrary to the spirit of the arbitration and the rule of the SCC itself *[SCC Arbitration Rules, Art. 19 par. 2]*.

47. It is true that Ms. Powers would be subjected to the rules of Danubia regarding the recognition of foreign insolvency proceedings. However, Respondent 2 believes there is no compelling public policy of Danubia that would prevent the recognition of Oceania's insolvency proceedings *[see sub part A]*. UNCITRAL harmonization affects also the non-signatory countries in order to ensure the stability of the international commerce. Model laws provide set of the most fundamental and core rules that are recognized in the global legal world. "*[I]ts influence greatly exceeds the scope of these states. On numerous points, the Model Law contains rules which are universally recognized in the practice of international commercial arbitration. On other points, it is a guide which no legislature can henceforth ignore, even if it decides not to adopt the Model law as such*" *[Poudret/Besson/Berti/Ponti 67]*.

48. To summarize, there is no need for states to adopt the proposed cross-border insolvency legislation in order to grant the right of foreign insolvency representative to appear before courts and tribunals. However, the *Insolvency Model Law* implies strong transnational public policy in favor of foreign insolvency proceedings grounded by the equal protection of creditors.

D. It is reasonable to use Oceanian law to govern the arbitration agreement.

49. If the parties failed to stipulate the governing law to the main contract (subsequently to the

arbitration agreement), there is no direct connection between the seat of arbitration and the substantive law applicable to the dispute. Though it is true that the *lex situs* of the arbitration is often considered to be applicable to evaluate the validity of an arbitration agreement, it is not the universal rule as it is claimed in the petition *[Memorandum for Claimant par. 21]*. The choice of the forum can simply mean nothing more than the choice of convenience for both parties *[Gaillard/Savage 235]*. Without knowing more about the real intention of the parties, it cannot be assumed that their intention was to impliedly determine the applicable law to the main contract by choosing the situs of the forum.

50. Secondly, Claimant suggests that in accordance with selecting the foreign tribunal it was the intention of the parties to transfer the jurisdiction over the dispute to different forum *[Memorandum for Claimant par. 22 citing Interim Award in ICC Case No. 6149]*. Even if Respondent 2 admits such allegation, such consideration has little effect on applicable law. Respondent 2 asserts that the intention of the parties was primarily aimed at the choice of jurisdiction not substantive law. However, if Claimant believes otherwise, there is no mutual consent of wills and at least it could not be concluded that the forum selection provided the applicable law selection.

51. Moreover, even the arbitral tribunal in quoted ICC award did not dispose of the law (Jordanian) that voided the contract. The ICC tribunal only held that even if arbitral tribunal is international body, "*court ... is not necessarily bound by the considerations of Jordanian domestic public policy at least insofar as Jordanian law is not applicable to the subject matter*." *[Interim Award in ICC Case No. 6149]*. However, in case presented the situation is different. The law of Oceania is not just some law of irrelevant third country, but potential law governing the contract itself (in scope not covered by the *CISG*). Contrary to the statement of Claimant *[Memorandum of Claimant, par. 24],* the appropriate rules to be applied in the contract are Oceanian. It was shown that the real intent of the parties is unknown; therefore the Tribunal must apply general rules of conflict of laws and determine the applicable law. Outside the scope of the *CISG*, Respondent 2 agrees with Claimant that the law of the party providing substantial performance (the seller) should govern the contract *[Memorandum of Claimant par. 25]*.

52. However, Respondent 2 does not share the Claimant's view that this law could not be the law of Oceania. Respondent 2 is not party to the legal relation from which the dispute arises *[see sub part C]*. Furthermore, the use of a logic employed by Claimant should result in finding "the principal wrongdoer". The crux of conflict is not in defective cars

themselves as claimed, but in faulty Engine Control Units. These units are manufactured by the separate entity – Bering Engine Controls. If the Tribunal accepted Claimant's reasoning and looked for the initial seller of faulty goods, the applicable law would not favour Equatoriana, but the law of seat of third subject. Or should the Arbitral Tribunal go further and discover the manufacturer of faulty chip? It is sufficient to note that neither Danubia nor other countries involved have rules that would protect commercial sub-purchaser and hold the manufacturer liable to him for faulty goods *[see Procedural Order No. 2 par. 6]*. In conclusion only two possible laws might be reasonable to apply in this case, i.e. law of one of the contracting parties - either Mediterraneo or Oceania.

E. The dispute is not arbitrable

53. Even if Danubian law is applied to the contract or the arbitration agreement, it does not mean that the insolvency proceedings have no influence on the arbitration proceedings. Still, the question of arbitrability must be determined.

54. In the list of the disputes that are not capable of being settled in arbitration there are generally those which concern competition, patents or insolvency *[Rubino-Sammartano 181]*. Also dispute between Claimant and Respondent 1 concerns insolvency. With regard to the arbitrability of the dispute core insolvency matters and non-core insolvency matters must be distinguished. Core insolvency issues are generally not arbitrable *[Lew/Mistelis/Kröll 206]*.

55. Whether the insolvency proceedings are core depends on: (1) whether the contract is antecedent to the reorganization petition, (2) the degree to which the proceedings are independent of the reorganization. The latter inquiry hinges on the nature of the proceedings. Proceedings can be core by virtue of their nature if either: (a) the type of proceedings is unique to or uniquely affected by the bankruptcy proceedings; or (b) the proceedings directly affect a core bankruptcy function. Core insolvency functions include fixing the order of priority of creditor claims against a debtor; placing the property of the bankrupt, wherever found, under the control of the court for equal distribution among the creditors; and administering all property in the bankrupt's possession *[In re United States, Inc. 637]*. In the case in question, the arbitration proceedings undoubtedly affected core bankruptcy functions as they were mentioned above. Therefore, the Arbitral Tribunal should hold the dispute non-arbitrable as a core insolvency issue and suspend the arbitration proceedings.

56. The non-arbitrability of the dispute is also supported by decisions of national courts in various countries. As showed by *Ancel* there are several judgments given by French Court of Cassation approving that the commencement of the insolvency proceedings constitutes an extraordinary situation and in these cases "*the dispute was not arbitrable since the public policy of (the place of) the court which had commenced insolvency proceedings does not allow to submit the dispute to neither arbitration proceedings nor to another court (which would be different from the court that commenced insolvency proceedings)*" *[Ancel 274]*. In the Netherlands, "*the arbitrability of claims against the estate in bankruptcy seems to be excluded unless the arbitration is already pending at the time of declaration of bankruptcy" [Poudret/Besson/Berti/Ponti 307]*. In addition, it was held in Germany that "*claims against the estate have to be filed in bankruptcy and if contested are then arbitrable"* and furthermore "*an arbitration agreement becomes inoperable if one of the parties lacks the necessary funds for arbitration proceedings, which might be the case when a company is insolvent" [Lew/Mistelis/Kröll 208]*. However, in the case laid before Tribunal, the arbitration proceedings were neither pending at the time of declaration of insolvency *[Statement of Claim par. 28],* nor the claim was included in the schedule of claim *[Procedural Order No.2 par. 31]*. Moreover, it is likely that insolvent Respondent 1 lacks necessary funds for arbitration proceedings.

57. The claims of ordinary insolvency creditors aiming at payment from the estate are core issues *[Lazic 264]* and as such are considered to be non-arbitrable. The current dispute falls under this category. It is an ordinary claim which arose from the ordinary commercial contract. Claimant with his claim falls under the category of ordinary creditor and as such has only possibility to require his claim through the insolvency proceedings commenced with Respondent 1.

58. Therefore, there are several serious reasons for the Arbitral Tribunal to dismiss the arbitration proceedings on the ground of non-arbitrability of the dispute. The dispute is core insolvency matter and as such it is non-arbitrable. Even if arbitrators hold that the case at hand does not concern core insolvency, it does not mean that the dispute is arbitrable. The non-arbitrability of the dispute is supported by decisions of national courts in various countries and as a result the Arbitral Tribunal does not have the jurisdiction to try this case.

F. Arbitral award rendered by this Arbitration Tribunal will be unenforceable in other countries

59. One of the general obligations of the Arbitral Tribunal is to render an enforceable arbitral award *[Art. 47 SCC Arbitration Rules; Barraclough]*. The Arbitral Tribunal owes this obligation mainly to the parties of the dispute. If the Arbitral Tribunal decides to carry on the arbitration proceedings, result of which is unenforceable arbitral award, this obligation will be neglected and the advantages of the arbitration proceedings will be frustrated.

60. The arbitral award is planned to be enforced in Oceania, home country of Respondent 1 or Polaria, where Respondent 1 has some assets, and in the Equatoriana, home country of Respondent 2 *[Memorandum for Claimant par. 12]*. All of these countries are parties to the *New York Convention* and the arbitral award rendered by this Arbitral Tribunal will be sought to be enforced under the rules of the *New York Convention*.

61. The arbitral award cannot be also enforced against Respondent 1 due to the requirements set by the *New York Convention*. The arbitral award cannot be enforced according to the *Art. V(1)(a) New York Convention* because Respondent 1 is under the incapacity to conduct arbitration proceedings, which is also confirmed by Claimant *[Memorandum for Claimant par. 1, 9]* and is a result of a dispossession and appointment of the insolvency representative. Furthermore, the arbitral award will be rendered in non-arbitrable dispute and as such unenforceable according to the *Art. V(2)(a) New York Convention [see also sub part E]*. Moreover, the arbitral award will be contrary to the public policy, which is another condition for the refusal *[Art. V(2)(b) New York Convention]*.

III. RESPONDENT 2 IS NOT LIABLE FOR THE BREACH OF CONTRACT BY RESPONDENT 1

62. The Arbitral Tribunal should find that Respondent 2 is not liable for the breach of contract by Respondent 1 because **(A)** arbitration agreement in question is independent from main contract and Respondent 2 is not jointly and severally liable for joint venture debts and obligations, **(B)** the relationship between Respondent 2 and Respondent 1 was a distributorship, not an agency. **(C)** Respondent's 2 actions may not be considered as principal's ratification of agent's acts and **(D)** Respondent 1 did not act with Respondent's 2 apparent authority

A. Arbitration agreement in question is independent from main contract and Respondent 2 is not jointly and severally liable for joint venture's debts and obligations

63. Claimant states that if the Tribunal finds that Respondent 2 is subject to the arbitration agreement through his joint venture interest (share) in Respondent 1, then Respondent 2 must also be subjected to liability for the breach of contract in question and that he as a joint venturer is jointly and severally liable for joint venture debts and obligations *[Memorandum for Claimant par. 30]*.

64. Even if the Arbitral Tribunal potentially finds that Respondent 2 is subject to the arbitration agreement through his joint venture interest in Respondent 1 or on any other grounds, this does not necessarily imply that Respondent 2 must also be liable for the defective Tera cars under the contract.

65. In spite of the fact that the arbitration agreement in question has been a part of contract, considering procedural and substantial matters, it is necessary to distinguish merits and effects of arbitration agreement with respect to the doctrine of separability of arbitration agreement from main contract. Consequently, the fact that Respondent 2 is bound by the arbitration agreement does not necessarily mean that he is liable for the breach of sale contract.

66. This approach has been supported in a well-known decision *Gosset* where the Court of Cassation held that *„[i]n international arbitration, arbitration agreement, whether concluded separately or forming part of legal document which it covers, always has completely legal autonomy" [Gosset]*.

67. According to the aforementioned case law and doctrine of separability of arbitration agreement, it appears clear that question of binding nature of arbitration agreement and question of liability for the breach of main contract must be considered separately and that they do not determine each other.

68. There have been four basic legal forms of joint venture used in international business world: a corporation, a partnership, a limited liability company and a contractual venture. The characteristic of the joint venture company and a lot of legal consequences that affect also issues regarding ownership and liability of company and venturers, rights and duties of venturers and type of management derive from the form of joint venture.

69. To answer the question whether Respondent 2 should be liable for the breach of contract because of his joint venture interest in Respondent 1 jointly and severally, it is necessary to take into account also the legal form of Respondent 1.

70. Respondent 1 was set up as a joint venture between Oceania Partners and Respondent 2 in order to market cars manufactured by Respondent 2 *[Procedural Order No. 2 point 12]*. There are two basic types of joint venture: an equity joint venture with legal personal status and a contractual joint venture without it *[Luo 215]*. Respondent 2 and Oceania Partners created legally and economically organized entity separated from its founders to achieve their business objectives, though they could have created a joint venture without separate legal personality.

71. Claimant states that a joint venturer is jointly and severally liable for joint venture debts and obligations *[Memorandum for Claimant par. 30]*. This allegation, however, cannot be applied in question of liability for the breach of contract in current case. Claimant failed to mention a significant fact that Respondent 1 is not a partnership but a limited liability company as it may be evidenced from his trade name.

72. Trade name of Respondent 1 contains an abbreviation of legal form "Ltd" which means, with respect to the general company law, that liability of each venturer is limited to the amount of the venturers's interest in the company *[Glover/Wassermann 4-11]*.

73. According to the aforementioned legal form of Respondent 1 and consequently the general principle of company law, it may be concluded that Respondent 2 is not and cannot be liable for the breach of contract jointly and severally because of the form of his joint venture interest in Respondent 1.

B. The relationship between Respondent 2 and Respondent 1 was a mere distributorship and not an agency

74. Claimant in his memorandum states that Respondent 2 as a principal impliedly ratified Respondent's 1 authority to act as an agent during the course of performance of the contract, thus forming an agency relationship pursuant to *Art. 15 CAISG [Memorandum for Claimant par. 33]*. Consequently, as Claimant states, Respondent 2 should be held liable for the breach of contract on these grounds *[Memorandum for Claimant par. 34]*. In the alternative, Claimant states that Respondent 1 acted with apparent authority of Respondent 2 under *Art. 14 CAISG* when contracting with Claimant *[Memorandum for Claimant par. 35-36]*. Respondent 2, however, is convinced that such interpretation of his

actions is wrong as there has never been an agency relationship between Respondent 2 and Respondent 1, neither expressed nor implied.

75. Since the very beginning of the contractual relationship between Respondent 2 and Respondent 1, both parties to the contract must have been conscious of the fact that it is a typical distributor agreement. Respondent 2 as a manufacturer was selling cars to his authorized importer Respondent 1, who was selling the cars further. As expressly stated in *Procedural Order No. 2*, the contract between Respondent 2 and Respondent 1 has indeed been a distributor agreement *[Procedural Order No. 2 point 13]*.

76. Moreover, even the trade name of Respondent 1 supports the fact that there was a distributor agreement rather than agency. The whole name of Respondent 1 in fact is "UAM Distributors Oceania Ltd" (with UAM standing for "Universal Auto Manufacturers"), leaving little doubt that Respondent's 1 business was based on distribution of products manufactured by Respondent 2 in the region of Oceania.

77. The fundamental distinction between a distributorship and an agency is clear. Unlike the principal in case of agency, the manufacturer in case of distributorship is not involved in the contracts concluded between the distributor and his customers and, as a result, it is exclusively the distributor who is to bear all consequences of his deals with the customers. In other words, the distributor is acting solely on his own behalf and not on behalf of the manufacturer as in cases of agency.

78. Similarly, as *Hesselink* explains, *"[d]istribution contracts are agreements concluded between a supplier (which may also be the manufacturer of the products) and a distributor (which may either be a wholesaler or a retailer). The supplier agrees to supply the distributor with products. The distributor commits itself to purchasing, distributing and promoting such products in its own name and on its behalf" [Hesselink et al. 257]*. Furthermore, *"[a]cquiring in his own name and on his own behalf the goods that he sells to his customers, the distributor does not qualify as an agent" [Cheng/Cheng 176]*.

79. Having clarified that the relationship between Respondent 2 and Respondent 1 amounted to a distributorship, it seems apparent that Respondent 2 as the manufacturer cannot in any way be held liable for the actions of Respondent 1 as the distributor.

C. Respondent's 2 actions may not be considered as principal's ratification of agent's acts

80. Claimant, having outlined the participation of Respondent 2 in Respondent's 1 attempts to remedy the defective cars, concludes that Respondent 2 ratified Respondent's 1 agent authority by his actions and should be held liable as a principal under *Art. 15 CAISG [Memorandum for Claimant par. 34]*. This conclusion, however, should be dismissed as there is no valid reason to claim that Respondent's 1 acts have been ratified by Respondent 2.

81. Firstly, the fact that Respondent 2 took part in the process of repairs does not *per se* render Respondent 2 liable. Under *CISG*, Respondent 2 was liable to Respondent 1. When Claimant reported the defective cars, Respondent 1 was solely liable (again under *CISG*) for the defects as Respondent 2 remained outside the contractual relationship between Respondent 1 and Claimant. However, it was in Respondent's 2 interests to make sure that the defective cars would be remedied as Respondent 1 might assert his rights against Respondent 2 consequently. It was undoubtedly Respondent 2 as the car manufacturer who would have to remedy the defects in the end. Therefore, staying idle would not be a desirable option for Respondent 2.

82. Secondly, although Respondent 2 agreed to undertake the repairs, at the same time he has expressly denied any liability in an e-mail sent to Claimant on February 28, 2008 *[Claimant's Exhibit No. 4]*. Importantly, Claimant did not make any effort to object to this denial in his response from February 28, 2008 *[Claimant's Exhibit No. 5]*. Thus, Claimant must have been aware of the fact that Respondent 2 did not accept any liability and as far as Claimant's actions are known to Respondent 2, he did not make any reservation in this respect.

83. Claimant states that Respondent 2 ratified Respondent's 1 agent authority by offering to repair the defective cars. In light of what has been previously said, this alleged ratification should be dismissed. On one hand, Claimant must have known about the denial of liability by Respondent 2 and did not oppose to that. On the other hand, Claimant now attempts to infer Respondent's 2 liability from his conduct. As far as Respondent 2 is concerned, it seems unacceptable that Claimant should now be allowed to infer Respondent's 2 liability from his conduct even though Claimant had many opportunities to object to or otherwise challenge Respondent's 2 express denial of liability before.

84. Furthermore, the doctrine of ratification, Claimant is relying on, seems not to be applicable in this case *[Memorandum for Claimant par. 34]*. The doctrine of ratification means that *"[a]n agency is created by ratification when a person who has no authority purports to contract with a third party on behalf of a principal… Where the principal elects to ratify the contract, it gives retrospective validity to the action of the purported agent" [Kelly/Holmes/Hayward 286]*. In other words, *"[i]n some situations, a principal can choose to adopt and ratify transactions which were made entirely without his authority. Where someone has presented to be his agent and used his name, the principal can subsequently ratify the transaction so as to obtain the benefit and undertake the obligations agreed" [Marsh/Soulsby 61]*.

85. Notably, the principle of ratification has been discussed in the case *Keighley, Maxted & Co. v Durant* as well, where Lord MacNaghten stated it to be *"a wholesome and convenient fiction [whereby] a person ratifying the act of another who without authority has made a contract openly and avowedly on his behalf, is deemed to be, though in fact he was not, a party to the contract" [Keighley, Maxted & Co. v Durant]*.

86. For the doctrine of ratification to be applied, several conditions need to be met. Significantly for the case in question, it is widely accepted that the agent must act as an agent if ratification is to be allowed. As *Richards* states, *"[t]he agent must purport to act on behalf of a principal. If an agent purports to act on their own behalf then the principal is not capable of ratifying the acts of the agent. The most common example of this is where the agent fails to disclose the existence of the principal. An undisclosed principal cannot ratify the act of an agent" [Richards 501]*. Similarly, *Kelly* stresses that *"[a]n undisclosed principal cannot ratify a contract. The agent must have declared that he or she was acting for the principal. If the agent appeared to be acting on his or her own account, then the principal cannot later adopt the contract" [Kelly/Holmes/Hayward 286]*.

87. Finally, the same approach has been adopted in the case *Keighley, Maxted & Co. v Durant*, where the House of Lords held that the principal could not be made liable as he was incapable of ratifying the acts of the agent because the agent failed to disclose the principal at the time of the contract concluded with the third person and the third person had not known at the time the contract was made that the agent was acting for anyone other than himself *[Richards 501]*. It needs to be stressed that in the case *Keighley, Maxted & Co. v Durant*, contrary to the case in question, the principal was expressly willing to ratify the actions of the unauthorized agent.

88. As far as Respondent 2 is aware, Respondent 1 did not declare that he was acting for Respondent 2 as his agent when contracting with Claimant. Respondent 1 of course was not even entitled to make such a declaration as a mere distributor relationship between it and Respondent 2 existed *[see sub part B]*. Accordingly, the condition required by the doctrine of ratification has not been met and ratification of Respondent's 1 acts by Respondent 2 would not be legally possible even if it would have been made.
89. Thus, Claimant's assertion that Respondent 2 is liable due to his ratification of Respondent's 1 acts should be rejected by the Tribunal.

D. Respondent 1 did not act with Respondent's 2 apparent authority

90. In the alternative, Claimant states that Respondent 2 should be bound by the acts of Respondent 1 as it had Respondent's 2 apparent authority pursuant to *Art. 14 CAISG [Memorandum for Claimant par. 36]*. Under the doctrine of apparent authority, an agency relationship has been allegedly established according to which Respondent 2 as a principal might be bound by the acts of Respondent 1 as his unauthorized agent. Respondent 2 again cannot agree with this opinion and requests the Tribunal to dismiss such argumentation on the following grounds.
91. According to Claimant, *"[i]n order for apparent authority to be established, there must be statements or conduct by the principal that induced a reasonable and good faith belief in the third party, and the third party must have believed that the principal had granted authority for the specific act or acts performed by the agent that are in issue" [Memorandum for Claimant par. 35]*. Claimant then in detail presents the course of performance of the contract in question according to which it should be clear that Respondent 1 acted with apparent authority of Respondent 2 *[Memorandum for Claimant par. 36-37]*.
92. As *MacIntyre* states, *"[apparent authority] arises not from any agreement between principal and agent, but on account of the principal having made a representation to a third party that the agent has the authority to act on his behalf. If a principal's words or actions give the impression that he has consented to a person acting as his agent, then the principal may be estopped (prevented) from denying this once the third party has acted upon the representation" [MacIntyre 327]*.
93. Respondent 2 believes that the doctrine of apparent authority may not be applied in this case as the factual circumstances of the case do not allow the doctrine's applicability.

According to the *Art. 14 CAISG*, *inter alia*, Respondent 2 must have induced a reasonable and good faith belief in Claimant that Respondent 2 had granted authority for the acts of Respondent 1. This condition of the doctrine's applicability, however, has never been satisfied.

94. Although the conduct of Respondent 2 possibly might have given rise to certain questions regarding the relationship between Respondent 1 and Respondent 2, Claimant could have never believed reasonably and in good faith that Respondent 1 acted with Respondent's 2 apparent authority.

95. Firstly, it needs to be highlighted that the nature of relationship between Respondent 2 and Respondent 1 undoubtedly amounted to a distributorship. Respondent 1 acted in his own name and, as Respondent 2 stresses, on his own behalf when contracting with Claimant. Initially, Claimant is very likely to have believed that he was dealing solely with Respondent 1.

96. Secondly and more importantly, Respondent 2 agreed to undertake the repairs and, at the same time, he expressly denied any liability in an e-mail sent to Claimant on February 28, 2008 *[Claimant's Exhibit No. 4]*. By this statement, Respondent 2 expressly manifested his will not to be bound by the contract concluded between Respondent 1 and Claimant. Since this moment, Claimant could not have believed reasonably and in good faith that Respondent 1 acted with Respondent's 2 apparent authority as Claimant must have been aware of the fact that Respondent 2 denied its liability with Respondent 1 being the only party liable to Claimant. Evidently, Claimant could not have had the impression that Respondent 2 consented to Respondent 1 acting as his agent (and binding Respondent 2, as a result). As Mann, Roberts and Smith state, *"[n]or can apparent authority exist where the third party knows that the agent has no actual authority" [Mann/Roberts/Smith 350]*.

97. Thus, Respondent 2 should not be held liable by the Tribunal as Respondent 1 did not have Respondent's 2 apparent authority due to the lack of reasonable and good faith belief of Claimant required by *Art. 14(2) CAISG*.

IV. CLAIMANT WAS UNJUSTIFIED IN CANCELLING THE CONTRACT

98. Claimant was not entitled to avoid the contract with Respondent 1, because he did not meet several crucial requirements for avoidance. **(A)** Firstly, Claimant's ability to avoid the contract was encumbered by seller's right to cure since there has been serious offer to remedy by repairing the cars. **(B)** Secondly, Respondent's 1 delivery did not constitute a

fundamental breach of contract under *Art. 25 of CISG* as an essential prerequisite of avoidance because necessitous elements of fundamentality of the breach were not fulfilled. **(C)** Last but not least, the contract should have been preserved as the concern over saving the contract prevailed. Claimant wrongfully violated the principle *non concedit venire contra factum proprium* by avoidance of the contract.

A. Claimant's ability to avoid the contract is encumbered by seller's right to cure

99. Claimant's reasoning is based upon his general statement, that his *"ability to avoid the contract is unencumbered by seller's right to cure" [Memorandum for Claimant par.40-41]*. It is to be told unreservedly, that Claimant is regrettably mistaken in this proposition. Respondents straightly contradict to such allegation and further submit clear evidence in disproof of this hypothesis.

100. According to *Art. 48(1) of CISG,* which gives the seller a right to cure defects in performance after the date for delivery, the seller is allowed to cure at his own expense any failure to perform his obligations, if he can do so without unreasonable delay and without causing the buyer unreasonable inconvenience or uncertainty of reimbursement by the seller of expenses advanced by the buyer. In sum, paragraph (1) of the article quoted *"addresses the seller's right to remedy defects or deficiencies in goods that have been tendered - by substituting conforming goods for defective goods or by repairing (or replacing) a defective component part" [Honnold]*.

101. In consonance and after consultation with Respondent 1, Respondent 2 agreed to voluntarily undertake the repair of the cars and offered this cure to Claimant in his letter from February 28, 2008 *[Claimant's Exhibit No. 4]*. In addition, Claimant himself does not contradict this fact *[Memorandum for Claimant par. 41]*. Moreover, Claimant set forth to be pleased and expressed his consent that Respondent 2 would undertake the repairs and his technical personnel would arrive within three days *[Claimant's Exhibit No. 5]*. Next, Respondent's 2 Regional Manager, Mr. Harold Steiner, assured Claimant that everything possible would have been done to speed the repair of the cars *[Claimant's Exhibit No .6]*. Described activities prove Respondents' effort to do as much as they could to fix the cars as soon as possible.

102. Consequently, Respondent‘s 1 right to cure could not have been frustrated. The seller's right to cure should be protected if the cure is feasible. However, the buyer hastily declares the contract avoided before the seller has an opportunity to cure the defect. As well,

whether a breach is "fundamental" under *Art. 25 of CISG* should be decided in the light of all of the circumstances of the case. Hence, where cure is feasible and where an offer of cure can be expected, one cannot conclude that the breach is "fundamental" until one knows the answer to the question, if the seller will cure *[Honnold]*.

103. Respondents' reasoning can be further supported by the view broadly maintained by the legal experts that "*the seller's right to cure under Art. 48, being more specific than the general right to avoid the contract, prevails over the buyer's right to avoid the contract" [Yovel]*. As well, *„in cases where cure by the seller - e.g. by repairing the goods or delivering substitute or missing goods is still possible without causing unreasonable delay or inconvenience to the buyer, there is not yet a fundamental breach, or rather, the buyer may not yet avoid the contract even though the breach otherwise appears to be fundamental" [Schwenzer]*.

104. This opinion is upheld by several decisions of respectable judicial and arbitrational authorities, e.g. by the ICC Court of Arbitration, which held that "*with respect to the buyer's claim for avoidance (termination) of the contract, the Arbitral Tribunal stated that, under both French domestic law and CISG, avoidance (termination) of the contract is only possible for fundamental breach (Art. 1184 French Civil Code and Art. 49 CISG). It held that the buyer was not entitled to avoid (terminate) the contract, because it had denied the seller the opportunity to cure the defects in the goods (Art. 1184 (3) French Civil Code and Art. 48 CISG). Evidence produced by the seller proved that the defects in the goods could have been repaired easily and at a minimal expense*" *[ICC Award No. 7754]*. Similarly, the *Appellate Court Koblenz* in consonance with the Court of the First Instance explicitly held *"that there is no fundamental breach if there is a serious offer to cure the defect" [Koch],* stating that "*even a severe defect may not constitute a fundamental breach of contract in the sense of Art. 49 CISG, if the seller is able and willing to remedy without causing unreasonable inconvenience to the buyer" [Appellate Court Koblenz]*.

105. Thereby, Claimant acted wrongfully in refusing to permit Respondent's 2 mechanics to make the repair, and thus, he was not entitled to terminate the contract in question, even if there was met the necessary requirement of avoidance, the fundamentality of the breach, which, in addition, was not in our case.

B. The sales contract was not breached fundamentally

106. As *Art. 25 of CISG* defines "*a breach of contract committed by one of the parties is fundamental if it results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract, unless the party in breach did not foresee and a reasonable person of the same kind in the same circumstances would not have foreseen such a result*." There was no major failure of Respondents, they performed all their obligations under the contract and therefore no detriment could deprived Claimant of what he was entitled to expect under the contract. Respondents are not liable for complications based on Claimant's anxiety concerning his financial situation, as he ordered 100 of cars, which is widely understood as a large order, made by strong dealers. Another fact is that the cars had been fixed with no difficulties and within a short time.

107. Due to these facts, such a situation could not lead to a fundamental breach of contract. Taking into account abovementioned facts, Claimant's statement that the contract was avoided pursuant to *Art. 49 of CISG* is of the essence. Contractual duties were performed, the cars were delivered, finally also fixed *[Claimant's Exhibit No. 12]* and in addition, they were resold to other distributors *[Procedural Order No. 2 point 24]*. Respondents clearly explained all possible and relevant situations and moreover, Claimant agreed to offered repairs. Thus, the only possible outcome is that Respondents' performance was in accordance with *Art. 48 of CISG* and that both Respondents sought a remedy and performed their contractual duties properly.

108. Claimant tried to base his argumentation on three elements framing fundamental breach *[Memorandum for Claimant par. 42]*. Nevertheless, he did not follow a frame that he had set. It was not proved by Claimant that all elements constituting a fundamental breach of contract were fulfilled. Consequently, there was no fundamental breach of contract if all elements were not fulfilled. Respondent 2 admits that cars might have suffered minor technical problems. As far as quantity and type of ordered goods are concerned Respondent 1 fulfilled his contractual obligations.

109. However, these minor defects could not have deprived Claimant of his contractual expectations. Claimant as an experienced sole trader should have been prepared for unpleasant circumstances. Moreover, as a businessman he must bear the business risk. Though it may be admitted that 25 cars with some misfiring problems could have caused him some difficulties, the situation could not have endangered his business. Therefore the risk was not unreasonable to bear.

110. Claimant ordered a large amount of cars and he agreed that cars were to be shipped as a partial shipment as there would be space available in order to reduce shipping costs *[Statement of Claim par. 9]*. As far as expenses are concerned, it must be mentioned that Claimant had to store only 25 cars from 100 expected. Claimant and Respondent 1 have not agreed on the exact amount of cars to be delivered in each shipment with partial consignment as a possibility, but not a necessity. As a result, Claimant must have expected various amounts of cars. Respondent 1 could have fulfilled the order in one shipment therefore Claimant must have been prepared to store 100 cars at a time. The amount of cars which arrived represented only a quarter of goods ordered. As was shown, Claimant must have been able to store four times more cars. Consequently, he was expected to have enough storage space. As an experienced sole trader, Claimant was supposed to be able to face such a situation. Respondent 1 might not have expected that Claimant was not prepared for such circumstances.

111. Claimant could not suffer monetary harm, as was suggested by Claimant *[Memorandum for Claimant par. 47]*. The minor problems of the cars might have been repaired in several days in Claimant's premises as was suggested by Respondent 2 *[Claimant's Exhibit No. 4 and 6]*. The defects were repaired in five working days by mechanics of Respondent 2 *[Procedural Order No. 2 point 22]*. Cars could have been easily repaired in Mediterraneo, instead of being shipped back to Equatoriana and then repaired. *"It is hereby important that one of the underlying principles for the implementation of the CISG is that a declaration of avoidance of a sales contract should be the mere ultima ratio, i.e., last resort. Any declaration of avoidance leads to the restitution of the parties' performances under their sales contract" [District Court München]*. Other remedies were reasonable and appropriate, e.g. reparation or a price reduction.

112. The aims of *CISG* are to bring the uniformity, save the contract and to prevent disputes among traders in the commercial sale of goods. It should be interpreted that merchants should seek conciliation or another peaceful solution and such one which would accommodate both parties. The contract should not be avoided whenever a minor problem occurs, but parties should try to find mutually satisfactory solution. Therefore, Claimant should have tried to cooperate with both Respondents and to find another solution than avoidance of contract.

113. The good financial situation of Claimant can be implied from the facts that he only paid down payment of 50% of the price and must have been prepared to pay the rest after the

shipments *[Claimant's Exhibit No. 1]* and moreover he was also able to purchase Indo cars with other down payment *[Claimant's Exhibit No. 9]*.

114. Respondent's 2 products have always received enthusiastic reviews and are of good quality as plenty of satisfied customers might be a proof. Claimant is exaggerating when stating that he could have not driven them *[Memorandum for Claimant par. 45]*. If they had been undriveable, they would not have been driven from the port to Claimant's showroom. As he managed to drive all 25 cars from the port to his showroom *[Claimant's Exhibit No. 2]*, these misfiring problems must have been only minor. Therefore, cars must have been driveable enough.

115. Moreover, the burden of proof is upon the party, who stated reasons, Claimant should have proved that the goods were defective at the time of passing the risk. In case *Aluminium and Light Industries Company*, the Court noted *"in addition that the buyer's claims were inadmissible on the merits, in view of the impossibility of determining with certainty the origins of the defects in the goods, since the defects could have been caused wholly or partly by the transport or storage conditions, which were the responsibility of the buyer" [Aluminium and Light Industries Company]*.

116. As stated above Respondents could not have foreseen such a result. On the contrary a new model of Tera small cars received enthusiastic reviews in the trade press *[Statement of Claim par. 9]*. Claimant's argument of the detriments that arose from defects that prevent further sale is exaggerated. He had to store only 25 cars from 100 expected; therefore, he must have been able to store four times more cars. Claimant also paid only 50% of the cars price, so he must have had another sum of cash if he was going to pay the rest of the price. Moreover, Respondent 2 sent his own mechanics to repair these cars, so that Claimant could have expected them to be repaired soon.

117. Respondent 2 ordered the ECU from Bering Engine Controls which is a very reliable company *[Claimant's Exhibit No. 3]*. Although these ECUs were used for the first time in the cars, Respondent 2 reasonably relied on the good quality of the products in the series. Even if Respondent 2 admits that new model might suffer minor technical defects, it was not reasonable to expect large scale problems and unroadworthly cars. Therefore Respondents were in good faith when delivering the goods. Consequently, the alleged deprivation could not have been foreseen by Respondents

118. Although the time can be of the essence in international sale of goods, this is not the issue in current the case, contrary to the Claimant's presumption *[Memorandum for Claimant*

par. 54]. The goods were delivered on time. Claimant confused the late delivery and the quality of goods *[Memorandum for Claimant par. 54]*. The contract allowed partial shipment as space was available and Claimant agreed to this way of shipment when he signed the contract *[Claimant's Exhibit No. 1]*. Respondent 1 followed this agreement. The first consignment was shipped on February 6, 2008, arrived in Fortune City on February 11, 2008 and was cleared customs on February 18, 2008. Claimant confirmed receiving the goods on time and he did not mention a late delivery *[Claimant's Exhibit No. 2]*. However, the goods had been already delivered because the contract contained CIF INCOTERMS 2000. Under these delivery conditions, the goods are delivered when *"the goods pass the ship's rail in the port of shipment" [ICC Incoterms 2000]*. Therefore, it took 12 days for Claimant to receive the cars under his control even if ownership was transferred in the port of shipment *[Statement of Claim par. 10]*. If Claimant was willing to wait a week or more to physically receive ordered cars, it may imply the time was not of the essence for him. Consequently, Claimant could have waited three more days for the mechanics which might have repaired the cars *[Claimant's Exhibit No. 4]*.

119. Nevertheless, Claimant did not seek solution and avoided contract. Despite he stated that he did not have enough space and funds, he bought cars from another manufacturer. If he had enough means to ensure another transaction, he might have waited for reparation because is financial situation could not have been as severe as he stated *[Statement of Claim par. 18]*.

120. The factual background of present case must be strictly distinguished from those to which Claimant refers *[Memorandum for Claimant par. 49, 50, 52]*. The goods purchased in these cases are different from cars, as far as appearance and qualities are concerned. Moreover, there are other differences which make comparisons inconsistent with this case. The non-conformity and unmerchentability were not as clear as proposed by Claimant *[Memorandum for Claimant par. 49]*. The cars were drivable if Claimant managed to drive them to his premises. Misfiring problems might have caused their unmerchantability. However, these problems were to be repaired. The cars might have been sold easily after reparations. Computers without software *[Memorandum for Claimant par. 50]* are comparable to cars without motor. Nevertheless, cars supplied by Respondent 1 did contain motors. The cars suffered misfiring problems, but motors were placed in all 25 cars delivered by Respondent 1. These cases would have been comparable if computers software suffers some problems when delivered. However, this was not the case. Cars were

equipped with all necessary components and misfiring problems might have been fixed. Furthermore, it usually takes less time to repair something than to deliver a new component and to adapt it. Moreover, clothes which are shrunk might not have been repaired *[Memorandum for Claimant par. 52]*. They were useless and the buyer was not able to sell them to anybody even later. Although cars which were repaired after within Respondent's 2 premises, might have been sold easily after the repair.

121. Cars were affected only by minor problems and might have become perfectly merchantable if they had been fixed. Claimant avoided the contract instead of using more appropriate way how to handle this issue like e.g. wait for arrival of mechanics of Respondent 2. The exact date of delivery was not mentioned in the contract. Therefore, it was not a reason for avoidance of the contract, if he could not have sold them immediately. Late delivery might be a reason for avoidance of the contract when it was expressed by a resolution in the contract that time is of essence *[Huber/Mullis 122-123]*. However, there was not such a notion in the contract. Therefore, Respondent 1 might not have known that time is of essence for Claimant.

122. As far as the air port strike, the experienced trader should not act only on the base of some news from the press, radio or television without checking the real situation *[Memorandum for Claimant par. 56]*. Moreover, there was a strong belief if the strike had come the state would have intervened and would have calmed down the situation, because the airport is the only one connection between Meditteraneo and the rest of the world *[Procedural Order No. 2 point 35]*. In this case Claimant could not have known real situation relevant to strike.

C. The contract should have been preserved

123. As there was not right to avoid the contract, Claimant was not released from his contractual obligations. No reason for avoidance of contract under the *Art. 49(1) of CISG* has been fulfilled. As stated above, there was no fundamental breach of contract. Claimant should have cooperated with Respondents, particularly with Respondent's 2 mechanics, to solve existing problems. Nevertheless, Claimant did not follow the principle of cooperation and saving the contract *[Huber/Mullis 183]*. He started to negotiate with another manufacturer. The reason that he had possibility to get cars from another subject caused Claimant's lack of interest in Tera cars and resulted in avoidance of contract *[Claimant's Exhibit No. 9]*.

124. Respondent 1 accepted Claimant's period of notification of his problems with Tera cars and he had offered and promised to Claimant his cooperation and help with this situation. Although Respondent 2 informed Claimant that he would have sent to Claimant his mechanics, Claimant decided to negotiate simultaneously with another manufacturer - Patria Importers, Ltd - and accepted his offer of 20 Indo cars *[Claimant's Exhibit No. 9]*. Thereby Claimant demanded return of the USD 380,000 down payment from Respondent 1 as soon as possible, as he mentioned in his email sent on February 29, 2008, to Mr. Samuel High *[Claimant's Exhibit No. 10]*. By doing so he did not meet his contractual obligations.

125. As stated above, the fact that Claimant notified the avoidance the entire contract is not essential in this case because he did not have the right to do it. Next, the argument that Claimant could not have got a guarantee of repairing the Tera cars is too exaggerated. Mr. Harold Steiner assured him that everything possible would have been done to speed the repair of the cars sent to him *[Claimant's Exhibit No. 6]*. Also the decision of Respondent 2 to send his technical personnel within three days to Mediterraneo should be satisfactory evidence of Respondent's 2 effort to do everything to fix the cars as soon as possible *[Claimant's Exhibit No. 5]*.

126. With regard to Claimant's previous conduct, Respondent 2 had a reasonable expectation and good faith that Claimant would have been waiting until Respondent's 2 technical personnel came. Furthermore, Respondent 2 expected the assistance of Claimant during performing Respondents' right to cure. On the contrary, Claimant changed his intention without circumstances had changed. By avoidance of the contract with Respondent 1, Claimant violated the principle *non concedit venire contra factum proprium,* which means that no one may set himself in contradiction to his previous conduct.

127. The fact that Respondent 2 did not send the service personnel and equipment to Mediterraneo at the end and the defective Tera cars were shipped from Mediterraneo to Universal in Equatoriana on May 17, 2008 *[Statement of Claim par. 22]* cannot be regarded as the acceptance of the avoidance of contract. This has to be conceived as the way how to save costs expended on all way of mechanics because Respondent 2 could have assumed that Claimant would not have cooperated with them *[Claimant's Exhibit No. 10, 11]*. And he also has had to solve the situation about the storage of the Tera cars.

128. To conclude, as both Respondents expressed their real intention to remedy in the sense of the *Art. 48 of CISG* provision, Claimant was not justified to refuse Respondent's 2 offer to

remedy. Irrespective of whether or not the delivered cars had been deficient, Respondent's 1 delivery did not constitute a fundamental breach of contract under *Art. 25 of CISG* as an essential prerequisite of avoidance. For this reasons Claimant was not entitled to avoid the contract with Respondent 1 pursuant to *Art.49(1) of CISG.*

REQUEST FOR RELIEF

129. In the light of the submissions made above, Respondent 2 respectfully requests the Tribunal to find that:

A) Respondent 2 is not bound by the arbitration clause in the contract between Claimant and Respondent 1,

B) The jurisdiction of Arbitral Tribunal is prevented by the insolvency law in Oceania and as a result the Tribunal does not have jurisdiction,

C) Respondent 2 is not liable for the breach of contract by Respondent 1,

D) There was no fundamental breach of contract authorizing Claimant to avoid the contract.

On behalf of Respondent 2
Universal Auto Manufactures S.A.
Respectfully submitted on January 22, 2009, by

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