



Twenty Third Annual Willem C. Vis International Commercial Arbitration Moot

ANALYSIS OF THE PROBLEM FOR USE OF THE ARBITRATORS

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And

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**XXIIIth ANNUAL WILLEM C. VIS
INTERNATIONAL COMMERCIAL ARBITRATION MOOT
XIIIth ANNUAL WILLEM C. VIS (EAST)
INTERNATIONAL COMMERCIAL ARBITRATION MOOT**

**Analysis of the Problem
For use of the Arbitrators**

If you do not already have a copy of the Problem, it is available on the Vis Moot web site, <https://vismoot.pace.edu/site/23rd-vis-moot/the-problem>. In case you downloaded the Problem during October you will need to download the revised version issued at the beginning of November including Procedural Order No 2 and subsequent comments.

This analysis of the Problem is primarily for the use of arbitrators. Arbitrators who may be associated with a team in the Moot are *strongly urged* not to communicate any of the ideas contained in this analysis to their teams *before* the submission of the Memorandum for RESPONDENT.

The analysis will be sent to all teams after all Memoranda for RESPONDENT have been submitted. Many of the team coaches/professors participate as arbitrators in the Moot and therefore receive this analysis. It only seems fair that all teams should have the analysis of the problem for the oral arguments. If the analysis contains ideas teams had not thought of before, the respective teams will still have to turn those ideas into convincing arguments to support the position they are taking. For that reason this analysis often does not more than merely flag the issue without mentioning the arguments for or against a certain position. It does not contain a full analysis of the problem.

All arbitrators should be aware that the legal analysis contained herein may not be the only way the Problem can be analyzed. It may not even be the best way that one or more of the issues can be analyzed. The amount of issues that arise out of the fact situation makes it necessary for the teams to take a decision which of the issues they *emphasize* in their submissions and oral presentations. Arbitrators should keep in mind that the team's background might influence its approach to the Problem and its analysis. In addition, the decision may be influenced by the presentation a team has to respond to. Full credit should be given to those teams that present different, though fully appropriate, arguments and emphasize different issues.

In the oral hearings, in particular in the later rounds, arbitrators may inform the teams which issues they should primarily focus on in their presentation, if they want to discuss certain issues specifically. They should do so, if they want to make the in-depth discussion of a particular issue part of their evaluation.

The Facts

On 11 July 2015, Mr Fasttrack initiated arbitral proceedings with the Secretariat of the Vienna International Arbitral Centre of the Austrian Federal Economic Chamber (VIAC) for his client, Kaihari Waina Ltd (CLAIMANT) against Vino Veritas Ltd (RESPONDENT).

CLAIMANT is a wine merchant specialized in top quality wines for the collectors' and high end gastronomy market. It has developed a particular expertise in Mediterranean Mata Weltin wines from the Vuachoua region and has gained a reputation with its customers of being a particularly reliable source. Due to its high end buyers CLAIMANT only sells Mata Weltin wines of diamond quality.

RESPONDENT is one of the top vineyards in Mediterraneo. It is the only vineyard in the Vuachoua region that has won the Mediterranean gold medal prize for its diamond Mata Weltin in the last five consecutive years.

CLAIMANT has sold RESPONDENT's diamond Mata Weltin wines for the last 6 years with great success. The base of the Parties' economic relationship is a framework contract concluded between them on 22 April 2009 [Exhibit C 1]. The framework contract provides in essence that every year, CLAIMANT would buy a certain minimum number of bottles from RESPONDENT which in return committed to deliver bottles up to a maximum amount of 10.000 bottles. The exact amount will be determined every year by orders placed by CLAIMANT at the end of the year and normally before RESPONDENT starts the negotiations with other customers. The price per bottle is to be agreed between the parties and if no agreement can be reached is to be determined by an independent expert.

The relationship deviates considerably from the normal practice in the wine industry where contracts are generally concluded orally on an annual basis and the producer is not committing to any fixed deliveries. The framework contract was concluded upon the initiative of CLAIMANT for whom certainty of supply is a crucial element of its business model. Thus CLAIMANT wanted to have a guarantee to receive a minimum amount of bottles every year. RESPONDENT agreed to enter into that contract in April 2009 as one of its major customers has gone insolvent at the time and RESPONDENT had a cash flow problem which could be solved through the contract with CLAIMANT.

Since 2009 CLAIMANT has always ordered between 7.500 and 8.500 bottles. In the first month of 2014 RESPONDENT's Mata Weltin wines of earlier vintages won a number of prices. As a consequence, the number of pre-orders which CLAIMANT received from its customers until the mid of September 2014 increased considerably. Unfortunately, extraordinary weather conditions at the end of August led to an extremely bad harvest in 2014 resulting in one of the lowest number of bottles produced. Thus, on 3 November 2014, RESPONDENT informed all its customers by fax that in comparison to previous years it would have to reduce the number of bottles it could deliver to each customer considerably. Due to an organizational oversight CLAIMANT did not read the fax but ordered the following day the maximum amount of guaranteed bottles under the contract. Furthermore, CLAIMANT made clear that beyond those 10.000 bottles of diamond Mata Weltin of the 2014 vintage it would be willing to buy more and enlarge the co-operation with RESPONDENT further [Exhibit C 2].

On 25 November 2014, CLAIMANT's development manager Ms Isme Buharit visited RESPONDENT to discuss the order and future possibilities for cooperation. She was informed by RESPONDENT's CEO, Mr Weinbauer, that he had been very annoyed about the order of 4 November 2014. It seemed to completely disregard his fax of 3 November 2014 in which the need to reduce of the amounts to be delivered had been announced. As a reaction to this perceived disregard Mr Weinbauer had originally even considered terminating the entire contract. In light of Ms Buharit's explanation that the offer was made without any knowledge

about the fax of the previous day Mr Weinbauer gave up the idea of termination and promised to give CLAIMANT's order "a favourable consideration" [Exhibits C 5, R 1].

On 1 December 2014, Mr Weinbauer informed CLAIMANT that RESPONDENT would be willing to deliver between 4.500 and 5.000 bottles of wine at a price of EUR 41,50 per bottle to CLAIMANT [Exhibit C 3]. He justified that reduction with the bad harvest which resulted in a loss of nearly 50% of the ordinary amount of grapes. According to Mr Weinbauer RESPONDENT, taking into account the long lasting relationship to all customers, decided "that it is in the best interest of everyone that we share the available quantities pro rata and deliver therefore only up to half of the ordered quantities" to each customer. Furthermore, Mr Weinbauer announced that RESPONDENT would in the future no longer be able to guarantee the delivery of more than 8.000 bottles due to a new strategy.

In its letter of 2 December 2014 [Exhibit C 6] CLAIMANT's COO Mr Friedensreich accepted the price but rejected the proposal concerning the quantities. He insisted on the delivery of 10.000 bottles and told RESPONDENT that he was not willing to accept any reduction. In his letter Mr Friedensreich raised doubts that RESPONDENT had already binding orders from its other customers as they would normally place their orders only later. In particular, CLAIMANT was not willing to "give up some of our bottles for the delivery to our biggest competitor SuperWines". Around the date of the letter, several articles in wine journals had been published which made reference to a deal between RESPONDENT and SuperWines, a major alcohol retailer [Exhibit C 4]. RESPONDENT had been negotiating with SuperWines since the beginning of 2014, when its biggest customer ran into financial difficulties and RESPONDENT was not sure whether that customer would still be able to take the usual amount of bottles. The new CEO of SuperWines, Mr Barolo, knew RESPONDENT from one of its former positions and according to the articles had been willing to pay a premium to ensure a delivery by RESPONDENT.

Mr Weinbauer reacted very strongly to CLAIMANT's insistence on full delivery. In its letter of 4 December 2014 [Exhibit C 7] he told Mr Friedensreich that he considered CLAIMANT's behaviour "extraordinary!!! Uncooperative and rude!!!" He accused Mr Friedensreich of not understanding the world of high end wine making which is based on "mutual trust and long lasting relationships" and not on written contracts. As a consequence, Mr Weinbauer declared the Framework Agreement to be terminated and declined to deliver a single bottle of Mata Veltin 2014 to CLAIMANT "even if we have to drink them ourselves".

CLAIMANT immediately looked for a law firm in Mediterraneo to represent it in an application for an interim injunction in the courts of Mediterraneo ordering RESPONDENT to keep 10.000 bottles of Mata Veltin 2014 to be delivered to CLAIMANT. In the end, CLAIMANT retained LawFix which is one of the top law firms in Mediterraneo and the only firm willing to work on a contingency fee basis. They agreed upon a considerably reduced hourly rate and an additional success fee of USD 15.000 for all wins on procedural issues and USD 30.000 for winning issues pertaining to the merits.

The application for interim relief was filed on 8 December 2014 and the order was granted on 12 December 2014. RESPONDENT did apparently not pay much attention to the action since its CEO Mr Weinbauer had to undergo open heart surgery at the time which also led to his early retirement by the end of 2014. Given that the 2014 vintage was only bottled in May 2015 RESPONDENT considered the order to be not justified due to a lack of urgency. Nevertheless, RESPONDENT's new management informed CLAIMANT through its lawyer Mr Langweiler on 14 January 2015 that it would not appeal the order for the time being to avoid additional costs [Exhibit R 2]. Mr Langweiler reiterated RESPONDENT'S interest in an amicable solution but made clear that the lack of certainty required a solution within the next two weeks. Mr Langweiler stated that RESPONDENT would start legal proceedings in case no settlement could be reached within the time. The claim to be brought in the courts was attached. RESPONDENT was of the view that the existing arbitration clause in the Framework Agreement was void for

uncertainty and therefore did not exclude the jurisdiction of the courts. The clause is clearly pathological referring to a non-existing "International Arbitration Tribunal (VIAC)". The clause provides:

Art 20: Dispute Resolution/Applicable Law

All disputes shall be settled amicably and in good faith between the parties. If no agreement can be reached the dispute shall be decided by arbitration in Vindobona by the International Arbitration Tribunal (VIAC) under its International Arbitration Rules in accordance with international practice. The number of arbitrators shall be three to be appointed in accordance with the Rules. The proceedings shall be conducted in a fast and cost efficient way and the parties agree that no discovery shall be allowed. The award shall be binding and each party shall comply with the award. This contract is governed by the law of Danubia including the CISG.

Mr Langweiler, however, also made clear that RESPONDENT was willing to agree to the VIAC standard clause with the addition concerning the exclusion of discovery should CLAIMANT consider the clause to provide for VIAC arbitration. As CLAIMANT did not react at all to Mr Langweiler's letter RESPONDENT started proceedings in the courts of Mediterraneo for a declaration of non-liability. On 23 April 2015, upon CLAIMANT's reliance on the arbitration clause the court declared that it lacked jurisdiction [Exhibit C 9]. To defend the action CLAIMANT used the services of LawFix again. For both proceedings CLAIMANT paid to LawFix fees in the amount of USD 50.280 out of which USD 45.000 were success fees. In neither action was RESPONDENT ordered to reimburse CLAIMANT's for the fees paid to its lawyers. Under the procedural law of Mediterraneo each party bears its own costs save in exceptional cases.

With its Statement of Claim dated 11 July 2015 CLAIMANT started arbitration proceedings to get these fees reimbursed from RESPONDENT as well as for the recovery of other damages incurred due to the non-delivery of 5.500 bottles. In CLAIMANT's view the refusal to deliver the 10.000 bottles ordered and the termination of the contract on 4 December 2014 was a breach of contract by RESPONDENT entitling CLAIMANT to recover the damages resulting from this breach. According to the Statement of Claim such damages include firstly the fees incurred by CLAIMANT in the action for interim relief. The latter was in CLAIMANT's view necessary to protect its rights in light of RESPONDENT's refusal to deliver the bottles. Secondly, the damages include the potential profit from selling 5.500 bottles which CLAIMANT lost due to the non-delivery of such bottles. Without specifying this profit any further CLAIMANT claims the profit RESPONDENT has made by selling the wine with a premium to SuperWines. In CLAIMANT's view that is admissible as its own profit would probably have been larger than the one made by RESPONDENT. Even if that should not be the case RESPONDENT should not be allowed to profit from its breach of contract.

The fees incurred for the defense against the action for a declaration of non-liability are in CLAIMANT's view recoverable as damages for RESPONDENT's breach of the arbitration clause.

More specifically CLAIMANT raised the following claims:

1. Payment of damages to be determined by the profits the RESPONDENT made by selling 5.500 bottles of Mata Weltin 2014 to SuperWines.
2. Reimbursement of legal costs of USD 50.280,00.

In addition, to allow a quantification of these profits under No. 1 CLAIMANT made the following procedural request for document disclosure to the Arbitral Tribunal:

To order RESPONDENT to provide to CLAIMANT all documents from the period of 1 January 2014 – 14 July 2015 pertaining to the communication between RESPONDENT and SuperWines in regard to the purchase of diamond Mata Weltin 2014 and any contractual documents, including documents relating to the negotiation of the said contract between SuperWines and the RESPONDENT in regard to the purchase of diamond Mata Weltin 2014. That includes in particular all documents relating to the number of bottles purchased and the purchase price.

RESPONDENT asked the arbitral tribunal to reject the claim for a disclosure of documents as well as all claims for damages.

RESPONDENT accepted the jurisdiction of the arbitral tribunal established under the Vienna Rules and both Parties agreed that the arbitration clause is governed by the CISG. Thus, there is no need to discuss the question whether the clause is valid and for what type of arbitration it provides.

These agreements, however, were only reached after the arbitration proceedings had been initiated. In January 2015, the content of the arbitration clause was still open to questions. Thus, the “pathology” may be relevant for the question of whether CLAIMANT had an obligation to cooperate with RESPONDENT in determining a specific meaning for the clause.

The Tribunal and the Parties have agreed on an unusual mode to proceed to save costs. They decided to address CLAIMANT’s claims for damages first on the basis of the assumption that the termination of the contract and the refusal to deliver any wine was a breach of contract. Furthermore, it was agreed that the Arbitral Tribunal will first merely address the questions whether an existing damage claim in principle covers the various heads of damages claimed. Any detailed discussion will then occur subsequently once the Arbitral Tribunal has taken a decision on whether or not to grant the request for document production. In light of the Arbitral Tribunal’s conclusion on the damages which may be due in such a scenario RESPONDENT is then entitled to decide whether it wishes to pursue its original defense that the decision to terminate the relationship was not a breach of contract but justified in light of the limited quantities of wine produced in 2014 and CLAIMANT’s behavior. That would then be addressed in a second phase of this case, should RESPONDENT decide to seek a decision on whether a breach actually occurred.

The Issues

In the light of the above agreement the Tribunal has set forth the issues to be decided in the first part of the proceedings, and therefore at issue in the Moot, in Procedural Order No 1 para. 5. It has ordered the Parties to address in their next submissions and at the Oral Hearing in Vindabona (Hong Kong) the following issues:

- a. Does the tribunal have the power and if so should it order RESPONDENT to produce the documents requested by CLAIMANT?
- b. Is CLAIMANT entitled to the damages claimed for the litigation costs of US\$ 50.280 incurred partly

- i. in its application for interim relief?
- ii. in its successful defence against the proceedings in the High Court of Capital City.
- c. Can CLAIMANT claim the profits RESPONDENT made by selling the bottles to SuperWines as part of its damages, even if that includes further profits?

It was left to the Parties to select the order in which they address the various issues. It was, however explicitly stated that **no further** questions going to the merits of the claims should be addressed. In particular the question of whether RESPONDENT's behavior constituted a breach was not to be discussed. The Parties had agreed that RESPONDENT reserved the right to contest that its behavior constituted a breach but accepted that for this phase of the arbitration it was to be assumed that it constituted a breach. Such an agreement is unusual in practice but may in the present case be driven by tactical considerations. RESPONDENT may consider its case on the breach of contract to be so weak that it is not willing to disclose at this stage all its contracts with other customers without having first tried to raise different defense where such a disclosure would not necessarily be required or could be limited to the contacts with one customer.

General Considerations

The case includes a number of problems which are regularly encountered in international business transactions. In the light of the Parties' agreement, not all of them are in the end relevant for the "solution" of the case and will have to be discussed in the written submissions or the oral pleadings. That applies, for example to the question of whether the clearly pathological arbitration clause constitutes a sufficient basis for the jurisdiction of the tribunal, which law governs the arbitration clause or whether the extraordinary weather conditions justified a reduction of the number of bottles to be delivered.

These facts provide, however, the background against which the questions finally relevant at this stage of the proceedings have to be discussed. The procedural as well as the substantive issues to be discussed both touch upon some of the fundamental principles of arbitration (party autonomy and its limits) and of the law on damages under the CISG. In combination with the contractual – and/or even statutory – obligation to cooperate in good faith the facts provide ample opportunity for the parties to discuss the topics from different angles.

The broad topics to be discussed by the students are the following:

- 1) In relation to arbitration:
 - a. The existence and extent of substantive obligations or duties arising from an arbitration agreement, in particular a duty to refrain from initiating court proceedings and a duty to cooperate in the resolution of the dispute,
 - b. Parties' agreement on the taking of evidence and possible limits in relation to document production.
- 2) In relation to the CISG:
 - a. The recoverability of legal cost under Art. 74 CISG and the reach of a possible reimbursement,
 - b. The extent to which profits made by a breaching party should be taken into account in the context of Art. 74 CISG (disgorgement of profits) .

In the case the procedural and substantive problems are closely interwoven. There are consequently several ways to structure the submissions and presentations. Procedural Order No 1 left it to the parties "to decide in which order they address the various issues". The

particularities of the present case would justify a deviation from the “normal” order to first discuss procedural issues. The requested documents, for example, are only relevant for the case and material to its outcome if RESPONDENT’s profits can be taken into account in the context of Art. 74 CISG or otherwise. Equally, it could make sense to address first whether legal costs are recoverable at all under Art. 74 CISG, before discussing the question of whether CLAIMANT was obliged to help sorting out the problems arising from the pathological arbitration clause. Consequently, the following remarks are merely intended to highlight the legal issues arising from the problem. They do not suggest any order in which issues should be treated. They are deliberately only based on a distinction between procedural and substantive issues. It is for the Arbitrators to evaluate whether the parties have addressed the problems in a convincing and effective order in their written submission and to suggest an order for the oral hearings should the parties not have agreed upon an order.

CISG Issues: Procedural Order No 1 para. 5 (1b)-(1c)

The substantive part deals with two controversial questions relating to the scope of the remedy of damages. The first concerns the question whether CLAIMANT can refrain from proving its own actual damages but instead claim the profits made by RESPONDENT as a consequence of the breach of the contract as damages or otherwise (I). The second issue is whether costs incurred in legal proceedings directly associated with the breach of contract and which are not reimbursed under the applicable procedural law constitute damages in the sense of Art. 74 CISG (II).

I. Calculation of Damages – Disgorgement of profits

1. Background

With its e-mail of 2 December 2014 [[Exhibit C 6](#)] CLAIMANT ordered 10.000 bottles of Mata Veltin 2014 for the price suggested by RESPONDENT. RESPONDENT in the end only delivered 4.500. Both parties have agreed for this phase of the arbitration that this constituted a breach of contract. CLAIMANT now wants to recover those damages which result from its inability to sell the other 5.500 bottles to its customers. In principle, the profits lost due to the non-availability of the 5.500 bottles would be damages recoverable under Art. 74 CISG.

According to the file (PO 2 para. 11), CLAIMANT managed to order the missing 5.500 bottles from Vignobilia, another high end producer from the region due to extraordinary circumstances. The profits generated by the sale of these other bottles would most likely have to be deduced from the damages incurred. In light of the particularities of the high end wine market it may turn out to be extremely difficult – though not impossible – to calculate the actual loss made by CLAIMANT taking into account the substitute transaction (PO 2 para. 13).

In the absence of presently available data CLAIMANT, however, does not even try – and may be not want - to prove those damages. Instead, CLAIMANT claims as damages the profits generated by RESPONDENT through the sale of those 5.500 bottles to SuperWines at a premium. First, CLAIMANT alleges that these profits are the minimum profit it would have generated from the sale of these bottles to its customers. In the wine industry it is very likely that the margin generated by the wine merchant in its sale to the end user is higher than that of the producer in its sale to the merchant. In the present case, it might, however, be necessary to deduce from the former the profits made by the substitute sale. In light of that CLAIMANT submits secondly that irrespective of the actual damage incurred by CLAIMANT, RESPONDENT should be deprived of any profits made through its breach of contract. In essence, what CLAIMANT is asking for is a disgorgement of profits.

To prove the profits made by RESPONDENT through its sale to SuperWines, CLAIMANT asks the Tribunal to order RESPONDENT to produce all documents relating to RESPONDENT's negotiations with SuperWines (see Arbitration Question 1).

2. Profits of a breaching party as damages

The wording of Art. 74 CISG leaves no doubt that the main purpose of the remedy of damages under the CISG is to ensure that a party is compensated for the losses resulting from the breach of contractual obligations by the other party. Different views exist, however, whether that is the sole purpose or whether there are additional purposes which could justify a disgorgement of profits.

According to the prevailing view Art. 74 CISG, in light of its clear wording, cannot constitute the basis to skim off the profits realized by the breaching party. It focusses only on the loss of the aggrieved party and does not make the gain of the breaching party a relevant factor in determining the amount of damages. Pursuant to the wording of Art. 74 CISG, damages "consist of a sum equal to the loss, including the loss of profit, suffered by the other party as a consequence of the breach".

According to some authors (e.g. Schmidt-Ahrendts, Disgorgement of profits under the CISG, in: Schwenger/ Spagnolo (eds.), State of play: the 3rd Annual MAA Schlechtriem CISG conference, international commerce and arbitration, Vol. 11, pp. 89 - 102) the rules on damages also serve additional purposes including the purpose to ensure compliance with contractual obligations, i.e. the principle of *pacta sunt servanda*. In their view, it is consequently also possible to take into account equitable considerations in applying the remedy of damages allowing for some flexibility in calculation. In particular, where the aggrieved party has difficulties in proving its loss otherwise, the profits realized by the breaching party are admitted as proof for the loss incurred, in light of the fact that Art. 74 CISG does not contain a definition by which method to calculate losses. The profits made by the breaching party are an indication of the market value of the goods.

In the present case, it would have been difficult – but not impossible – for the CLAIMANT to calculate and prove the exact profit it would have made selling the 5.500 bottles (PO 2 para. 13). Whether that is sufficient to calculate CLAIMANT's damages on the basis of profits made by RESPONDENT depends to a large extent on the position taken on the interpretation of Art. 74 CISG. Furthermore, concerning the difficulties in proving the actual loss the following facts may become relevant:

- CLAIMANT actually received 4.500 bottles of RESPONDENT's Mata Veltin 2014 and charged a price for them and sold the 5.500 bottle from Vignobilia to his customers at a certain price
- Eventual loss of goodwill and reputation for not being able to deliver the required quantity

3. Other ways to justify disgorgement of profits

An alternative way of justifying the claim for a disgorgement of profits is by an analogy to Art. 84 (2)(b) CISG. It provides that in case of the avoidance of a contract the buyer which is unable to return the goods has to "account to the seller for all benefits which he has derived from the goods". One could consider it to be a general principle on which the CISG is based in the sense of Art. 7(2) CISG which fills in a gap as to the treatment of the disgorgement of profits. That line of argumentation requires, however, the existence of a gap within the CISG. Again, the argument is

difficult to make in light of the comparatively detailed provisions on damages but not impossible. One could take Art. 84 (2)(b) CISG as the basis for a remedy for unjust enrichment.

CLAIMANT furthermore relies in its Statement of Claim (para. 26) on “the principle of good faith underlying the CISG”. Pursuant to Art. 7 (1) CISG good faith has to be taken into account in the interpretation of the various provisions of the CISG. Whether it may also justify an interpretation against the clear wording or may even create additional substantial duties for the Parties is, however, very doubtful and controversial.

Other considerations which may become relevant either in the context of one of the above lines or arguments or as separate line of argument are

- that disgorgement of profits best serves the purposes of the CISG to ensure performances by reducing any incentive for breach
- that there is a growing trend to allow for disgorgement of profits in the law of damages in various countries
- that the bad faith behaviour of RESPONDENT in admitting a new customer and delivering 5.500 bottles to this customer requires the disgorgement of all profits made through this behaviour

II. Compensation of legal costs in proceedings under Article 74

1. Background

Following Mr Weinbauer’s emotional reaction to CLAIMANT’S insistence on delivery in December 2014 and his threat to deliver no bottles at all CLAIMANT looked for a law firm which could represent it in an action for interim relief. Representation by local counsel is mandatory in Mediterraneo. As the legal costs in Mediterraneo are higher, there was an unfavorable exchange rate and CLAIMANT was in the process of acquiring another company which would have tied up much of its resources, CLAIMANT was first looking for third-party funding and then for a contingency fee arrangement. The only firm willing to agree on a contingency fee was LawFix which was then retained by CLAIMANT followed by the conclusion of a Contingent Fee Agreement [Exhibit C 10]. According to this agreement LawFix charged an hourly rate of USD 200, which was below the ordinary hourly rate of the firm (see PO 2 para. 39: USD 450 per partner, USD 150 for first year associate) and the average partner rate in Mediterraneo (USD 350). In return it asked for a contingent fee in case of success. The relevant provision in the contract reads:

(2) The contingency upon which compensation is to be paid as:

- Winning on procedural matters pertaining to the contract: US \$15,000
- Winning on issues pertaining to the merits of the contract: US \$30,000

CLAIMANT also retained LawFix to defend the action for a declaration of non-liability initiated by RESPONDENT in early 2015 in the Courts of Mediterraneo. CLAIMANT has been successful in both actions but each time no reimbursement of costs was ordered as according to the procedural law of Mediterraneo each party has to bear its own cost.

CLAIMANT has incurred costs in the amount of USD 50.280 [Exhibit C 11] for both actions which it now wants to recover as damages under Art. 74 CISG. The main difference between both

claims is that in the first action, i.e. the request for interim relief, the legal costs are associated with a breach of the delivery obligation in the main contract while in the second case, an alleged breach of the arbitration agreement forms the basis for the damage claim.

2. Cost incurred in the proceedings for interim relief

a) General applicability of Article 74 to legal costs

Whether parties may recover attorney fees incurred in legal proceedings and which are not reimbursed under the applicable procedural law as damages for a breach of contract pursuant to Art. 74 CISG is highly controversial.

In *Zapata Hermanos v. Hearthside Baking*, the Court of Appeal for the 7th Circuit in the US considered such legal fees not to be recoverable “losses” under Art. 74 CISG. The court’s decision was based on the following arguments which have received wide support in legal writing. First, the court considered the recoverability of attorney fees in proceedings to be a question of procedural law outside the realm of the CISG. The court found no support in the drafting history of the Convention that “loss” in Art. 74 CISG was intended to cover attorneys’ fees, which are not “expressly settled” in the CISG. Second, the recoverability under Art. 74 CISG would produce anomalies in so far that it would favor winning claimants over winning respondents. The former would always be reimbursed as a breach of contract as a prerequisite for a damage claim is established. By contrast, winning respondents would generally not be reimbursed as the rejection of a claimant’s case does not prove a breach of contract by the Claimant which could be the basis of a damage claim. Additionally, it is argued that the causal link between attorney fees and breach is too remote that they could qualify as damages under Art. 74 CISG.

The opposite view (see e.g. Piltz, *Litigation Costs as Reimbursable Damages*, pp. 286 – 294, in DiMatteo, *International Sales Law – A global challenge*, CUP 2014) relies on the wording of Art. 74 CISG and the underlying principle of full compensation. Its supporters argue that Art. 74 CISG does not explicitly exclude attorney fees or other expenses having their cause in legal proceedings and that compensation would not be full if such losses were not covered. In their view the procedure-substance distinction under domestic law has no relevance for the application of the CISG as the latter does not adhere to that distinction but contains itself rules of a procedural nature such as Art. 11 CISG. Nor do they consider eventual asymmetries between claimants and respondents to be sufficiently problematic to override the plain wording of Art. 74 CISG. They point out that in actions for a declaration of non-liability successful claimants could probably not recover their legal fees as damages while successful respondents could do so. Furthermore, the inclusion of legal fees into the scope of Art. 74 CISG is also justified by the objective of the CISG to harmonize the law applicable to international trade. That requires an extensive interpretation of the CISG in particular in area where the national rules differ, as is the case concerning attorney fees.

b) Foreseeability and other concerns

An additional problem which arises in this connection is the foreseeability of the damages. In general, RESPONDENT bottles the wine of a particular vintage only in April/May of the following year. Thus, in December, a sale and delivery to other customers was not imminent. It is questionable whether RESPONDENT could foresee at the time of contracting that CLAIMANT would seek interim relief in December.

At the same time, certainty about the delivery of the wine is crucial for CLAIMANT’s business model which is based on the reputation of being a particularly reliable source of supply.

CLAIMANT has created a “Collectors Club” and an elaborate system of pre-ordering, in which it basically guarantees delivery, subject to force majeure conditions (PO 2 para. 6). Thus, it is for CLAIMANT of considerable importance to be able to protect itself and take the necessary steps to ensure that it can deliver the wine ordered to its customers.

The second issue which creates concerns as to the foreseeability of damages is the agreement on contingency fees. The contingency fee agreed was reasonable under ordinary circumstances but in the case at hand less time than anticipated was spent (PO 2 para. 39). The amount claimed was correctly calculated and paid by CLAIMANT (PO 2 para. 41). Contingency fees are allowed in Danubia and are even fairly common in Mediterraneo, RESPONDENT’s country of origin. RESPONDENT itself is familiar with such fees and has tried to enter into such an agreement in at least one dispute albeit unsuccessfully (PO 2 para. 42). By contrast, contingency fee agreements are prohibited in Equatoriana, where CLAIMANT is based (PO 2 para. 40). Whether contingency fees were foreseeable in such circumstances is debatable. Issues which could play a role in this discussion are inter alia the size of CLAIMANT and the market structure.

A related but separate issue is whether the Contingent Fee Arrangement is not a contract to the detriment of RESPONDENT, in so far that CLAIMANT promised its lawyers a success fee. This fee had led in the present case to expenses which were far beyond those which would have been incurred if the full hourly rates would have been paid.

The timing of the request for interim relief as well as the agreement of contingency fees may also raise questions as to whether CLAIMANT complied with its obligation to mitigate the damages under Art. 77 CISG. In the discussion the same factors (e.g. time of bottling / structure of business) would be relevant.

Last but not least one can raise the question whether the decision by the Court in Mediterraneo that each party bears its own cost does not have res iudicata effect or a comparable effect settling the question of costs for the proceedings between the parties. At least on the basis of a narrow understanding of the concept reliance on res iudicata is doubtful as the court decision concerned a claim under procedural law while CLAIMANT tries to invoke a claim under substantive law. In light of the different understandings of res iudicata in the various jurisdictions and the existence of related and perhaps broader doctrines in some countries, the opposite argument can well be made in case it is properly reasoned.

3. Cost incurred in the proceedings for a declaration of non-liability.

The claim for a reimbursement of the legal costs incurred in the proceedings for a declaration of non-liability is encountering the same problem in relation to the general recoverability of attorney costs under Art. 74 CISG.

Additionally, it has to be discussed whether the initiation of the proceedings constitute a breach of the arbitration agreement and whether RESPONDENT can invoke Articles 80 or 77 CISG due to CLAIMANT’s refusal to cooperate in sorting out the problems resulting from the “pathological arbitration clause”. Both issues are arbitration related problems and will be discussed under the next heading.

Arbitration Questions:

I. Order for Document Production: Procedural Order No 1 para. 5(1a)

1. Background

RESPONDENT failed to deliver 5.500 bottles of wine due under the contract to CLAIMANT and at the same time sold an equal number of bottles to SuperWines. As the bottles were sold with a premium above the price charged to CLAIMANT, RESPONDENT made an additional profit which CLAIMANT asks for with its action. While it is uncontested that a premium was paid, its exact amount is not known (PO 2 para. 24). For that reason CLAIMANT has requested the Tribunal to order RESPONDENT to “provide to CLAIMANT all documents from the period of 1 January 2014 – 14 July 2015 pertaining to ... the purchase of diamond Mata Weltin 2014... “.

In the present case, the Parties come from jurisdictions which have different approaches to document production and have in their arbitration clause a provision which can be interpreted as pertaining to the issue of document production.

2. Document production

According to the Danubian Arbitration law, which is a verbatim adoption of the Model Law, the Arbitral Tribunal is in principle free in determining the conduct of the arbitration, including the taking of evidence, unless there is an agreement by the Parties providing for a particular procedure. The applicable Vienna Rules contain in Articles 28 and 29 largely identical provisions.

In the present case, the arbitration clause in Art. 20 of the Framework Agreement contains a number of elements that could be used by both parties in favour of their respective position. It states *inter alia* that all “disputes shall be settled amicably and in good faith between the parties” or if no agreement can be reached, “in accordance with international practice”. In the most pertinent part it states that the “proceedings shall be conducted in a fast and cost efficient way and the parties agree that no discovery shall be allowed”[[Exhibit C 1](#)].

The clause had been taken over from the brother of CLAIMANT’s COO Mr Friedensreich. That brother was the head of dispute resolution of a multinational company and had included the relevant part relating to “discovery” as a consequence of a multimillion court case with extensive pre-trial discovery in the US courts. During the discussions of the Framework Agreement Mr Weinbauer explicitly welcomed the clause in light of an own bad experience in the courts of Mediterraneo [[Exhibits C 12, R 1](#)] where a broad request was finally defeated as in Mediterraneo production of documents is only available in narrow circumstances and for specific documents.

RESPONDENT interprets the part which excludes “discovery” to constitute an agreement by the parties excluding production of documents. CLAIMANT by contrast considers it to extend only to very wide discovery proceedings in the American style. The question is first one of construction of the arbitration clause, which is not completely clear in this respect. Since the parties have explicitly agreed that the arbitration clause is governed by the CISG the interpretation of the arbitration clause would have to be made on the basis of Art. 8 CISG. Consequently, first the parties’ actual intent has to be established (Art. 8 (1)) and – in case such intent was not known to the other party which was also not required to know it – how a reasonable third party would have understood the provision.

Circumstances which might be relevant in interpreting the clause are *inter alia*

- the origin of the clause,
- comments upon its inclusion,
- the legal situation in both parties’ home jurisdictions,
- the remaining wording of the clause itself (“in accordance with international practice” – “fast and cost efficient way”), and
- the validity of the clause.

Both parties further allege that the position of the other party and the interpretation of the arbitration clause suggested by that party would violate fundamental principles of arbitration law. CLAIMANT alleges that if the clause were to provide for an exclusion of document production that should be regarded by the Tribunal as violating CLAIMANT's right to be heard.

RESPONDENT by contrast argues that granting disclosure would violate the principle of equality favouring CLAIMANT which comes from a jurisdiction allowing for document production and which could therefore rely on privileges. Furthermore, RESPONDENT alleges that any grant of document production would conflict with the system of burden of proof established under the CISG.

In addition, RESPONDENT argues that the documents requested are not relevant for the case and its outcome. The Parties have not explicitly agreed on the application of the IBA Rules on the Taking of Evidence in International Arbitration. They have, however, provided that disputes shall be resolved "in accordance with international practice". Thus, one may well argue that the standards provided for in Articles 3 and 9 of the IBA Rules should be guiding the Tribunal in determining whether it should grant the request for document production or not, in case the Parties have not generally excluded such powers.

The documents requested are necessary to establish the profits made by RESPONDENT. Such profits are primarily relevant if the CISG allows for a disgorgement of profits which is, however, contested by RESPONDENT.

The other factors which the tribunal should take into account when making the order are, pursuant to Art. 9 (2) IBA-Rules, the existence of privileges, the burden imposed upon RESPONDENT, the need for confidentiality and considerations of procedural economy. They may be discussed but should in themselves present no major obstacles to granting the order. The greatest relevance has in this context the potentially sensitive nature of the information requested – i.e. RESPONDENT's pricing policy towards its different customers.

II. Breach of the arbitration agreement: Procedural Order No 1 para. 5(1bii)

The second arbitration related issue concerns the question whether the arbitration agreement, beyond allocating jurisdiction, is also the source of additional contractual duties for the parties, the breach of which may result in damage claims or constitute a defence against such claims. In the present case, two obligations are invoked by the parties.

CLAIMANT relies upon a duty by RESPONDENT to seek dispute resolution only by arbitration which the latter has breached by initiating court proceedings for a declaration of non-liability in the High Court of Capital City. There is considerable support for the existence of such a duty in international arbitration, though it is by no means uncontested. Antisuit injunctions, for example, ordering a party to refrain from starting or continuing court proceedings in light of the existence of an arbitration agreement, are often based on such a duty.

The second question which could arise in this context is whether the breach of such a duty would give rise to a claim for damages. As correctly stated in RESPONDENT's Answer to the Statement of Claim paras 37 seq. the UNCITRAL Model Law does not contain any provision providing for damages for a breach of the arbitration agreement. In Procedural Order No 1 para. 5 (3) the Parties had agreed that the arbitration clause is "governed in principle by the CISG, if no special procedural rules apply to the arbitration clause". The formulation is deliberately vague. With few exceptions, if any, teams will argue that the question of breach of the duty and the existing remedies for that is governed by the CISG, i.e. Articles 45 and 74 CISG. In light of the vague

formulation teams are, however, not prevented from arguing that the UNCITRAL Model Law contains “special procedural rules” for the breach of an arbitration agreement (Art. 8 referral to arbitration) so that the CISG rules on damages are not applicable.

In case the CISG is argued, CLAIMANT’s damage claim is only successful under two conditions: first, if legal costs incurred in court proceedings can constitute damages in the sense of Art. 74 CISG at all (see below); second, if CLAIMANT is not precluded by Articles 77 or 80 CISG.

The latter issue relates to the second contractual duty arising from the arbitration agreement which is relied upon in the case and the existence of which is highly controversial. RESPONDENT invokes a duty of CLAIMANT to co-operate in resolving uncertainties which result from the unclear content of the arbitration agreement. The latter is clearly pathological as its wording refers to a non-existing institution, i.e. the “International Arbitration Tribunal (VIAC)”. RESPONDENT tried to resolve this uncertainty before initiating the proceedings in the High Court of Capital City. In its letter of 14 January 2015 [[Exhibit R 2](#)], RESPONDENT announced its intention to start legal proceedings and explained why it considered the arbitration clause in its present form to be void for uncertainty. In addition, RESPONDENT offered to enter into an unequivocal arbitration clause on the basis of the VIAC Model clause, should CLAIMANT consider the clause to be valid. RESPONDENT had furthermore indicated that, if no agreement could be reached on a new clause, it would start court proceedings in the High Court of Capital City, which had been selected by CLAIMANT for its request for interim relief. CLAIMANT did not reply at all to this letter which RESPONDENT considered to be a breach of a duty to co-operate arising from the arbitration agreement.

The assumption of any duty to co-operate has to overcome objections resulting from the adversarial nature of arbitration. In principle, in all types of adversarial legal proceedings parties are entitled to pursue their position as effective as possible. Also in the arbitration context courts have held that there is usually no obligation to support the other party in its case. The file contains a number of facts which could be raised in the context of the discussion whether in the present case, there is at least a limited duty for the CLAIMANT to co-operate. The most important one is naturally the wording of the arbitration clause which states that the disputes are to be “settled amicably and in good faith between the parties” and that the “proceedings shall be conducted in a fast and cost efficient way”.