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Parties:

KEYWORDS

DISTRIBUTORSHIP AGREEMENT BETWEEN EUROPEAN COMPANY AND LATIN AMERICAN COMPANY - CHOICE OF LAW CLAUSE INEFFECTIVE BUT INDICATING PARTIES' DESIRE FOR A NEUTRAL SOLUTION - APPLICATION BY ARBITRAL TRIBUNAL OF THE LEX MERCATORIA (ARTICLE 17.1 ICC RULES OF ARBITRATION) - REFERENCE TO UNIDROIT PRINCIPLES - LIMITS

CONTRACT FORMATION - ACCEPTANCE CONTAINING MODIFIED TERMS - AMOUNTS TO ACCEPTANCE IF MODIFICATIONS ARE NOT MATERIAL (ARTICLE 2.11 [ART. 2.1.11 OF THE 2004 EDITION] UNIDROIT PRINCIPLES)

CONTRACT FORMATION - CONCLUSION OF CONTRACT DEPENDENT ON AGREEMENT ON SPECIFIC MATTERS (ARTICLE 2.13 [ART. 2.1.13 OF THE 2004 EDITION] UNIDROIT PRINCIPLES)

CONTRACT INTERPRETATION - TERMS TO BE GIVEN EFFECT (ARTICLE 4.5 UNIDROIT PRINCIPLES)

TERMINATION OF CONTRACT - FUNDAMENTAL BREACH REQUIRED (ARTICLE 7.3.1(1) UNIDROIT PRINCIPLES) - NOTICE OF TERMINATION WITHOUT FUNDAMENTAL BREACH - TERMINATION NEVERTHELESS EFFECTIVE (ARTICLE 7.3.2 UNIDROIT PRINCIPLES) - NOTIFYING PARTY LIABLE FOR DAMAGES

DAMAGES - LOSS OF PROFIT - CALCULATION (ARTICLE 7.4.2 UNIDROIT PRINCIPLES)

DAMAGES - DISCRETIONARY ASSESSMENT BY COURT (ARTICLE 7.4.3(2))

ABSTRACT

Defendant, a European manufacturer, and Plaintiff, a Latin-American distributor, entered into an agreement (hereinafter "the Agreement") for the exclusive distribution of Defendant's products in Plaintiff's country. Although the Agreement provided that payment of the price of the goods was due 120 days after delivery, Defendant, after receiving from Plaintiff an order for a larger than usual quantity of goods, requested advance payment. Plaintiff refused, and the parties entered into negotiations with a view to finding a mutually acceptable solution. Ultimately it was agreed that Plaintiff would pay the price in advance, but Defendant in turn would grant Plaintiff a discount corresponding to the additional costs thereby incurred by Plaintiff. While the parties still argued as to whether the new terms of payment concerned only future orders or applied also to the order already placed, Defendant all of a sudden terminated the Agreement alleging Plaintiff's failure to meet the contractually agreed sales figures over the last two years. Plaintiff objected that the termination was ineffective, first, because Defendant did not formally put Plaintiff into breach ("mise en demeure") and in any case notice of termination was not given timely; second, because the sales figures indicated in the Agreement were not binding commitments; and third, because its failure to meet the figures was due to Defendant's refusal to deliver the goods according to the originally agreed terms. Since Defendant insisted on the termination of the agreement, Plaintiff

commenced arbitration proceedings, requesting the arbitral tribunal to declare the termination of the Agreement ineffective and to compel Defendant properly to perform the Agreement until its expiry.

The first question addressed by the arbitral tribunal was whether it had jurisdiction in the case at hand. In deciding in the affirmative, the arbitral tribunal, while conceding that the language of the clause of the Agreement entitled “Fuero Competente” was rather ambiguous, pointed out that the drafters of that clause were not lawyers and could therefore not be expected to use proper legal terminology; what was important was what reasonable persons in the same situation as the parties would have understood by such language, and that the clause was being given a meaning which did not deprive it of any effect, and in this respect the arbitral tribunal expressly referred to Articles 4.1 and 4.5 of the UNIDROIT Principles, respectively.

As to the law applicable to the substance of the dispute, the arbitral tribunal held that, notwithstanding that the Agreement provided “El presente contrato [...] se regirá [...] por la CAMARA DE COMERCIO INTERNACIONAL o en su defecto por una legislación neutral definida en comun acuerdo por las partes”, the parties had not made any valid choice of the applicable law, since there is no ICC legislation nor did the parties agree on the application of any other neutral legislation. As a consequence the arbitral tribunal, in view of the fact that the parties apparently wanted a neutral solution, decided to apply “general principles and rules of international contracts, i.e. the so-called *lex mercatoria*”, and to refer in this context to the UNIDROIT Principles representing - with some exceptions such as the provisions on hardship – “a restatement of the rules which business persons engaged in international trade consider to be meet their needs and expectations”.

Concerning the merits of the case, the arbitral tribunal, invoking the principle of *pacta sunt servanda* laid down in Article 1.3 of the UNIDROIT Principles, first of all held that Defendant’s refusal to deliver the goods on the originally agreed terms of payment constituted a breach of the Agreement, but that this breach was no longer relevant because the parties had reached a settlement agreement. Indeed, the valid conclusion of this agreement was not prevented by the fact that Defendant’s letter of acceptance of Plaintiff’s proposed terms of settlement contained some minor modifications, and that another issue of minor importance had been left open by the parties, and in support to its findings the arbitral tribunal referred to Articles 2.11 and 2.13 [Arts. 2.1.11 and 2.1.13 of the 2004 edition] of the UNIDROIT Principles, respectively. Turning to the question as to whether the subsequent termination of the Agreement by Defendant was effective, the arbitral tribunal, referring to Article 7.3.2(1) of the UNIDROIT Principles according to which the right to terminate the contract is exercised by notice without any further formality, rejected Plaintiff’s argument that Defendant before terminating the Agreement should have put Plaintiff formally into breach. At the same time, however, the arbitral tribunal held that Defendant’s notice of termination had not been given timely and, more importantly, that it was not justified since in view of the non binding nature of the sales figures laid down in the Agreement Plaintiff’s failure to meet the figures could not be considered a fundamental breach of the Agreement, and in support of its findings it referred to Articles 7.3.2(2) and 7.3.1(1) of the UNIDROIT Principles, respectively. Yet this did not mean that, as asserted by Plaintiff, the Agreement was still in force: according to a rule widely accepted in international trade and in the view of the arbitral tribunal also confirmed by the UNIDROIT Principles (see in particular Articles 7.3.2(1) and 7.3.5(1)), a notice of termination is effective even if unjustified with the result that the other party may not require specific performance of the contract but can only claim damages for the unjustified termination. In the case at hand, Defendant, having terminated the Agreement without justification, has to compensate the loss thereby caused to Plaintiff. As to Plaintiff’s lost profit, the arbitral tribunal held that it should be calculated not on the basis of the gross margin of the forecast sales volumes but on the basis of the net margin, i.e. the difference between the gross margin and the avoided costs or harm, and in this respect referred to Article 7.4.2 of the UNIDROIT Principles. However, since Plaintiff has not provided any information for the calculation of the net margin, in the case at hand the arbitral tribunal made an equitable quantification of the lost profit in accordance with Article 7.4.3(3) of the UNIDROIT Principles.

FULL TEXT

[...]

1. THE ANTECEDENTS OF THE DISPUTE

[...]

The Defendant [a European company] and the Plaintiff [a South American company] [...] concluded in [...] two exclusive distribution contracts (hereinafter “the Contracts”) for the resale of the goods manufactured by the Defendant in the Plaintiff’s country [...].

[...]

In its letter of [...] the Defendant informed the Plaintiff that it had been purchased by Group [X] and entrusted “... the management, the follow-up and the control of [the contractual products]” in the territory of [territory comprising a number of countries including the Plaintiff’s country] to Company [Y], affiliate of the Group [X]. [...]

In the same period the Plaintiff transmitted to the Defendant two orders No. XXXX/98 and No. YYYY/98 for a total amount of US \$ 82.402 [...].

In its letter of [...] the Defendant, after having confirmed receipt of orders No. XXXX/98 and No. YYYY/98, confirmed its decision to entrust the marketing of its products to Company Y and added that:

“Given the large sums [the Plaintiff] owes to [a company of the Group X], [the Defendant] cannot execute your orders before receiving payment in advance.”

The Plaintiff opposed this request on the ground that Article 4.4 of the Contracts made provision for payment within 120 days of the date of dispatch and that an alleged debt with a third company could not justify a change in the conditions of payment [...].

[...]

In its letter of [...] the Defendant explained in more detail the reasons why it wished to obtain payment guarantees. [...] At the same time the Defendant proposed to negotiate a discount for immediate payment and/or compensation or a discount for the Plaintiff to take into consideration the costs it would sustain to guarantee payment by means of a letter of credit, a bank guarantee or any other form of guarantee.

The Plaintiff responded in a letter of [...]. While stressing that from a legal point of view it had a right to refuse the Defendant’s proposals, the Plaintiff agreed in principle to provide payment guarantees provided that the Defendant undertook to cover the costs of those payment guarantees [...].

The parties met on [...] to discuss the terms of an agreement. In the course of this meeting they reached an agreement in principle which the lawyers summarised in the following terms:

“In a purely commercial spirit, [the Plaintiff] agreed to pay you in advance for the goods indicated in its future orders [...] on condition that you undertake to cover the costs of payment in advance (the time limit within which payment was originally indicated in the Contracts was 120 days) and that the harm it suffered on account of the delay in deliveries be, at least in part compensated.”

[...]

In its letter of [...] the Defendant agreed to the Plaintiff’s proposals. [...]

Subsequently, in its letter of [...] the Plaintiff raised a new problem: in order to safeguard distribution in the Christmas period the Plaintiff asked the Defendant to send the goods by air and cover the costs of air transport. [...]

In a fax message of [...] the Defendant agreed to the Plaintiff’s latest proposal.

[...]

On [...] the Defendant asked the Plaintiff to inform it of details of sales of its products in the year [...], in the year [...] up until the month of October. The Plaintiff sent the information in question on [...].

On [...] the Defendant informed the Plaintiff [...] that, as it, the Plaintiff, had not reached the minimum sales stipulated in Article 11.4 of the Contracts for the years [...], it was notifying the Plaintiff that it was terminating the Contracts in advance according to Art. 10.1.3 (and, that is “por incumplimiento grave de alguna de sus cláusulas”) with effect as of [...]

[...]

In its letter of [...] the Plaintiff challenged the validity of the Defendant’s termination of the

Contracts. It stressed in particular that it was contrary to good faith to have been given notice of termination after the parties had concluded an agreement in principle on the conditions on which the goods would be supplied; that the Plaintiff, had undertaken no obligation to purchase a minimum quantity, since Art. 11.4 only mentioned a simple forecast of the quantity to be purchased [...] At the same time it ordered the Defendant to perform the contract and to deliver with no further delay the goods indicated in Orders No. XXXX/98 and No. YYYY/98 [...]. After a final fruitless exchange of letters the Plaintiff decided to submit the dispute to arbitration. [...]

2. THE PROCEEDINGS

[...]

3. THE QUESTIONS TO BE DECIDED

According to the Terms of Reference, the questions to be decided by the Arbitral Tribunal are the following:

1. Does the Arbitral Tribunal have jurisdiction?

If so:

2. What law is applicable to the merits of the dispute?

3. Are the parties' claims admissible and, if so, to what extent?

4. Are the counterclaims admissible and, if so, to what extent?

5. Should there be a set-off between the claim and the counterclaim?

6. Which party must pay the costs and the arbitrator's fees or, alternatively, how should the costs and fees be shared by the parties?

[...]

5. DOES THE ARBITRAL TRIBUNAL HAVE JURISDICTION ?

[...]

Article 12 of the Contracts contains the following clause:

"12. FUERO COMPETENTE

12.1. El presente contrato, así como todas sus disposiciones, se regirán en todos los sentidos por la " CÁMARA DE COMERCIO INTERNACIONAL " o en su defecto por una legislación neutral definida en común acuerdo por las partes, pero que en ningún caso podrán ser los Tribunales de Justicias de los respectivos países de las partes contratantes.

12.2 Todas las interpretaciones que se requieran de este contrato, así como los litigios que puedan surgir entre las partes contratantes, se someterán a los Jueces y Tribunales de las Cortes definidas en el punto 12.1 implicando con ello que ambas partes renuncian a otros fueros, si existieren."

[...]

According to the Plaintiff, the clause, entitled, after all, "Foro competente", is a jurisdiction clause and not a choice of law clause. The reference to the applicable law was probably due to a drafting error consisting in the use of the term "legislación neutral" instead of "jurisdicción neutral".

In such a context reference to the ICC could have no other meaning than the submission of possible disputes to ICC arbitration. This solution would also be justified by the need to prefer an interpretation capable of providing a useful outcome rather than an interpretation that would render the clause inoperative. [...]

Moreover, the express exclusion of the jurisdiction of the courts of the parties' respective countries contained in Article 12 would lead to an absurd result. Indeed, should the clause be denied the value of an ICC arbitration clause, the parties could not then bring the dispute before a court that would normally be competent/have jurisdiction in the absence of an arbitration clause (i.e. the courts of the countries of the two parties) as precisely this solution has been expressly excluded by the clause.

Lastly the Plaintiff claims that the Defendant itself had agreed to arbitration in its letter of 26 May 1999 in which it proposed the name of an arbitrator.

[...]

According to the Defendant, Article 12.1 was a choice of law clause. As it was not an arbitration

clause, it would not be possible to commence arbitration proceedings on the basis of it. As concerns Article 12.2 indicating jurisdiction by reference to Article 12.1, the Defendant claims that this provision is ineffective as it refers to a law that does not exist (that of the ICC) or a neutral law that, however, should have been specified (but in fact was not specified) by the parties.
[...]

5.4 The Arbitral Tribunal's Position

The provision contained in Article 12 must be interpreted by searching for the parties' common intention, without dwelling on the literal meaning of the words, on the basis of a widespread principle that has also been incorporated in Article 4.1 of the UNIDROIT Principles according to which "1. A contract shall be interpreted according to the common intention of the parties. 2. If such an intention cannot be established, the contract shall be interpreted according to the meaning that reasonable persons of the same kind as the parties would give to it in the same circumstances."

In applying this criterion it must be considered that the persons who drew up and negotiated the clause were not jurists and did not therefore have a clear idea of the meaning (from a legal point of view) of the concepts of competent forum, arbitration and applicable law. [...] In order to understand the meaning of the provision one would have to put oneself in the condition the parties were in (or that of a reasonable person of the same kind as the parties). The parties, not having had legal training, tend to confuse the concepts of applicable law and jurisdiction, their main concern being to put into effect the most neutral solution possible for the settlement of disputes that might arise.

Now, if one reads Article 12 in this perspective, the reference to International Chamber of Commerce, contained in Article 12.1, is to be understood in the first place as a clause aimed at establishing jurisdiction, and this is, after all, confirmed by the last part of the sentence which reads "... which can in no case be the courts of law of the contracting parties' respective countries". In other words, when the parties declare their intention to submit the contract to an applicable law (that of the ICC) other than that of the courts of their respective countries (placing law and jurisdiction on the same level), it is clear that they intend to refer to jurisdiction (that of the ICC) and therefore to ICC arbitration.

This appears to be further confirmed by the title of the article in question ("Competent Forum") as well as by that fact that Article 12.2 refers to the courts specified in Art. 12.1. This confirms that the parties intended the function of Article 12.1 to be the determination of jurisdiction. [...] In conclusion: if one looks at Art. 12 as a whole and seeks to identify its real meaning (beyond the technical meaning of the legal terms used), one sees that the parties' intention was to settle any disputes that might arise in a neutral way, having recourse to the International Chamber of Commerce which they considered an instrument well known to be suitable for that purpose. Consequently, if they intended to submit their disputes to the ICC, that can only mean that they intended to have recourse to arbitration, the ICC being universally well known as an arbitration institution and also considering that the parties had agreed on ICC arbitration in a previous contract.

This interpretation of Article 12 is moreover in conformity with the principle of all terms being given effect contained in Article 4.5 of the UNIDROIT Principles, according to which: "Contract terms shall be interpreted so as to give effect to all the terms rather than to deprive some of them of effect."

On the other hand if Article 12 were to be interpreted not as arbitration clause, the parties could not have recourse to either arbitration or to the domestic courts that would normally have jurisdiction (and namely those of the Defendant's country or of the place of performance of the Contracts) since their jurisdiction has been expressly excluded by the clause in question. This would deprive the parties of any possibility to act in the case of a dispute, unless the clause is considered in its entirety ineffective. [...]

Consequently the arbitral tribunal affirmed its jurisdiction to decide the dispute.

6. WHAT LAW IS APPLICABLE TO THE MERITS OF THE DISPUTE?

As concerns the applicable law, Article 12 of the Contracts makes reference to the ICC and to a “neutral legislation specified by mutual agreement by the parties”. In view of the fact that no ICC legislation exists and that the parties have not specified by mutual agreement a neutral law, it must be concluded that the parties have not expressly chosen the applicable law.

The Arbitral Tribunal will therefore have to determine the applicable law in conformity with the second sentence of Art. 17 (1) of the ICC Arbitration Rules according to which: “In the absence of an agreement between the parties the Arbitral Tribunal shall apply the rules of law it considers appropriate in the case at hand”.

The Arbitral Tribunal holds that, in order to determine the most appropriate rules of law, the fact that the parties wanted a neutral solution had to be taken into account.

Now, in the absence of an express indication as to the domestic law of a third country, the most appropriate solution in the case in which the parties express their desire for a neutral solution is to apply the general rules and principles of international contracts, the so-called *lex mercatoria*.

In this context, for questions concerning general contract law, reference can be made to the “UNIDROIT Principles of International Commercial Contracts” which represent – except for a few provisions (such as for example the provisions on hardship: see ICC Award N° 8873 of 1998, in *Journal droit int.*, 1998, p. 1017) – a “restatement” of the rules that parties engaged in international trade consider to be consonant with their interests and expectations. This has been recognised in numerous arbitral awards in which the UNIDROIT Principles have been applied as an expression of the *lex mercatoria* or of international trade usages: see for example ICC partial Award N° 7110, in *Bull. Arb. CCI*, 2/1999, pp 40-50; ICC Award N° 7375, in *Mealey's International Arbitration Report*, vol. 11/n° 12 (December 1996), pp. A1-A69; ICC Award N° 8502, in *Bull. Arb. CCI*, 2/1999, pp. 74-77.

The Tribunal will therefore apply the rules and principles generally recognised in international trade (*lex mercatoria*) and in particular the UNIDROIT Principles, to the extent that they represent rules recognised by international business people as being applicable to international contracts.

7. ARE THE PARTIES' CLAIMS AND COUNTERCLAIMS ADMISSIBLE AND, IF SO, TO WHAT EXTENT?

[...]

The Plaintiff reproached the Defendant for not having performed the Contracts (by refusing to supply the contractual products in the absence of the Plaintiff's acceptance of the contractual modifications the Defendant wanted to impose) and for having subsequently illegally terminated, without placing Plaintiff formally into breach and without any justification, while negotiations were underway in an attempt to solve the problem which had been artificially created by the Defendant itself.

The Plaintiff claims that termination is unjustified and ineffective, and that consequently the Contracts remain in force until their date of expiry. It therefore requests that the Defendant be ordered to perform the Contracts until they expire and to supply the Plaintiff, according to the terms of the Contracts, the goods ordered and any goods that may be ordered subsequently and to compensate the harm (lost profit and detriment to its credit standing and commercial reputation), suffered on account of the refusal to supply the goods until the date of the arbitral award.

Alternatively, if termination, notice of which was given by the Defendant, is considered effective (notwithstanding its illegal nature), the Plaintiff requests that the responsibility for termination of the Contracts be laid entirely and exclusively on the Defendant and that, consequently, the Defendant be ordered to compensate the Plaintiff for the harm (lost profit and detriment to credit and commercial reputation), suffered as a result of the illegal termination.

The Defendant, on its part, maintains that termination of the Contracts was justified [...] by the Plaintiff's breach of an essential obligation such as that of reaching the minimum agreed purchases and that, moreover, the Plaintiff had no right to be compensated for alleged harm deriving from termination.

On the contrary, the Defendant maintains that it has a right to compensation for the harm suffered on account of lost profits, loss of gross margin and of the market in the Plaintiff's country.

The questions of merit resulting from the parties' claims that must be settled are essentially the following:

1. In the first place it must be established whether, in the period preceding termination of the Contracts, the Defendant's behaviour (refusal to supply the goods on the contractually agreed conditions) constituted non-performance of the Contracts.
2. In this context it must also be determined whether the parties solved the problem by a settlement agreement concerning the orders in course and possible future orders.
3. Then it will be necessary to establish whether termination of the Contracts by the Defendant was justified and in particular whether such termination was validly made and whether the reasons invoked by the Defendant can justify termination of the Contracts before their expiry.
4. Should termination by the Defendant be considered illegal, it must be decided whether it has put an end to the Contracts or whether, on the contrary, they remain in force notwithstanding termination by the Defendant.
5. Depending on the replies given to the above questions, it must lastly be decided whether, and to what extent, the Plaintiff's claim for damages and the Defendant's counterclaim must be granted.

[...]

The Plaintiff claims that the Defendant, by unilaterally modifying the conditions of payment in its letter of [...] and by refusing subsequently to supply the goods ordered on the conditions set out in the Contracts, breached the Contracts and should compensate the Plaintiff for the harm it suffered on account of such breach of the Contracts.

[...]

The Defendant's behaviour is in principle contrary to a fundamental rule of contract law, namely, the principle of *pacta sunt servanda*, which has been incorporated also in the UNIDROIT Principles in Art. 1.3 according to which "A contract validly entered into is binding upon the parties. It can only be modified or terminated in accordance with its terms or by agreement or as otherwise provided in these Principles."

This principle is not of course absolute and therefore it is perfectly conceivable that a seller may, in particular circumstances, be permitted to no longer adhere to the agreed terms of payment. Thus it would be contrary to the principle of good faith to oblige a seller to continue to supply goods to its distributor without the possibility of requiring adequate payment guarantees whenever there are good reasons to fear that the latter will not pay for the goods on the date due. In the case at hand there were of course certainly facts prompting a certain prudence before accepting orders. [...].

Nevertheless such facts were not sufficient to justify the Defendant's unilateral decision to modify the terms of payment of the Plaintiff whose solvency was not in question. Consequently the Defendant's refusal to supply the goods on the contractually agreed terms certainly constituted a breach of contract.

[...]

After the first exchanges of correspondence indicated above the parties began to seek an amicable solution. [...] It remains to be seen whether the parties have reached an agreement capable of overcoming the differences examined in the foregoing paragraph.

For this purpose the negotiations concerning the terms of supply and of payment of the two orders No. XXXX/98 and No. YYYY/98 and the terms of payment of future orders will be examined separately.

[...]

As concerns orders N. XXXX/98 and No. YYYY/98 negotiations between the parties resulted in an agreement through an exchange of letters of [...] and of [...]. The only – completely negligible – difference is that the Defendant agreed to pay the difference between the cost of carriage by air and the cost of carriage by sea, while the Plaintiff asked the Defendant to pay the entire cost of carriage by air.

However, this does not exclude that a valid agreement has been reached. Indeed, in the context of the *lex mercatoria* correspondence between offer and acceptance is not a strict requirement, it being held (in conformity with the current view held by parties engaged in international trade) that an acceptance of an offer containing modifications or additions does not prevent the conclusion of a contract provided that the modifications and additions are of minor importance. Thus Article

2.11 (2) of the UNIDROIT Principles provides that "... a reply to an offer which purports to be an acceptance but contains additional or different terms which do not materially alter the terms of the offer constitutes an acceptance, unless the offeror, without undue delay, objects to the discrepancy."

In the case at hand the Plaintiff did not challenge the modification contained in the Defendant's acceptance and the agreement on the terms of payment and supply of the two orders can therefore be considered concluded on the not objected terms of acceptance of the Defendant. It may therefore be concluded that with respect to the two orders No XXXX/98 and No YYYY/98 the parties had reached an agreement according to which the Plaintiff undertook to pay the sum of US \$ 70.897,55 and the Defendant to send the goods in question within the next 8 days.

[...]

As concerns future deliveries, the parties agreed in a subsequent exchange of letters that the Plaintiff would pay for the goods in advance, on the basis of a pro forma invoice sent to it by the Defendant, and would obtain a discount corresponding to the discount rate in the Plaintiff's country for a period of 120 days, fixed for the current at 5%.

[...]

Nevertheless the parties did not expressly agree on the criteria to be followed to establish the amount of the discount in the event of a change in the discount rate. [...]

Must it therefore be concluded that an agreement as to the terms of payment of future deliveries had not been reached?

It is important to note that negotiations were carried out in successive stages leading to the progressive conclusion of the agreement. In a similar context it is quite possible that the parties reach partial agreements (that leave some terms open) provided that they did not intend to make their agreement dependant on the conclusion of an agreement covering all issues under discussion.

This principle is recognised in Art. 2.13 of the UNIDROIT Principles, according to which "Where in the course of negotiations one of the parties insists that the contract is not concluded until there is agreement on specific matters or in a specific form, no contract is concluded before agreement is reached on those matters or in that form".

Indeed, this rule implies, a contrario, that the agreement on some of the matters under discussion binds the parties with respect to those matters unless the parties intended to make conclusion of their contract conditional upon the agreement on all other matters. This corresponds after all to the usages and practices in international trade in the context of which contracts are frequently formed in stages, and a partial agreement is considered binding and parties are obliged to reach agreement on matters still open: see, for example, in Bull. Arb. CCI, 2/1999, p. 67-70.

In the case at hand it is certain that the parties agreed that the discount had to be determined on the basis of the discount rate in the Plaintiff's country. [...] the absence of agreement on a matter of such marginal importance [to modify the 5% rate only if the discount rate in the Plaintiff's country rose by more than 0,5%] cannot jeopardize the parties' overall agreement concerning terms of payment and supply.

It must therefore be concluded that the parties modified, by means of the of the agreements of [...], the terms of payment provided for in the Contracts by substituting payment within 120 days by payment in advance with a discount corresponding to the discount rate in the Plaintiff's country for a period of 120 days.

[...]

The Defendant gave notice of the termination of the Contracts to the Plaintiff in its letter of [...] and motivated it by the Plaintiff's failure to meet the sales figures established in Article 10.1.3 of the Contracts.

[...]

The Plaintiff claims that the failure to meet these figures does not constitute non-performance of the Contracts, since the figures were only market forecasts and not binding commitments. [...] Moreover, termination of the Contracts would in any case have required the formal placing of the Plaintiff into breach.

[...]

Before turning to the central question as to whether termination was justified, two preliminary questions have to be answered, whether termination must be preceded by a formal placing into

breach and whether notice of termination is subject to a time-limit. [...]

The Plaintiff claims that termination could not be declared without formally placing it into breach beforehand, thereby giving it the chance to remedy its alleged non-performance.

This position would be justified if there were (as frequently happens in Anglo-american contract practice) a contract term imposing a duty on the party giving notice of termination to grant the other party an additional period of time within which to remedy the alleged breach. However, since this was not the case in the case at hand, reference must be made to the general rule set out in Art. 7.3.2(1) of the UNIDROIT Principles according to which "The right of a party to terminate the contract is exercised by notice to the other party."

Consequently, Defendant's failure to formally place the Plaintiff into breach does not affect the validity of termination.

[...]

The Plaintiff objects that the claim that it failed to reach the sales forecast for the period [...] is late and cannot therefore be taken into consideration.

This is correct. The principle of good faith imposes on the party intending to terminate the contract on account of the other party's non-performance the duty to inform it of its intention within a reasonably short period of time from the moment when it came to know of the non-performance. This principle is contained also in the UNIDROIT Principles. Indeed, Art. 7.3.2(2), states: "If performance has been offered late or otherwise does not conform to the contract the aggrieved party will lose its right to terminate the contract unless it gives notice to the other party within a reasonable time after it has or ought to have become aware of the offer or of the non-conforming performance."

Now, in the case at hand, the Defendant already knew at the beginning of [...] that the Plaintiff had not reached the purchases forecast for the year [...] and did not bring up this fact until the month of [...] of [...].

Consequently only the claim concerning the year [...] will be taken into consideration in the following part .

[...]

The principle according to which a fixed term contract can be terminated before it expires if there are serious reasons for termination constitutes a widely recognised principle in international trade: even the UNIDROIT Principles state, in general terms, in Art. 7.3.1(1), that: "A party may terminate the contract where the failure of the other party to perform an obligation under the contract amounts to a fundamental non-performance."

At any rate, in the case at hand reference to the general rule is not necessary since Art 10.1.3 of the Contracts makes express provision for the right to terminate the contract before it expires when there has been a serious infringement of one of its clauses.

It is a matter therefore of establishing whether the Plaintiff's non-performance, invoked by the Defendant, amounts to a breach of the Contracts serious enough to justify termination before expiry.

Contrary to widespread contracting practice, the Contracts do not expressly state that the failure to meet the agreed sales figures permits the supplier to terminate the contract. Article 11.4 of the Contracts only makes provision for annual sales volumes ("Las partes acuerdan el siguiente presupuesto de compras"), but does not specify the consequences of a possible failure to meet the indicated sales figures. This means that failure to meet the forecast sales figures could justify termination of the contract only to the extent that such failure amounts to a fundamental breach of one of the contractual terms.

Considering that breach of a contractual clause necessarily implies the breach of the obligation provided in such a term, it is essential to establish whether Article 11.4 is intended to make provision for a commitment to purchase or whether it amounts, on the other hand, to a non-binding forecast.

The term used ("presupuesto") seems to indicate objectives rather than minimum purchases. On the other hand however the presence of the parties' signature next to the clause in question stresses the importance the parties attributed to that aspect.[...]

Having said this, it should be noted that the clause, which merely states that the parties have agreed on determined sales objectives, contains no obligation on the Plaintiff's part to guarantee that such a result is achieved: if this had been the parties' intention, they would simply have

agreed that the Plaintiff would undertake to purchase the annual quantities indicated in the clause.

Under such conditions the failure to meet the purchase objectives does not, in itself, amount to a breach of contract and as such cannot therefore be considered a justifiable reason for termination in advance.

Now, in the case at hand, it has not been proven that the failure to reach agreed purchases has been for reasons imputable to the Plaintiff rather than to the state of the market or to the place in which the new conditions of payment were negotiated (originating in the Defendant's unjustified refusal to supply). Under such conditions the mere reference to failure to reach the purchase objectives cannot be considered sufficient reason for terminating in advance a contract which had not even reached the mid point of its duration.[...]

The Arbitral Tribunal concludes that the reasons invoked by the Defendant to justify termination do not amount to a fundamental breach of Art. 10.1.3 of the Contracts and that termination must consequently be considered unjustified.

[...]

The Plaintiff claims that since the termination was unjustified it was ineffective and consequently the Contracts will remain in force until their expiry.

[...].

The problem of the effects of an unjustified termination of a contract is dealt with in different ways in the various legal systems: in some countries (above all in civil law systems) unjustified termination is ineffective, with the result that such a contract will remain in force and the parties will continue to have to fulfil their obligations; in other legal systems (and in particular in common law systems), even an unjustified termination puts an end to the contractual relationship, while the party who has unjustifiably terminated the contract is liable for damages to compensate the loss the other party has suffered.

This second approach, which has the advantage of certainty in contractual relationships, is the one generally adopted in international trade law. The UNIDROIT Principles seem to confirm this point of view by providing in Art. 7.3.2(1) that "The right of a party to terminate the contract is exercised by notice to the other party", and in Art. 7.3.5(1), that "Termination of the contract releases both parties from their obligation to effect and to receive future performance."

The Arbitral Tribunal holds that the latter solution corresponds to the rules and principles applicable in international trade and that, therefore, the consequences of an unjustified termination are limited to the terminating party's obligation to make compensation for the harm caused thereby to the other party.

It follows that the Plaintiff's request to have the other party obliged to perform the Contracts after they have been terminated (in particular as concerns the obligation to supply the goods and to respect exclusivity) cannot be granted.

[...]

The Defendant, considering that it unjustifiably terminated the Contracts, is obliged to compensate the harm caused to the Plaintiff by the termination.

The Plaintiff requests [...] for lost profits, the sum of US \$ 509.661,40, [...] and for detriment to its credit standing and reputation, the sum of US \$ 637.076,75, that is the abovementioned amount requested for lost profits of US \$ 509.661,40 multiplied by 1,25.

[...]

As concerns the years [...], the Plaintiff considered that in the year [...] the total amount of sales was equal to about US \$ 250.000, and drew the conclusion that it would be reasonable to expect at least the same result in the years [...] and a slightly higher volume of business (US \$ 300.000) in [...].

The purchases indicated by the Plaintiff are based on wholesale prices [...] It is worth noting that such a figure corresponds to the volume of sales, at the wholesale price purchasers in the Plaintiff's country paid to the latter. [...] With respect to the volume of business based on the wholesale price, the Plaintiff applied [...] a margin of 47,5%, [...].

The Arbitral Tribunal notes however that the margin of 47,50% is a gross margin that cannot serve to calculate the Plaintiff's lost profits which should be calculated on the basis of the net margin.

Indeed, as established in Article 7.4.2 of the UNIDROIT Principles "The aggrieved party is entitled

to full compensation for harm sustained as a result of the non-performance. Such harm includes both any loss which it suffered and any gain of which it was deprived, taking into account any gain to the aggrieved party resulting from its avoidance of cost or harm.”

Now, the gain the Plaintiff lost on account of the interruption of the Contracts and the consequent termination of supply is not a gross margin on the sale price, but the net gain after all expenses have been deducted.

This principle has on numerous occasions been recognised in arbitral awards: see arbitral award in the This principle has on several occasions been recognised in arbitral awards: see ICC Award n° 1250 (in Jarvin, Derains, Revueil des sentences arbitrales de la CCI 1974-1985, p. 30-33) concerning a Lebanese distributor in which the arbitros recognised a damages based on “average net profit”; ICC Award n° 5418 (in Jarvin, Derains, Arnaldez, Recueil des sentences arbitrales de la CCI 1986-1990, p. 132) referring to “net profit”; ICC Award n° 8362 (in Yearbook Commercial Arbitration, XXII-1997, p. 164-177) which considers damage to be “lost profits”.

In the absence of any indication concerning the calculation of net margin, the Arbitral Tribunal held that it had to use the criterion contained in Article 7.4.3 § 3 of the UNIDROIT Principles, according to which:

“Where the amount of damages cannot be established with a sufficient degree of certainty, the assessment is at the discretion of the court.”

In making this assessment the Tribunal considered on the one hand the value of the goods the Plaintiff had purchased from the Defendant and on the other the sales of the Defendant’s goods made by the Plaintiff (proportionate to the corresponding purchase price).

[...]

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