THE INTERNATIONAL ADR MOOTING COMPETITION

HONGKONG 2013

MEMORANDUM FOR RESPONDENT

TEAM NO. 739R

In The Matter Of:

ENERGY PRO. INC. V. CFX LTD.

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LIST OF ABBREVIATIONS

¶	Paragraph
CIETAC	China International Economic and Trade Arbitration Commission
CLAIMANT	Energy Pro. Inc.
RESPONDENT	CFX Ltd.
p.	*Pagina* (Page)
pp.	*Paginae* (Pages)
v.	*versus*
Art.	Article
UPICC	UNIDROIT Principles of International Commercial Contracts
CISG	United Nations Convention on Contracts for the International Sale of Goods

INDEX OF AUTHORITIES

BOOKS, ESSAYS, ARTICLES

Rovine, Arthur, W.	*Contemporary Issues in International Arbitration and Mediation*, Martinus Nijhoff (2012) *Cited as: Rovine*	**1**
Sanders, P.	Commentary on the UNCITRAL Arbitration Rules, IInd Ybk Commercial Arbitration (1977) *Cited as: Sanders*	**4**
Schlechtreim P.H.; Schwenzer I	Commentary on the UN Convention on the International Sale of Goods, Oxford University Press, 3rd edn. (New York: 2010) *Cited as: Schlechtriem / Schwenzer*	**8**
W. Craig, W.Park & J. Paulsson	International Chamber of Commerce Arbitration, (3rd ed. 2000) *Cited as: Craig/Park/Paulsson*	**2**
Bartolotti, Fabio	Drafting & Negotiating International Commercial Contracts: A Practical Guide, ICC Publication No. 671 (2008) *Cited as: Bartolotti*	**12**

CASES

Cited as: Laker v. FLS

LEGAL INSTRUMENTS

ARGUMENTS ADVANCED

I. FUTURE ENERGY CANNOT BE MADE A PARTY TO THIS ARBITRATION

1. Arbitration is a consensual process, based on a contract between or among parties that often confers on each of them a right to participate in selecting the arbitrators. These realities greatly complicate the task of facilitating joinder in arbitration, where limitations of contractual privity, principles of party autonomy and particular questions of procedural fairness must be addressed. [*Rovine, p.105*]

A. Voluntary Participation Is Fundamental To The Procedure Of Arbitration

2. In arbitration only those who are parties to the arbitration agreement expressed in writing could appear in the arbitral proceedings either as claimant or as defendants. [*Art. II, NY Convention*]

(I) ABSENCE OF FREE WILL

3. The arbitration agreement under consideration, only involves consent of the CLAIMANT and RESPONDENT to arbitrate disputes arising from the Purchase Contract signed between them. In settling disputes through arbitration, an agreement to engage in arbitration should first of all be reached by parties concerned upon free will. [*Art.4, Chinese Arb Law, 1994*].

4. There is no evidence of the CLAIMANT having obtained the consent of Future Energy to join the arbitration proceedings. In either case, any consent obtained by them would not be free consent since they have attempted to coerce Future Energy by threat of litigation. [*CLAIMANT's Exhibit 9*]

(II) LACK OF CONSENT OF ALL SIGNATORIES TO THE ARBITRATION AGREEMENT

5. Although the non-signatory's intent is often most controversial, the intention of other parties to be bound by the agreement to arbitrate with the non-signatory is also necessary. The requirement for both parties' consent is implicit in both international conventions and national law. [*Craig/Park/Paulsson, ¶5.09*]

6. Not only is free consent of Future Energy absent, the RESPONDENT is also against the joinder of a non-signatory to the proceedings. For the most part, authorities agreed that consent is usually the essential foundation for ascertaining whether a particular entity is a party to an arbitration. Whatever legal construct is utilized, the beginning and ending question is ordinarily, whether the parties, with their actions considered objectively and on the bases of commercial good faith, intended that a particular entity be a party to the arbitration clause. [*Born, p. 1205*]

B. <u>There is no arbitration agreement between Future Energy and the CLAIMANT.</u>

(I) ABSENCE OF AGREEMENT TO ARBITRATE

7. The fact that a "non-signatory" might be bound to arbitrate does not dispense with the need for an arbitration agreement. Rather, it means only that the agreement takes its binding force through some circumstance other than the formality of signature. The legal framework for normal commercial arbitration (whether statute, treaty, or institutional rules) continues to require some assent to arbitrate, whether express, implied or incorporated by reference to other documents or transactions. [*Park, ¶ 1.28*] No such agreement exists, whether written or otherwise, between Future Energy and CLAIMANT.

8. Arbitration is a matter of consent and, in particular, consent to arbitrate particular disputes with particular counter-parties, not consent to arbitrate generally or with the entire world. Arbitration is a consensual means of dispute resolution, between specified parties, and there is no justification for assuming that signatories to an agreement to arbitrate with particular counter parties intended to arbitrate with other, non-parties. [*Born, p. 1141*]

(II) ROLE OF FUTURE ENERGY IN PERFORMANCE OF THE CONTRACT DOES NOT AMOUNT TO CONSENT TO ARBITRATE

9. Future Energy merely had to certify the manufactured goods. [*Clarification 13*] Tribunals have held that a company's awareness of a contract (including an arbitration clause) between other parties, and its confirmation of one aspect of the underlying contract, does not necessarily make the company a party to the arbitration clause. [*Born, p. 1151*]

10. Role of non-signatories in negotiation and performance of contract was insufficient to warrant conclusion they had assumed contract. [*ICC Case No. 4504*] In general, merely incidental involvement in contractual performance has fairly consistently been held insufficient to constitute consent to the underlying contract. [*Born, p. 1152*]

II. MS. ARBITRATOR 1 CANNOT RESIGN DURING THE ARBITRATION PROCEEDINGS.

A. It is an obligation of the arbitrator to complete his mandate.

11. Whether or not express provisions dealing with the subject exist, an arbitrator's acceptance of his or her appointment entails an implied undertaking to complete that mandate, by issuing a final award (unless the parties otherwise resolve the dispute or the arbitration agreement is declared invalid or inapplicable.) [*Born, p. 1635*] The CIETAC Rules do not give any indication as to specific grounds or circumstances in which a resignation may be justified. Once the arbitrator has agreed to function, he should fulfil his task. [*Sanders, pp. 172,191*]

12. The arbitrators are required to pursue their functions until their conclusion or, in other words, until the final award is made. [*Gaillard/ Goldman/ Savage, p.* 611] Ms. Arbitrator 1 will be breaching her obligation if she resigns before making the final award.

B. Resignation of Ms. Arbitrator 1 and appointment of new arbitrator will cause inordinate delay and loss of money

(I) RESIGNATION OF MS. ARBITRATOR 1 IS DILATORY.

13. The resignation of Ms. Arbitrator 1 is a dilatory one. Appointing a new arbitrator may be impractical when the resignation, or refusal to participate, occurs late in the arbitral proceedings. The situation is particularly aggravated if the arbitrator chooses to resign, or refuses to participate, at the stage of the tribunal's deliberations. [*Redfern/ Hunter, ¶ 4-73*]

(II) ADDITIONAL DAMAGE MIGHT BE ACCRUED IF PROCEEDINGS ARE REPEATED WITH THE ENTRY OF A NEW ARBITRATOR.

14. Any premature termination of the arbitrator's mandate could have serious repercussions on the arbitration and lead to considerable losses of time and money. Finding and appointing a replacement, and allowing the new arbitrator to familiarise himself with the case, inevitably causes delay. Proceedings may have to be repeated and the delay involved in that may lead to additional damages. [*Lew/ Mistelis / Kroll, p. 281, ¶ 12-15; Laker v. FLS*]

(III) MS. ARBITRATOR 1 WILL BE A BETTER JUDGE FOR THE ISSUE OF QUANTUM THAN A NEW ARBITRATOR.

15. She will be in the best position to arbitrate on the issue of quantum because she will be present in the oral hearings and will hear both parties as well as be well-aware about the facts. It will take the new arbitrator more time to accustom himself with the facts of the case and will add to the delay.

C. CLAIMANT must pay Ms. Arbitrator 1 additional fees for the extra three days.

16. CLAIMANT believes that extension of hearings for three days is no justification to pay her more once an agreement has been reached. [*Clarification 10*] This violates Ms. Arbitrator 1's right to remuneration for the services that she will be rendering for the next three days.

17. The principle right of an arbitrator, in return for his obligations, is to receive payment. In the absence of an agreement to the contrary, the arbitrator is entitled to receive fees and be reimbursed for his expenses. This principle seems unquestioned. [*Poudret/Lesson, p. 371*]

18. Even where national law or institutional rules do not expressly provide for a right of remuneration, it is indisputable that an arbitrator is entitled to financial compensation for his or her services: this is an obvious consequence of the contractual relationship between the parties and the arbitrator, as well as customary practice and expectations in international arbitration. [*ICC Bulletin p. 27*]

D. ASSUMING BUT NOT CONCEDING that Ms. Arbitrator 1 can resign, the proceedings should continue with a truncated tribunal.

19. As mentioned above, it is felt that appointing a new arbitrator will lead to inordinate delay and will not help in any way. It is felt that the proceedings should continue in the form of a truncated tribunal without appointing a new arbitrator, if Ms. Arbitrator 1 resigns.

20. After consulting with the parties and upon the approval of the Chairman of CIETAC, the other two arbitrators may also continue the arbitration proceedings and make decisions, rulings, or render the award. [*CIETAC Rules, Art. 32*]

III. CLAIMANT DID NOT TERMINATE THE CONTRACT VALIDLY.

A. RESPONDENT wasn't under any obligation to purchase the gearboxes and hence make payments.

(I) CLAIMANT FAILED TO PERFORM ITS OBLIGATIONS

21. CLAIMANT has not upheld its contractual obligations as per clauses 10.1 and 10.2 **[***CLAIMANT's Exhibit 2***]** in the Purchase Contract. CLAIMANT has not met the requirements under clause A of the Purchase Contract as per which it had to deliver gearboxes conforming to Model No. GJ 2635. It had a duty to achieve this as per Art 5.1.4, UPICC. However, the fit certificate was erroneously granted by Future Energy for gearboxes of model GH 2635. Hence, CLAIMANT failed to perform its obligations under both clauses.

(II) RIGHT TO WITHHOLD PERFORMANCE.

22. RESPONDENT's non-payment cannot constitute a breach as it is entitled to seek replacement of defective performance [*UPICC, Art. 7.2.3*]. The non-performance of CLAIMANT gives RESPONDENT a right to withhold performance of its own reciprocal obligations. [*UPICC, Art. 7.1.5(2)*]

B. RESPONDENT's failure to pay the second and third instalments cannot be relied upon by CLAIMANT.

23. The non-payment of the second and third instalments by RESPONDENT does not amount to fundamental non-performance giving CLAIMANT the right to terminate the contract. RESPONDENT had to abstain from paying because it was supplied with non-

conforming goods. RESPONDENT's act of not paying was due to CLAIMANT's non-performance and CLAIMANT cannot rely on the same to terminate the contract.

(I) GOODS DELIVERED TO RESPONDENT WERE NON-CONFORMING AND HENCE CLAIMANT IS LIABLE.

(a) Seller responsible for non-conformity.

24. Art. 36(1), CISG makes the seller liable for non-conformity. To find out whether the goods meet requirement of the contract, the primary test as per CISG, Art. 35(1) is what characteristics of goods are laid down in the contract by means of qualitative and quantitative descriptions. [*Schlechtriem / Schwenzer p. 571*] These are laid down in Clause A of the Purchase Contract [*Claimant's Exhibit 2*]. Any discrepancy in quality, regardless of whether the quality is better or worse than that stipulated under the contract represents a lack of conformity. [*Schlechtriem / Schwenzer p. 573]*

25. In the *Hammer mill case*, equipment delivered to the Buyer did not meet technical specifications of the agreement and the CIETAC Arbitral Tribunal gave an award in favour of buyer and the seller was made to provide substitute goods complying with the requirements of the contract. In the *PTA case*, the Seller was held liable for delivering non-conforming goods under Art. 35, CISG.

26. Since the goods were not of exact specifications mentioned in Clause A of Purchase Contract, they are of no use to RESPONDENT and CLAIMANT is liable to perform its obligations including replacement of defective performance which is RESPONDENT's right. [*UPICC, Art. 7.2.3*]

(b) Seller liable for third party's non-performance.

27. The defaulting party will be exempt from liability *only if* the non-performance of third party suits the condition mentioned in Art. 79(1) of UPICC, i.e. non-performance is due to an impediment beyond that party's control. [*Art. 79(2), CISG*] Since this is not the case, CLAIMANT is also liable for acts of the third party i.e. Future Energy.

28. Pursuant to this article, CLAIMANT will be liable for not performing its obligations under the contract. Consequently, RESPONDENT had the right to suspend the contract since it received faulty gearboxes and was not obligated to purchase from CLAIMANT. No material obligation was breached.

(II) RESPONDENT'S NON-PAYMENT RESULTED OUT OF CLAIMANT'S NON-PERFORMANCE.

29. A party may not rely on the non-performance of the other party to the extent that such non-performance was caused by the first party's act or omission or by another event for which the first party bears the risk. [*UPICC, Art. 7.1.2*] [*ICC 09/10*]

30. Art. 7.1.2, UPICC is based on the principle *Exceptio Non Adimpleti Contractus*, meaning "an exception in a contract action involving mutual duties or obligations, to the effect that the plaintiff may not sue if the plaintiffs own obligations have not been performed." There is a causal link between the act of CLAIMANT and RESPONDENT. CLAIMANT failed to supply goods in conformity with the contract due to which RESPONDENT did not pay the second and third instalments because it was not in its best interest to make advance payments for a non-conforming product. RESPONDENT has merely exercised its right as a buyer and thus CLAIMANT cannot terminate the contract for the non-payment of the instalments as it committed the non-performance.

IV. CLAIMANT CANNOT CLAIM TERMINATION PENALTY

A. CLAIMANT cannot claim termination penalty because of invalid termination.

31. As proved above in Issue 3, CLAIMANT. did not terminate the contract as provided in Clause 15.1 of the Purchase Contract. Hence, it cannot claim the termination penalty according to Clause 15.2 of the Purchase Contract.

B. ASSUMING BUT NOT CONCEDING, that Termination of the Contract is valid, RESPONDENT is still not liable to pay termination penalty

(I) AGAINST THE SPIRIT OF GOOD FAITH

32. Clause 15 of the Purchase Contract is against the spirit of good faith and fair dealing as given in UPICC, Art. 1.7. CLAIMANT is violating this principle by demanding from RESPONDENT a penalty of 8 million when in fact it has delivered gearboxes worth only 2 million which were non-conforming goods.

33. The present termination clause should be held to fall under the category of exemption clauses as per UPICC, Art. 7.1.6 and should not be invoked because it would be grossly unfair to do so and its execution will be manifestly inequitable. [*Seguros v. Transportadora*]

34. Terms regulating the consequences of non-performance are in principle valid but the court may ignore clauses which are grossly unfair. [*UPICC Commentary p. 233*] Exemption from liability for non-performance or other forms of relief are therefore excluded under the UNIDROIT Principles if the Party claiming it was "in control" of the situation or if it would be "grossly unfair" to allow for such exemption. [*El Paso*]

(II) INVALIDITY OF THE TERMINATION CLAUSE

35. The termination clause between the parties gives the right to suspend or terminate the Purchase Contract exclusively to CLAIMANT. The same right is not available to RESPONDENT in case of CLAIMANT's non-performance. There is also no relief mentioned in Clause 15 for RESPONDENT but only for CLAIMANT when it terminates the contract. Majority of contractual terms were proposed, adopted and drafted by CLAIMANT itself and RESPONDENT went along with it as CLAIMANT was a powerhouse in the energy sector in Cyrus and RESPONDENT acted in good faith.

36. If the contract unfairly burdens one party more than the other, courts and arbitrators refuse to enforce such provisions. Furthermore, in case of dispute, contracts are typically interpreted against the party who drafted the contract considering that it had the opportunity to phrase the terms and conditions definitively. [*Bartolotti*]

37. Moreover, the penalty granted to CLAIMANT is inequitable and grossly unfair as not only will RESPONDENT's payments made be forfeited, but RESPONDENT will have to pay further remainder of 8 million. Clause 15 of Purchase contract shows inequity and unfairness and should be struck down as invalid.

C. ASSUMING BUT NOT CONCEDING that the Termination clause is valid, the penalty payable by RESPONDENT must be reduced.

38. As any other means of protection, the guarantee of the fulfilment of an obligation shall correspond to the criteria of proportionality and conformability with the negative consequences of the breach of the obligations to the sum of the penalty claimed by the seller. [*Case No. 134*] The same approach is reflected in UPICC, Art. 7.4.13. Arbitral

Tribunals have exercised Article 7.4.13(2) to reduce the penalty to a reasonable amount where the penalty was excessive. [*Case No. 229, Case No. 88*]

39. The termination penalty should be reduced from 8 million to a reasonable amount the Tribunal sees fit as the amount in the penalty clause is grossly excessive compared to the actual harm suffered by CLAIMANT since they have supplied gearboxes worth only 2 million to RESPONDENT.

E. RESPONDENT is entitled to restitution of the 2 million dollars.

(I) RESTITUTION UPON TERMINATION OF CONTRACT.

40. Under general principles of law, upon termination of the contract either party may claim restitution of whatever it has supplied, provided that such party concurrently makes restitution of whatever it has received. Thus, restitution necessarily entails that both parties return what they have received under the contract. [*Case No. 9797*]

(II) UPICC, ART. 7.3.6 IS APPLICABLE AND NOT ART. 7.3.7

41. Under UPICC, Art. 7.3.6 deals with restitution with respect to contracts to be performed at one time and Art. 7.3.7 with contracts to be performed over a period of time. In case of termination of a contract to be performed over a period of time, the parts already performed should not be affected by the termination. [*Case No. C07*]

42. Article 7.3.6 is applicable, not Article 7.3.7. The reason for differentiating between the two articles is that performances under the contracts usually falling under 7.3.7 operated for a long period of time before being terminated and it was thus nearly impossible to unravel these performances [*UPICC Commentary, p. 263*]. However that is not the case presently as just one transaction took place between the parties which itself resulted in

non-performance. In *Case No. 7365*, the case concerned had two contracts for sale between the parties but the tribunal had applied Article 7.3.6 quoting it verbatim.

43. Hence, termination penalty cannot be rightfully claimed by CLAIMANT in either of the scenarios discussed above.

PRAYER

44. In light of the submissions made above, RESPONDENT respectfully requests Tribunal to declare that:

- Future Energy cannot be made a party to this arbitration;
- Ms. Arbitrator 1 cannot resign and CLAIMANT must pay her additional fees;
- CLAIMANT did not terminate the contract validly and cannot claim termination penalty; and
- CLAIMANT must return the first part payment of USD 2,000,000 to RESPONDENT.

Respectfully signed and submitted by counsel on June 21, 2013.