MEMORANDUM FOR CLAIMANT

WILLEM C. VIS INTERNATIONAL COMMERCIAL ARBITRATION MOOT

CLAIMANT	**RESPONDENT**
Mediterraneo Exquisite Supply, Co.	Equatoriana Clothing Manufacturing, Ltd.
45 Commerce Road	286 Third Avenue
Capital City	Oceanside
Mediterraneo	Equatoriana

FALTUS Vojtěch • FEIGLER Michal • HOLOUBKOVÁ Kamila
MALANÍK Michal • ŠLAMPA Martin • THIELOVÁ Linda
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FACULTY OF LAW

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Table of Contents

List of Abbreviations

AA	Application for Arbitration
Art./Arts.	Article/Articles
CIETAC	China International Economic and Trade Arbitration Commission
CISG	United Nations Convention on Contracts for the International Sale of Goods
CISG ACO	United Nations Convention on Contracts for the International Sale of Goods Advisory Council Opinion
CEAC	Chinese European Arbitration Centre
CE	Claimant's Exhibit
Claimant	Mediterraneo Exquisite Supply, Co. Manufacturing, Ltd. 45 Commerce Roead, Capital City, Mediterraneo
the Contract	The sales contract for 100,000 polo shirts concluded by Claimant and Respondent on 5 January 2011
the Convention	United Nations Convention on Contracts for the International Sale of Goods
e.g.	*exempli gratia* (for example)
et seq./et seqq.	*et sequens/sequentes* (and the following)
Dr.	Doctor
i.e.	*id est* (that is)
IBA	International Bar Association
ICC	International Chamber of Commerce
ILO	International Labour Organization
L/C	Letter of Credit
LCIA	London Court of International Arbitration
No./Nos.	Number/Numbers
NYC	New York Convention on the recognition and enforcement of foreign arbitral awards

Oceania Plus	Oceania Plus Enterprises
Oceania Plus group	Group of multinational companies owned by Oceania Plus; both Claimant and Doma Cirun belong to the group
p./pp.	Page/pages
para./paras.	Paragraph/paragraphs
PO	Procedural Order
RE	Respondent's Exhibit
Respondent	Equatoriana Clothing Manufacturing, 286 Third Avenue, Oceanside, Equatoriana
SCC	Stockholm Chamber of Commerce
SD	Statement of Defence
the Tribunal	The arbitration tribunal constituted for the case at hand consisting of Professor Presiding Arbitrator, Dr. Arbitrator 1 and Ms. Arbitrator 2
UCP	Uniforms Customs and Practice for Documentary Credits
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNIDROIT	International Institute for the Unification of Private Law
US/U.S.	United States
USD	United States Dollar
USDL	United States Department of Labour
v.	Versus
Vienna Convention	Vienna Convention on the Law of Treaties

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Rules

Cited as	**Title**
CEAC Rules	CEAC Hamburg Arbitration Rules
CISG	United Nations Convention on Contracts for the International Sale of Goods
Danubian Arbitration Act	Danubian Arbitration Act based on UNCITRAL Model Law on International Commercial Arbitration with amendments as adopted in 2006. Option II of Article 7.
IBA Rules	IBA Rules on the Taking of Evidence in International Arbitration
ILO Convention 182	ILO Convention No 182 on Worst Forms of Child Labour
ILO Convention 183	ILO Convention No 138 on the Minimum Age for Admission to Employment and Work
LCIA Rules	London Court of International Arbitration Rules
NYC	New York Convention on the recognition and enforcement of foreign arbitral awards
SCC Rules	Stockholm Chamber of Commerce Rules
UCP	Uniform Customs and Practice for Documentary Credits

UK Procedural Laws	Civil Procedure (Amendment No.2) Rules 2012, United Kingdom of Great Britain and Northern Ireland http://www.legislation.gov.uk/uksi/2012/2208/pdfs/uksi_20122208_en.pdf
UNIDROIT Principles	UNIDROIT Principles of International Commercial Contracts, 2010
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UN Global Compact/ Compact	United Nations Global Compact http://www.unglobalcompact.org	paras. 57, 61, 62, 63, 68
UN Global Compact participants	United Nations Global Compact participants http://www.unglobalcompact.org/ParticipantsAndStakeholders/index.html	para. 62
U.S. Apparel Industry Partnership's Workplace Code of Conduct	U.S. Apparel Industry Partnership's Workplace Code of Conduct http://lrgusa.com/files/documents/wright_code.PDF	para. 61
USDL Report	Report on codes of conduct in the apparel industry http://www.dol.gov/ilab/media/reports/iclp/apparel/apparel.pdf	para. 64
WRAP	Worldwide Responsible Accredited Production http://www.wrapcompliance.org/images/handbooks/wrap%20facility%20handbook%202010%20edition.pdf	para. 61

Statement of Facts

Claimant is registered and managed in the country of Mediterraneo. It is one of fifteen jointly owned subsidiaries of Oceania Plus and Atlantica Megastores that contracts with manufacturers of the clothing needed by them.

Respondent is a manufacturer of apparel residing in Equatoriana. It contracted with Claimant as well as with other members of Oceania Plus group in the past.

2007

Claimant conducted audit on Respondent in connection with April 2008 contract. The aim was to ensure that Respondent and all of its sub-contractors satisfy high ethical standards of Oceania Plus. During the audit Claimant discovered that one of Respondent's suppliers used child labour. However, Respondent intervened and had the manager of the plant, where child labour was used, fired around the date of the audit.

2011

5 January	Claimant contracted with Respondent for the delivery of 100,000 polo shirts, FAS Incoterms 2010 Oceanside, Equatoriana, by 19 February 2011, for USD 550,000. The polo shirts were destined for sale in Doma Cirun stores in Oceania. Contractual "policy clause" required Respondent to comply with ethical standards of Oceania Plus in the conduct of its business. Furthermore, the Contract included incentives for timely delivery.
9 February	Mr. Short, Respondent's Contracting Officer, called Mr. Long, Claimant's Procurement Specialist, to inform him about the delay in delivery.
24 February	The polo shirts were delivered to Port City, Oceania.
March/April	From 20 March to 5 April Doma Cirun sold 1000 Polo shirts to its regular customers.
5 April	A documentary was broadcasted in Oceania, showing children as young as eight years old working in appalling conditions in one of Respondent's sewing plants. Both Doma Cirun and Oceania Plus were condemned strongly for dealing with Respondent.
6 April	In reaction to the documentary, there were two-week demonstrations in

	front of Doma Cirun stores. Doma Cirun's sales dropped by 30 % and the sales of "YES CASUAL" polo shirts stopped.
8 April	Oceania Times published an article about Oceania's leading role in the efforts to abolish child labour and the support of business community in this regard. In reaction to that, the upheaval against Doma Cirun strengthened. Doma Cirun avoided the contract with Claimant. Subsequently, Claimant avoided the Contract with Respondent and requested disposal of the remaining stock of the polo shirts.
10 April	Respondent denied that it breached the Contract and refused to take back the goods.
20 April	After its previous announcement to Respondent, Claimant sold remaining 99,000 polo shirts to Pacifica Trading for USD 470,000 on Respondent`s account.
	Claimant bought 90,000 substitute polo shirts from Gold Service Clothing for USD 612,000.
15 September	Doma Cirun began arbitration proceedings against Claimant in accord with the arbitration clause in their contract.
	2012
January	Mr. Short finished his job with Respondent and started working for Jumpers Production.
14 January	Settlement agreement was reached in the arbitration between Claimant and Doma Cirun for USD 850,000.
15 February	Oceania Plus brought suit against Claimant in the courts of Oceania claiming reimbursement of USD 700,000 paid by Oceania Plus in the settlements with the investors.
25 June	Claimant reimbursed Oceania Plus for settlements with its investors.
1 July	Claimant submitted a Notice of Arbitration and a Statement of Claim against Respondent.
4 October	Claimant requested Mr. Short´s appearance at an oral hearing before the Tribunal in order to question him regarding his witness statement. Respondent informed Claimant that Mr. Short refuses to appear.

Summary of Argument

I. THE TRIBUNAL SHOULD DISREGARD THE WRITTEN TESTIMONY OF MR. SHORT, IF HE DOES NOT APPEAR AT THE HEARING. When a party intends to use a witness as evidence it must submit written witness statement as well as present the witness at the oral hearing before the Tribunal. The Tribunal should not permit Respondent to present the witness statement only, especially when Claimant is ready to present its witness and demanded cross-examination of Respondent's witness. Incomplete testimony of Mr. Short should be disregarded under both CEAC and IBA Rules, unless it is supported by his oral presentation. By admitting Mr. Short's testimony in written form the Tribunal would deprive Claimant of its right to cross-examine the witness and moreover, it would ignore Respondent´s failure to bear its burden of proof. Such a deprivation would be considered as a breach of fundamental principle of fair trial and would lead to setting aside of the arbitral award.

II. THE PARTIES DID NOT AMEND THE CONTRACTUAL DATE OF DELIVERY. Parties did not amend the date of delivery in the Contract. The amendment is not formally valid since it was not concluded in written form. Written form is required because parties could not have excluded national reservation in their choice-of-law clause. In any case, the parties did not amend the delivery date in the Contract during their telephone conversation. Respondent's statements during the conversation did not constitute a valid offer and even if there was a valid offer, Claimant did not accept it either by assent during the conversation or by change of L/C.

III. RESPONDENT FUNDAMENTALLY BREACHED THE CONTRACT BY USING CHILD LABOUR. Respondent was under the obligation not to use child labour in the conduct of its business. It breached this obligation by using child labour in one of its plants. Alternatively, Respondent failed to deliver goods fit for the particular purpose of resale in Oceania. Respondent breached the Contract fundamentally, since Claimant was substantially deprived of what it was entitled to expect under the Contract and the consequences of the breach were foreseeable.

IV. IN ANY EVENT, THE ARBITRAL AWARD APPROVING THE USE OF CHILD LABOUR WOULD BE SET ASIDE. The Tribunal has the obligation to render valid and enforceable arbitral award. An award that would find that Respondent's use of child labour did not constitute fundamental breach of the Contract would be in strong conflict with Danubian international public policy. Therefore, Claimant would apply for setting aside of such award.

V. CLAIMANT IS ENTITLED TO ALL CLAIMS IT SEEKS. Claimant paid contractual price and rightfully avoided the Contract. Hence, it is entitled to restitution of the purchase price. Moreover, Respondent delivered the goods late and must therefore pay stipulated contractual penalty. Finally, since both Claimant's settlements with Doma Cirun and Oceania Plus respectively were foreseeable, reasonable and thus recoverable, Respondent must compensate Claimant in full.

I. THE TRIBUNAL SHOULD DISREGARD THE WRITTEN TESTIMONY OF MR. SHORT, IF HE DOES NOT APPEAR AT THE HEARING

1 The parties have not agreed on the document only arbitration. Claimant has provided this Tribunal with witness statement and is willing to present its witness before the Tribunal as well. On the contrary, Respondent has submitted merely written statement of Mr. Short. The purpose of witness of facts, who Mr. Short undoubtedly is, is to clarify controversial issues between the parties – to help the Tribunal to solve the dispute. Two conditions must be met. First, a written witness statement shall be presented and second, the witness has to appear in oral hearing before the Tribunal. These two conditions together constitute an indivisible complex.

2 Under applicable CEAC Rules the Tribunal should disregard Mr. Short's written testimony unless he appears in person [**A.**]. Alternatively, the problem should be solved by using the IBA Rules as the best practice in the field. Under Art. 4.7 IBA Rules the Tribunal should disregard any witness statement, which is not supported by an oral presentation [**B.**]. If the Tribunal accepts written testimony without oral presentation, it would breach Claimant's right to fair trial due to impossibility to cross-examine witness. This would lead to setting aside of any final award [**C.**].

A. CEAC Rules allow the Tribunal to disregard Mr. Short's witness statement

3 The parties agreed on CEAC Rules as procedural rules applicable to the dispute at hand [*CE 1, p. 13, para. 20*]. CEAC Rules allow the Tribunal a relatively wide discretion in the area of evidence taking in order to ensure a flexible and individualized conduct of arbitration [*Franchini, p. 2223*]. The main borders being Art. 28(2) CEAC Rules, giving the Tribunal authority to decide the manner of hearing witnesses, and Art. 17(1) CEAC Rules, stipulating right of each party to a fair and efficient process for resolving disputes. A general rule can therefore be derived; if the Tribunal decides not to hear a witness, the decision should by no means infringe the opposing party's right to a fair process of resolving the dispute. However, this infringement would be the precise result if the Tribunal were to admit Mr. Short´s witness statement without ensuring his attendance at the hearing.

4 Furthermore, at the absence of any valid reasons for non-appearance on Mr. Short's side, Claimant's right to hear the witness is also supported by other CEAC Rules provisions. From the wording of numerous sections of CEAC Rules [Arts. 27, 28, 29 and 31 CEAC Rules] also clearly arises a heavy reliance on the presence of oral witness testimony. These articles demonstrate vital importance of oral testimony not only to the opposing party, but also to the Tribunal itself. In the current situation when the two witnesses (Mr. Short and Mr. Long) are contradicting each

other, the Tribunal will certainly benefit if it could observe both witnesses' demeanour and responses during the cross-examination in order to form best-informed and objective opinion based on its own first-hand impressions. The oral aspect of a hearing is very important to ascertaining the credibility of witnesses [*Waincymer, p. 914*].

5 Undoubtedly, the Tribunal cannot reach such insight into the witness credibility by being merely presented with Mr. Short's written witness statement. Without Mr. Short actually attending the hearing his one-sided statement would remain unverifiable. The Tribunal would therefore have no means of forming an objective and unbiased opinion of Mr. Short's testimony. As for Claimant, it is asked to accept Respondent's evidence without having the possibility to question it.

6 Under these circumstances the oral mode of hearing is crucial to the Tribunal's ability to reach best-informed and balanced opinion. Without hearing Mr. Short the Tribunal would compromise its main role during the decision making - to give the parties an equal opportunity to present their case. CEAC Rules honouring both oral hearing and fair process of arbitration would therefore be best served by the Tribunal disregarding Mr. Short's statement altogether on the basis of Art. 28(2) CEAC Rules.

B. The Tribunal is authorised to apply IBA Rules and as a result Mr. Short's written statement should be disregarded

7 The Tribunal should apply IBA Rules to the case at hand [**1.**] and decide in accordance with Art. 4.7 IBA Rules that Mr. Short's witness statement is inadmissible [**2.**].

1. IBA Rules represent the best practice in the field and thus shall be applied to the case at hand

8 If the Tribunal is not satisfied with the legal framework provided by CEAC Rules, it may reach to other rules as allowed under Art. 17(1) CEAC Rules. These secondary rules can be used to further interpret CEAC Rules and to provide more precise and better-fitting guidelines for solving the problem of Mr. Short's testimony. The Tribunal should therefore base the decision on CEAC Rules and also on general arbitration principles and best practice guidelines. IBA Rules represent appropriate arbitration guidelines through which the problem should be solved for three reasons.

9 Firstly, IBA Rules were formed notably for such a situation when the problem at hand cannot be solved by applying exclusively the rules of the selected arbitration centre. Arbitration rules and

statutes are usually silent on witness testimony. The IBA Rules thus fill in a substantial gap. The IBA Rules are perfectly suited to provide such guidance, because IBA Arbitration Committee has now more than 2,500 arbitration practitioners from 90 countries around the world [*IBA Commentary, pp. 2, 14*]. Hence, IBA Rules are globally accepted and represent a guiding authority as well as the best practice in the field for interpreting evidentiary issues in international arbitration [*Berger, p. 502*; *Moses, p. 175*].

10 Secondly, IBA Rules also prove to be the "best fit" to the situation at hand, since they provide an extensive amount of detail concerning the situation of an absentee witness and his witness statement which would supplement the current CEAC Rules provisions perfectly.

11 Thirdly, arbitration rules as well as national laws and general principles in many countries suggest the same approach as IBA Rules. As an example, Art. 20.4 LCIA Rules provides the Tribunal with explicit authority to disregard witness statement upon his failure to attend the oral hearing. A similar rule is present in Art. 28(3) SCC Arbitration Rules which puts a direct link between reliance on witness testimony and witness attendance at a hearing. Furthermore, most common law countries [Art. 81.28(2)(b) UK Procedural Laws; Rule 614(a) US Rules of Evidence] rely to a great extent on a Browne v. Dunn rule [*Browne v. Dunn*], which stipulates the necessity of cross-examination and allowance for the witness to explain his position on disputed issues. The negative result of these rules would be disregarding of the evidence since it cannot be questioned and therefore its reliability is uncertain.

12 For all these reasons, IBA Rules should be applied as the best-fitting guidelines to the particular situation of disregarding Mr. Short's witness statement.

2. Under Art. 4.7 IBA Rules the Tribunal should disregard Mr. Short's witness statement

13 By applying IBA Rules, the Tribunal can easily use a clean cut rule in Art. 4.7 which states that *"If a witness whose appearance has been requested pursuant to Article 8.1 fails without a valid reason to appear for testimony at an Evidentiary Hearing, the Arbitral Tribunal shall disregard any Witness Statement related to that Evidentiary Hearing by that witness"* [Art. 4.7 IBA Rules]. As Mr. Short's presence was clearly requested [*PO 1, p. 48, para. 4*], his testimony should be disregarded unless he appears at the hearing.

14 Although the same rule suggests that the Tribunal may still consider orally unsupported evidence, if exceptional circumstances exist [Art. 4.7 IBA Rules]. Claimant maintains that none are given in the case at hand. Exceptional circumstances can be seen as in cases of serious illness, fear for life

[*Born, p. 1843*] or obstacles of similar intensity. However, the problem of Mr. Short's new employer not approving of his attendance, hardly reaches the threshold. Neither can the argument that Mr. Short is having a very tight timetable [*PO 1, p. 48, para. 4*]. In *Parsons & Whittemore case* the court held that the petitioner was not prohibited from presenting its case where an arbitral tribunal refused to accommodate a key witness's schedule [*Parsons & Whittemore case*]. There is always the option of conducting a videoconference [Art. 28(4) CEAC Rules; *De Witt, p. 444*], a sufficient, cost-effective and less time-demanding way of compensating for witness presence during the oral hearing. The available sources, however, do not show that Respondent has ever proposed such solution.

15 Under such circumstances the Tribunal should apply the strict rule found in Art. 4.7 IBA Rules and conclude that scheduling conflicts do not constitute valid reasons excusing Mr. Short's absence at the hearing.

C. Claimant's deprivation of the right to cross-examine Mr. Short constitutes violation of due process which would lead to setting aside of the award

16 The Tribunal shall treat the parties with equality and provide them with reasonable opportunity to present their case [Art. 17(1) CEAC Rules]. This also necessarily applies to the evidence-taking part of arbitration. Ignoring this rule would lead to violation of due process, and therefore to setting aside of the future arbitral award under Art. 34 (2)(a)(ii) Danubian Arbitration Act.

17 Respondent asks the Tribunal to consider only written statement of its witness instead of evaluating his personal oral submission. At the same time, it asks Claimant to waive its right to cross-examine the witness and basically to give up on gaining more information on the controversial issues of the case. The importance of the oral witness testimony is emphasized by the fact that "*the exact wording of the phone call between Mr. Long and Mr. Short is not remembered with certainty by the two witnesses"* [*PO 2, p. 55, para. 27*].

18 As Claimant established, the Tribunal should disregard Mr. Short's witness testimony, if he fails to appear at the oral hearing. If Mr. Short's written testimony was admitted, it would be contrary to Claimant's right to cross-examine the witness, while the same right of Respondent would remain intact. Coming from common law background [*PO 2, p. 57, para. 36*], Claimant naturally gives high importance to the cross-examination of the witness. Even Respondent's civil law tradition depends to a large extent on oral hearing of witnesses to ensure greater degree of certainty [*Elsing, p. 59*].

19 Therefore, if the Tribunal deprives only Claimant of its right to cross-examine Respondent's witness, it is obvious that the parties are not treated equally. Equal treatment of the parties is an indivisible part of due process principle. By breaching this principle, the Tribunal faces the risk of its award being set aside under Art. 34 (2)(a)(ii) Danubian Arbitration Act. For the same reason Claimant could successfully resist the recognition of the award under Art. V(1)(b) NYC.

Regarding the admissibility of Mr. Short's written witness statement, Claimant asks the Tribunal to disregard it under both CEAC and IBA Rules, unless he appears at the oral hearing. Otherwise, the Tribunal would strip Claimant of its immanent right to cross-examine the witness. By admitting Mr. Short's testimony the Tribunal impairs arbitration process and thus taints any final award.

II. THE PARTIES DID NOT AMEND THE CONTRACTUAL DATE OF DELIVERY

20 On 9 February 2011, a telephone conversation between the representatives of Claimant and Respondent took place. In this phone call, Respondent notified Claimant about the delay of its performance [*AA, p. 7, para. 13*]. In Respondent's view, the conversation between both representatives constituted an amendment to the Contract [*SD, p. 36, para. 14*].

21 Claimant will prove that the delivery date was not amended during their telephone conversation as only written amendments could modify the Contract [**A.**]. Alternatively, even if the parties could have modified their Contract by an oral agreement, the conduct of the parties did not constitute an amendment at all [**B.**].

A. The amendment is not formally valid since it was not concluded in a prescribed written form

22 The Contract was not amended as only a written document can constitute a valid amendment. In the case at hand, freedom of form principle does not apply, as the parties could not have derogated from Art. 96 CISG [**1.**]. Since the parties could not have excluded the application of Art. 96 CISG, it would be further argued that the interpretation of Art. 96 CISG leads towards the direct application of the form requirements of Mediterraneo [**2.**].

1. The parties could not have excluded national reservation in their choice-of-law clause

23 Claimant and Respondent agreed that the Contract *"shall be governed by the United Nations Convention on Contracts for the International Sale of Goods of 1980 (CISG) without regard to any national reservation"* [*CE 1, p. 13, para. 20*]. It appears from the wording of the clause that national reservation under Art. 96 CISG is excluded. However, CISG has to be applied with all of its provisions for two reasons.

24 Firstly, CISG has a non-mandatory character, i.e. parties are allowed to exclude the application of CISG or derogate from or vary the effect of any of its provisions [Art. 6 CISG; *Secretariat Commentary*]. Nevertheless, party autonomy is not unlimited and is restricted expressly in one particular case [*Schlechtriem/Schwenzer, p. 47*]. Parties are explicitly prohibited to derogate from Art. 12 CISG which regulates the effects of the reservation under Art. 96 CISG [*Bonell*]. When a reservation under Art. 96 CISG is made, freedom of form does not apply where any party has its place of business in a reserving State [Art. 12 CISG].

25 Secondly, even if there was no explicit provision stating the mandatory nature of Art. 96 CISG, the impossibility to exclude a national reservation can be deduced from public international character of Art. 96 CISG. Final provisions of CISG are not addressed to individuals whose contracts are governed by CISG, but are addressed to Contracting States [*Winship, pp. 1-39; Schroeter*]. It follows that only Contracting States can have rights or obligations arising out of these provisions. Since Art. 96 CISG entails a right of the Contracting States to exclude certain effects of the Convention, only Contracting States may vary the effect of the national reservation by withdrawing it.

26 In addition, public international law background of national reservations can be seen in other legal instruments, not only in the CISG. Mediterraneo, Oceania, Danubia and Equatoriana are all parties to the Vienna Convention [*PO 2, p. 57, para. 36*], which also deals with national reservations. Vienna Convention sets forth the principle that every treaty in force is binding upon the Contracting States [Art. 26 Vienna Convention] and reservations have legal effects between these States [Art. 21 Vienna Convention]. Nothing is said about a right of an individual to modify legal effects of reservations.

27 To summarize, Claimant and Respondent could not have excluded national reservation under Art. 96 CISG because such exclusion is strictly prohibited by Art. 12 CISG. What is more, only

Contracting States can modify the effects of the reservation as Art. 96 CISG is not addressed to individuals.

2. Mediterraneo's form requirements must be applied directly

28 Interpretation of Art. 96 CISG indicates that form requirements of a reserving State must be applied directly. The reasons for following this interpretation are twofold. Firstly, drafting history of CISG shows that the Contracting States insisted on preservation of the national form requirements and this approach is still valid even today [**2.1.**]. Secondly, uniform application of CISG and foreseeability in the international trade can be better achieved by the interpretation favouring the direct application of form requirements [**2.2.**].

2.1. Direct application of national form requirements was intended by the reserving States in the past and such approach is reasonable even today

29 When diplomatic conference was called on 11 April 1980, the drafters wanted to create an international convention for the sale of goods which could be viewed as satisfactory for as many countries as possible [*Explanatory Note*]. The most difficult struggles the drafters had to face were the differences among the countries how to approach contract formation issues. Predominantly in the Western world, the freedom-of-form principle was recognized whereas in other states, form requirements were seen as crucial for the proper functioning of the international trade [*Honnold, p. 138*].

30 In order to harmonize legal traditions and perspectives of Western and Eastern countries, compromise was reached in Art. 96 CISG. Reserving Contracting States interpreted this provision in a way that their form requirements apply directly. This can be documented by various case law where the direct applicability of form requirements is not even questioned and is taken for granted by these States [*Flanges case; Lindane case; Tinplate case; Engines case; Russian case I*]. Even States that have not signed Art. 96 reservation acknowledge the direct applicability of form requirements [*Frozen Raspberries case; Microflock Textile case*].

31 Direct applicability of form requirements can be seen as reasonable even today. Although the international trade is more frequent and informal than ever before, legal certainty and the protection of the parties are still reasons for preservation of form requirements. Mr. Long has been concluding international sales contracts in writing since there was no possibility of oral amendments under the law of Mediterraneo [*PO 2, p. 56, para. 34*]. Moreover, where transactions of large sums of money take place, for instance a deal worth USD 550,000 [*CE 1, p. 12, para. 2*], it is reasonable to have at least written evidence of such a major transaction.

32 To conclude, the interpretation of Art. 96 CISG should be the one that fulfils the needs of all Contracting States. The demand for written form in contract is reasonable even today since it ensures legal certainty among the contracting parties. In consequence, writing requirement should be respected when a party has its place of business in a reserving State.

2.2. Uniform application of the CISG can be better achieved by direct application of form requirements

33 The Tribunal may be tempted to view Art. 96 CISG as creating a gap in the Convention. In such a case, conflict of laws rules should apply [*Winship pp. 1-47; Rajski p. 659; Schlechtriem p. 45*]. However, this approach goes against the uniform application of CISG [Art. 7(1) CISG]. Uniform application is a situation where every court or tribunal interprets the provisions of CISG with the same results [*Huber II*]. Claimant will establish that same results cannot be achieved by the application of conflict of laws rules.

34 The parties did not choose applicable national law. In the absence of the choice of law, legal orders in Danubia, Oceania, Mediterraneo and Equatoriana call for the law with the closest connection to the Contract [*PO 2, p. 56, para. 33*]. Although the closest connection is a common criterion for all the countries concerned, still different factors play a role in determining what the closest connection is. In one country, the important factor could be the place of conclusion of the contract while in another country the place of business of the seller might be decisive [*PO 2, p. 56, para. 33*]. It follows that these criteria do not contribute to legal certainty as different results can be achieved with different factors in Danubia, Oceania, Mediterraneo or Equatoriana.

35 The direct application, on the other hand, is always a certain solution. In every single case, in which a party has its place of business in a reserving Contracting State, the formal requirements of this state will apply. This would lead to the same result in each and every court of the Contracting State.

36 In conclusion, the application of conflicts of laws rules would have unforeseeable results and thus would not contribute to the uniform application of CISG. In contrast, direct application of form requirements would always lead to the same and foreseeable outcome.

B. Even if a written form of amendment was not required, the parties did not modify the delivery date in the Contract during their telephone conversation

37 Respondent's phone call and its statements during the telephone conversation did not constitute an offer to change the delivery date in the Contract [**1.**]. Even if Respondent's conduct

constituted a valid offer Claimant did not accept it either during the conversation or by changing of L/C [**2.**].

1. Respondent's statements during the telephone conversation did not constitute a valid offer to change the delivery date in the Contract

38 An offer is constituted when it is sufficiently definite and Respondent indicates its intention to be bound in case of acceptance [Art. 14(1) CISG]. Respondent's unclear statements for an offer need to be interpreted. Under Art. 8 CISG party's statements and conduct have to be interpreted according to the intent of that party. However, the party's intent is relevant only if the other party knew or could not have been unaware what the intent was [Art. 8(1) CISG]. Otherwise, the understanding of a third reasonable person is decisive [Art. 8(2) CISG]. In determining the intent of the parties, or the understanding that a third reasonable person would have had, the Tribunal should take into account all relevant circumstances including conduct, statements and negotiations [Art. 8(3) CISG]. Claimant will show that it was not possible to interpret Respondent's statements as a valid offer.

39 Respondent did not explicitly ask to amend the Contract during the conversation [*PO 2, p. 55, para. 27*], therefore Claimant did not know about Respondent's intent to amend delivery date in the Contract, and as such there was no meeting of minds [*Chemical Products case*]. Since subjective analysis is not conclusive in the present case, the Tribunal should interpret Respondent's statements according to the understanding of the third reasonable person under Art. 8(2) CISG as the next step [*Schlechtriem/Schwenzer, p. 151*]. The third person interpretation should be viewed from the point of Claimant [*Sun, p. 78*].

40 Both parties agree that Claimant emphasized the importance of timely delivery of the goods during negotiations [*AA, p. 7, para. 14; SD, p. 35, para. 7*]. The Contract expressly obliged Respondent to deliver on 19 February 2011 and it included incentives for early delivery and penalties for a late one [*CE 1, p. 12, para. 10*]. Respondent was very well aware that the contractual date of delivery was the latest by which the shirts could be easily transported to individual stores for the launch of the spring sales season [*AA, p. 7, para. 14; SD, p. 35, para. 7*]. Timely delivery was therefore of the essence for Claimant.

41 Respondent called Claimant only to inform it about the delay in delivery without any express reference to the Contract [*CE 2, p. 14; RE 1, p. 37*]. By this phone call Respondent could not have intended to amend the Contract because it could not have expected Claimant to bear all the costs of Respondent's breach. In addition, Respondent apparently wanted to further develop its

business relationship with Claimant. This is evidenced by the fact that Respondent offered the purchase price which barely covered its production costs [*PO 2, p. 52, para. 6*]. It is then possible and economically viable that Respondent only notified Claimant without any intent to amend the Contract because potential incomes from future contracts with Claimant would surely prevail over minor amount of stipulated penalties.

42 To summarize, the third reasonable person in the shoes of Claimant would have not understood the informative phone call as being an offer to amend the delivery date in the Contract.

2. Even if there was a valid offer Claimant did not accept it either during the telephone conversation or by change of L/C

43 Claimant did not accept the offer either during telephone conversation [**2.1.**], or by amending L/C [**2.2.**].

2.1. Claimant did not accept the offer to change delivery date in the Contract during the telephone conversation

44 Since the intent of the parties is disputed, the only reasonable interpretation of Claimant's statements is objective analysis under Art. 8(2) CISG. Therefore, the Tribunal should analyse only the third reasonable person approach.

45 There is no agreement which precise terms Claimant used during the phone conversation, but the terms were alongside "necessary paperwork" [*PO 2, p. 55, para. 27*]. However, it is undisputed that Claimant never made a specific reference to the Contract [*PO 2, p. 55, para. 27*]. When Respondent notified Claimant about late delivery, Claimant had to resolve this issue. Claimant had to change L/C, because it called for documents indicating arrival of the goods by 19 February 2011 [*AA, p. 7, para. 12*] and later date on documents would have not been acceptable. On the other hand, it did not make any sense for Claimant to amend the Contract itself, because by amending it Claimant would have waived its right to seek stipulated penalties. Claimant had no financial reason to accept Respondent's offer. It follows that Claimant's statement could not have been understood as an assent with Respondent's offer.

46 Under these circumstances, the third reasonable person familiar with the commercial practice and the transaction itself would not consider statements of Claimant during the phone conversation as an acceptance of the delivery date amendment.

2.2. The change of the date in L/C does not mean change of the Contract by conduct

47 The Tribunal may be willing to consider the subsequent conduct of Claimant as proving the acceptance of change of the delivery date. However, neither Claimant, nor the third reasonable person could have acted otherwise, because of L/C being involved in the transaction.

48 Under the strict compliance doctrine, Respondent had to present exactly the same documents as required in L/C contract [Art. 18(c) UCP]. Even minor mistake can lead to the bank's refusal to pay off money to the seller. For example, the bank refused the payment to seller who presented cargo documents with shipped amount of 4.997 pieces of goods whereas contract of L/C called for the delivery of 5.000 pieces of the goods [*Carr, p. 482*]. L/C is also governed by the principle of autonomy [Arts. 4, 5 UCP]. It means that the banks involved in the transaction are not bound by the original contract, because they deal with documents only [*Carr, p.* 478].

49 L/C required documents indicating arrival of polo shirts by 19 February 2011 [*AA, p. 7, para. 12*], but Respondent's delivery was late. Following the strict compliance doctrine Claimant had to change L/C. If it had not, the bank would have refused to pay off the money. That would have equalled to Claimant's refusal to pay the purchase price [*Fashion Products case*]. Therefore, it is preposterous to think that by changing L/C Claimant would have agreed to amend the Contract.

50 In addition, following the autonomous doctrine, once Claimant opened L/C its existence became independent on the Contract. Unless Respondent proves that the intent to change L/C involved also the intent to amend the Contract, change of one L/C element does not automatically constitute amendment of the Contract.

51 For all these reasons, Claimant had to change L/C in order to fulfil its contractual obligation to pay the purchase price. Claimant's change of autonomous L/C does not mean its implied assent with the amendment of the Contract. Not even a third person in the shoes of Respondent would have interpreted the change of L/C as an assent with Respondent's offer.

Regarding the alleged amendment of the delivery date, Claimant asks the Tribunal to find that the telephone conversation did not constitute an amendment to the Contract as only written agreement could modify the Contract. Notwithstanding parties' agreement, Art. 96 CISG must be applied. As a result, form requirements of Mediterraneo shall be used directly.

Alternatively, if the Tribunal holds that an oral agreement could constitute a formally valid amendment, the conduct of Claimant and Respondent cannot be understood as an agreement in the first place. Respondent's statements during the telephone conversation cannot be viewed as an offer to change the delivery date; even if so, this offer was never accepted by Claimant.

In conclusion, parties did not amend the delivery date in the Contract.

III. RESPONDENT FUNDAMENTALLY BREACHED THE CONTRACT BY USING CHILD LABOUR

52 Respondent used children as young as eight to work for it in at least one of its sewing plants. The working conditions were appalling [*AA, p. 8, para. 18; PO 1, p. 49, para. 8*]. Normally, this would be morally inacceptable. In the case at hand, not only is this practice morally inacceptable, but it also constitutes fundamental breach of the Contract.

53 Respondent breached the contractual obligation by using child labour in one of its plants [**A.**]. Alternatively, Respondent breached the Contract since the polo shirts were not fit for the particular purpose, i.e. resale in Oceania [**B.**]. In any event, Respondent breached the Contract fundamentally [**C.**].

A. Respondent breached the Contract by using child labour in one of its plants

54 Respondent used child labour in at least one of its sewing plants [*PO 1, p. 49, para. 8*]. Therefore, Respondent breached the Contract because pursuant to "policy clause" it was obliged not to use child labour in any of its business operations [**1.**]. Furthermore, the obligation to avoid child labour is an international trade usage applicable to the Contract [**2.**].

1. Respondent had contractual obligation to avoid child labour in the conduct of its business

55 Respondent was obliged not to use child labour in the conduct of its business since it contractually agreed to follow Oceania Plus policy. Art. 12 of the Contract provides that: *"all suppliers to Oceania Plus Enterprises or one of its subsidiaries will adhere to the policy of Oceania Plus Enterprises that they will conform to the highest ethical standards in the conduct of their business"* [*CE 1, p. 12, para. 12*].

56 In order to determine what Oceania Plus policy encompasses, one must refer to Art. 8 CISG and interpret the Contract. As a member of Oceania Plus group Claimant audited Respondent and its subcontractors in connection with the 2008 contract and provided it with a "policy document" containing ethical and environmental standards to be complied with in the production of the goods [*AA, p. 6, para. 9; PO 2, p. 52, para. 4*]. In the negotiations following the audit results parties extensively discussed policy of Oceania Plus [*PO 2, p. 52, para. 4*]. In particular, the focus was placed upon the use of child labour [*AA, p. 6, para. 9*]. It was established in the audit that one of Respondent's suppliers used child labour in at least one of its plants producing for Respondent. Respondent intervened and the manager of the plant had been fired around the date

of the audit [*PO 2, p. 51, para. 3*]. Based on these facts, it is conclusive that Respondent knew or could not have been unaware that Oceania Plus policy encompasses complete avoidance of child labour [Art. 8(1) CISG].

57 In addition to that, Oceania Plus participates in the *UN Global Compact* [*AA, p. 8, para. 19*]. Hence, the reference to its policy must be seen in light of the *UN Global Compact*. This is a policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption. Principle 5 is the effective abolition of child labour [*UN Global Compact*]. Therefore, a third reasonable business person would have understood that Oceania Plus policy includes prohibition of child labour as such [Art. 8(2) CISG].

58 To summarize, by virtue of Art. 12 of the Contract and its interpretation Respondent was prohibited to use child labour as such.

2. Prohibition of child labour is an international trade usage in the garment industry

59 Even if the Tribunal holds that the parties did not make the obligation to avoid child labour explicitly or implicitly part of the Contract, Respondent is still under such obligation, as it is an international trade usage.

60 In order to establish the existence of international trade usage that automatically supplements contracts governed by CISG, two conditions have to be met. First, the usage has to be widely known and generally observed in the pertinent trade, and second, the parties to a contract at least ought to have known about it [Art. 9(2) CISG].

61 Fulfilment of the first condition, i.e. the knowledge and general observance of it in the clothing industry, is evidenced by massive proliferation of private initiatives aimed at compliance with basic ethical standards in general and abolishment of child labour in particular, e.g. *SA8000*, *U.S. Apparel Industry Partnership's Workplace Code of Conduct*, *WRAP* as well as the abovementioned *UN Global Compact*.

62 The *UN Global Compact* is prominent among these initiatives, because it has over 10,000 participants including 7,000 businesses in 145 countries. Compact participants include many major clothing brands like Levi Strauss & Co., Nike, Inc., PUMA SE, Inditex, Industrias de. [*UN Global Compact participants*] and also Oceania Plus, the parent company of Claimant [*AA, p. 8, para. 19*]. The influence of the *UN Global Compact* is so substantial and widespread that the basic ethical standards set by it, including the prohibition of child labour, form international trade usage in the

sense of Art. 9(2) CISG in every industrial sector [*Schwenzer/Leisinger, p. 265*], manufacturing of apparel being no exception.

63 The heart of the *UN Global Compact* is The Ten Principles, which comprise the basic ethical standards to be followed by all the businesses. Principle No. 5 is the effective abolition of child labour. Abolition standards are defined with reference to ILO Conventions 182 and 138. Any hazardous work done by children under 18 years of age should be banned, as well as any light work done by children under 13 years of age. Under ILO Convention 182 a textile machine operator is recognized as a hazardous work [*Diallo, p. 30*]. At one of Respondent's sewing plants, this hazardous work was done by children as young as 8 years [*AA, p. 8, para. 18; PO 2, p. 54, para. 17*].

64 Besides the Compact, every major clothing company has also a code of conduct. Pursuant to these codes of conduct, the companies publicly declare which ethical standards they and all their sub-contractors comply with. Avoidance of child labour is always on the list [*USDL Report*].

65 These private initiatives as well as individual codes of conduct are not only formal declarations; their observance is backed by substantial economic interests of entrepreneurs. This is because the public image is the most valuable asset in the clothing industry, and it often determines which brand the public will choose to buy [*Sajhau, p. 10*]. Such public declaration then puts enormous pressure on the companies. If it is discovered that a company deviated from the principles it publicly sworn to, the consequences are harsh. The damage to a company's reputation may be irreparable.

66 This is well illustrated by the "Kathie Lee Gifford scandal". When it was discovered that the Kathie Lee Gifford line of women's clothing sold by Wal-Mart was manufactured under sweatshop conditions in Honduras by children as young as 12, the public reaction was extremely negative. It was so strong that it caused massive financial losses to Wal-Mart due to consumers' boycott, Gifford's career took a down-turn, and even the ABC channel where Gifford hosted a popular show, otherwise not connected to the scandal, suffered serious loss of reputation [*Van Vleet*].

67 The second condition of existence of international trade usage, i.e. Respondent's knowledge or imputed knowledge about it, is also met. Respondent is a professional in the textile industry and as such it ought to know about the international trade usage that is applicable in this trade. It is also worth noting that Respondent regularly does business with companies owned by Oceania Plus and that Respondent resides in the ILO Convention 182 member state [*AA, pp. 10-11, para. 32; PO 2, p. 53, para. 15*].

68 In conclusion, the *UN Global Compact* and all the major clothing companies' codes of conduct have something in common. They prohibit the use of child labour. Nowadays, in the 21st century, there is little doubt that the obligation to avoid child labour is an international trade usage. The usage is generally observed, and it is especially observed in the apparel industry where the sensitivity of the public to the child labour issue is very high. Every corporate stumble in this regard brings a huge scandal and massive loss. For all these reasons, the implications of child labour usage are well-known by Respondent, as Respondent is a professional in the clothing industry. For all these reasons, by virtue of Art. 9 (2) CISG, Respondent was obliged not to use child labour in its operations.

B. In the alternative, the polo shirts were not fit for the purpose of resale in Oceania

69 Even if the Tribunal holds that Respondent did not breach its contractual duty, Respondent breached its obligation under Art. 35(2)(b) CISG because the polo shirts were not fit for the particular purpose made known to it [**1.**]. Claimant reasonably relied on Respondent's skill and judgement [**2.**]. Finally, Claimant could not have been aware of any lack of conformity when the Contract was concluded and thus Article 35(3) CISG is not applicable [**3.**].

1. Respondent breached the Contract by delivering polo shirts that were not fit for the purpose of resale in Oceania

70 Under Art. 35 CISG Respondent must deliver goods that conform to the quantity, quality and description required by the Contract. Furthermore, Art. 35(2)(b) CISG provides that the goods will not conform to the Contract unless they are fit for particular purpose expressly or impliedly made known to Respondent at the time of the conclusion of the Contract. In other words, the polo shirts delivered by Respondent ought to possess qualities necessary for the purpose, which Respondent knew of at the time of the conclusion of the Contract.

71 Quality must be understood as meaning *"all factual and legal circumstances concerning the relationship of the goods to their surroundings"* [*Schlechtriem/Schwenzer, p. 572*]. Therefore, compliance with certain manufacturing standards or fundamental ethical principles forms part of the quality characteristics [*Schlechtriem/Schwenzer, p. 573*]. In the case at hand, quality requirements included prohibition of child labour because Respondent knew the particular purpose of the goods, i.e. resale of the polo shirts in ethically oriented country of Oceania.

72 Oceania endeavours to abolish child labour both domestically and internationally. It played leading role in the creation of ILO Convention 182 and its work in this field is heavily supported

by businesses such as Oceania Plus [*AA, p. 8, para. 19*]. Therefore, goods manufactured by a company that uses child labour are as a matter of principle unmerchantable in Oceania.

73 Respondent was aware that the goods were destined for Oceania to be resold to final customers by Doma Cirun, subsidiary of Oceania Plus [*PO 2, pp. 53-54, paras. 15, 16*]. Respondent should have known about the peculiarities of the market there, namely the emphasis on ethical conduct of businesses [Art. 8(2) CISG] since it had previously concluded contracts with third parties in which the goods were destined for Oceania [*PO 2, p. 53, para. 15; Schlechtriem/Schwenzer, p. 578; Spanish Paprika case*].

74 Hence, by using child labour in one of its plants Respondent failed to deliver conforming goods because the polo shirts were not fit for the purpose of resale in Oceania.

2. Claimant reasonably relied on Respondent's skill and judgement

75 Under Art. 35(2)(b) CISG Respondent shall be responsible for the fitness for the particular purpose once it is established that Claimant reasonably relied on Respondent's skills and judgement. Reliance occurs when the seller is an expert or professional in the field in which the buyer intends to use the goods and it is maintained even if the buyer possesses knowledge in the same field as the seller [*Schlechtriem/Schwenzer, p. 582*]. Here, Respondent is clearly a professional manufacturer of textile. Furthermore, it had experience with both concluding contracts in which the goods were to be resold in Oceania and with supplying clothing to Claimant [*PO 2, p. 53, para. 15*]. Therefore, Claimant reasonably relied on Respondent's skill and judgement in purchasing the polo shirts.

3. Claimant could not have been aware of use of child labour by Respondent at the time of the conclusion of the Contract

76 The Tribunal may dismiss liability claim, only if Respondent proves that Claimant could not have been unaware of Respondent's use of child labour at the time of the conclusion of the Contract [Art. 35(3) CISG]. Liability can only be excluded for a lack of conformity that is obvious [*Schlechtriem/Schwenzer, p. 586*]. Though, at the time of the conclusion of the Contract, Claimant did not know about Respondent's use of child labour [*PO 2, p. 51, para 3; PO 2, p. 52, para. 5*], otherwise it would have never entered into the Contract.

77 To summarize, Claimant could not have been aware of the use of child labour by Respondent at the time of the conclusion of the Contract.

C. Respondent breached the Contract fundamentally

78 Respondent's breach of the Contract is fundamental because it resulted in such detriment to Claimant as substantially to deprive it from what it was entitled to expect under the Contract [**1.**], and such a result was foreseeable for Respondent as well as it would be for any reasonable person in the shoes of Respondent [**2.**].

1. Claimant was substantially deprived of what it was entitled to expect under the Contract

79 Claimant expected Respondent to comply with all contractual provisions and to deliver 100,000 YES CASUAL polo shirts fit for resale in Doma Cirun stores in Oceania. Respondent's use of child labour deprived Claimant of what it was entitled to expect under the Contract so substantially, that Respondent's breach has to be considered fundamental [Art. 25 CISG; *Bonaventure case*]. The fundamental nature of Respondent's breach follows from two aspects. First, the particular obligation that was breached, i.e. the obligation to avoid child labour was of immense importance under the Contract. And second, Respondent's breach had profound impact on Claimant.

80 To the first aspect, the fundamental importance of the contractual obligation to avoid child labour is demonstrated by the effort Claimant invested into the audit and discussions accompanying it. Respondent knew that Claimant is strongly against any use of child labour. This is supported by Respondent's own conduct; Respondent itself actively intervened in a case where one of its suppliers was using child labour and made sure that the manager responsible for it was fired [*PO 2, p. 51, para. 3*]. Respondent knew that not only it had to avoid child labour in all of its plants but also all of its suppliers had to be child labour-free in order for Respondent to get and stay on the list of potential suppliers of all companies belonging to Oceania Plus group [*PO 2, pp. 51-52, paras. 2, 4*].

81 To the second aspect, the Tribunal shall examine the seriousness of the breach to establish whether the breach was fundamental. Claimant belongs to the Oceania Plus group operating in the textile industry. Within the group, Claimant has a role of intermediary. It contracts with manufacturers, such as Respondent, and subsequently supplies the retailers belonging to the group, such as Doma Cirun, with the textile they need [*AA, p. 6, para. 7*]. When the public in Oceania learned that Respondent, company manufacturing apparel carrying Doma Cirun's label YES CASUAL, is using child labour, the reaction was extremely strong. There were demonstrations in front of Doma Cirun stores which continued for two weeks [*AA, p. 8, para.*

20]. The sales of YES CASUAL polo shirts stopped and the overall sales of Doma Cirun dropped dramatically. Even after more than a year has gone by, the sales are still down by 50 % [*AA, p. 8, para. 20; PO 2, p. 54, para. 19*].

82 It is without any doubt that the reputation of Doma Cirun and Oceania Plus was irreparably damaged. Doma Cirun's lost profit was enormous and the loss of Oceania Plus in the form of decrease of shareholder value was in hundreds of millions USD [*AA, p. 8, para. 21*]. As a result, Claimant had to pay huge settlement amounts both to Doma Cirun and Oceania Plus [*AA, pp. 9-10, paras. 27, 29*]. But the biggest loss caused to Claimant is in fact the loss of goodwill of Oceania Plus and Doma Cirun. And because of the interconnectedness of the companies belonging to the Oceania Plus group, Claimant is on the same leaking life-boat with them.

83 To sum up, Claimant was substantially deprived of what it was entitled to expect under the Contract, because the obligation to avoid child labour was essential under the Contract and its breach by Respondent had serious consequences for Claimant.

2. Respondent should have foreseen the detriment and its consequences

84 Respondent should have foreseen that the use of child labour would constitute substantial deprivation of what Claimant expected under the Contract, thus it cannot rely on the foreseeability requirement [Art. 25 CISG].

85 Respondent was aware that the goods were to be delivered to Oceania, a country known for its high ethical standards [*AA, p. 8, para. 19*]. Apart from the relations with Claimant, Respondent concluded at least three other contracts, in which the goods were destined for Oceania [*PO 2, p. 53, para. 15*]. Consequently, Respondent was familiar with the country of destination for the YES CASUAL polo shirts from its previous dealings. As for YES CASUAL and Doma Cirun, these are well known to manufacturers of clothing in Equatoriana, therefore also to Respondent [*PO 2, p. 53, para. 16*].

86 Moreover, Respondent also knew that Claimant is a part of a bigger structure of companies [*PO 2, p. 52, para. 5*]. Hence, it was possible for Respondent to make a link between the losses of Claimant and the other companies in Oceania Plus group. Under these circumstances, any reasonable person in the shoes of Respondent would have foreseen such result.

87 In conclusion, Respondent's use of child labour constituted fundamental breach of the Contract because it resulted in substantial deprivation for Claimant of what it was entitled to expect under the Contract, and such result should have been foreseeable for Respondent.

Regarding Respondent's use of child labour, Claimant asks the Tribunal to find that Respondent was under the obligation not to use child labour and that it breached this obligation. Alternatively, the Tribunal should rule that Respondent failed to deliver goods fit for the particular purpose of resale in Oceania. In any case, Respondent breached the Contract fundamentally.

IV. IN ANY EVENT, THE ARBITRAL AWARD APPROVING THE USE OF CHILD LABOUR WOULD BE SET ASIDE

88 Arbitrators are obliged to issue enforceable awards, at least in the sense that awards rendered by them would not be set aside in the state of origin, i.e. under the *lex arbitri* [*Platte, p. 308*].

89 Under Art. 34(2)(b)(ii) Danubian Arbitration Act, a court may set aside the arbitral award if it conflicts the public policy of Danubia. According to one of the most frequently cited attempts to define what the public policy exception encompasses, it should apply "*only where the forum state's most basic notions of morality and justice*" would be violated [*Parsons & Whittemore*]. There is no doubt that public policy exception should be interpreted very narrowly [*Harris, p. 11*].

90 However, the issue at stake is the use of child labour in its worst form. Respondent used children as young as 8 years old to work in its sewing plant under appalling working conditions [*AA, p. 8, para. 18*]. Claimant maintains that not only is this a fundamental breach of the Contract, but also a breach of basic humanity and morals. Should the Tribunal find in its award that the use of child labour in Respondent's operations did not constitute a fundamental breach of the Contract, it will in fact approve unethical behaviour of Respondent. Such award would surely violate Danubian public policy. In that case, Claimant will have to stand for its principles and apply for setting aside.

Regarding the duty to render an enforceable award, Claimant appeals to the members of the Tribunal to take into account Danubian public policy when deciding on the issue of the breach of the Contract.

V. CLAIMANT IS ENTITLED TO ALL CLAIMS IT SEEKS

91 Due to the use of child labour in one of its plants Respondent breached the Contract fundamentally. This had several significant impacts: drops of sales of Doma Cirun, loss of Doma Cirun's and Oceania Plus' reputation, as well as decrease in value of Oceania Plus' shares [*AA, p. 8, paras. 20, 21; PO 2, p. 54, para. 19*]. As a consequence, Doma Cirun avoided the contract

with Claimant [*CE 5, pp. 18-19*] and subsequently Claimant avoided the Contract with Respondent [*CE 6, p. 20*]. Proceedings against Claimant brought by Doma Cirun and Oceania Plus followed. Fortunately, Claimant succeeded in reaching very favourable settlements.

92 Claimant is now seeking to compensate the financial consequences it suffered due to Respondent's fundamental breach of the Contract. Claimant is entitled to the restitution of the purchase price [**A.**], payment of the penalty for delayed delivery [**B.**] and recovery of the settlements with Doma Cirun and Oceania Plus [**C.**].

A. Claimant is entitled to the restitution of the purchase price

93 Under Art. 81 CISG two conditions must be met in order to restitute the purchase price. First, the purchase price had to be paid, and second, the Contract rightfully avoided. As to the first condition, Claimant paid full purchase price to Respondent via L/C [*AA, p. 7, para. 15; SD, p. 35, para. 7; Fashion Products case*]. Moving to the second condition, Claimant properly exercised the right to declare the Contract avoided [**1.**] and it did not lose such right [**2.**].

1. Claimant properly exercised the right to declare the Contract avoided

94 Due to Respondent's use of child labour, Claimant gained the right to avoid the Contract. Claimant effectively exercised this right because it fulfilled all the conditions required. Under Art. 26 CISG the declaration of avoidance must be made known by notice to the other party. The notice must clearly express that the buyer now treats the contract as at an end [*UNCITRAL Digest on Art. 49*]. And such notice must be made in the reasonable time after the party knew or ought to have known of the breach [Art. 49(2)(b)(i) CISG].

95 Claimant declared the Contract avoided in its letter where it expressly stated that, "*as a result* [of Respondent's breach] *we are avoiding the contract*" [*CE 6, p. 20*]. This notice was clear and in a written form. It was also timely because Claimant learned about the breach on 5 April 2011 [*AA, p. 8, para. 18*] and sent the notice on 8 April 2011 [*CE 6, p. 20*].

96 In conclusion, Respondent fundamentally breached the Contract and as a consequence Claimant gained the right to avoid it. The declaration of avoidance was sufficiently definite and timely.

2. Claimant did not lose its right to declare the Contract avoided

97 Art. 82(1) CISG states that "*The buyer loses the right to declare the contract avoided* […] *if it is impossible for him to make restitution of the goods substantially in the condition in which he received them*." The principle of natural restitution must be interpreted narrowly whereas the exceptions to it extensively [*Schlechtriem/Schwenzer, p. 1116*]. The key distinguishing point is whether the goods were sold

before or after the avoidance. If the goods are sold after a contract is avoided, it does not prevent avoidance as long as the buyer is able to return the goods at the time of the avoidance in substantially unimpaired condition [*Schlechtriem/Schwenzer, p. 1118; Shoes case; Packaging Machine case*]. Claimant will show that firstly, it resold the polo shirts to Pacifica Trading Co. after the avoidance of the Contract [**2.1.**] and secondly, Doma Cirun sold the polo shirts in the normal course of business [**2.2.**].

2.1. Claimant resold 99,000 polo shirts to Pacifica Trading Co. after the rightful avoidance in order to mitigate damages

98 Claimant urged Respondent to dispose the polo shirts from its warehouse in its letter of avoidance [*CE 6, p. 20*]. Nevertheless, Respondent categorically refused to do so [*PO 2, p. 54, para. 21*]. After that Claimant informed Respondent about its intention to sell the polo shirts and finally sold them to Pacifica Trading on Respondent's account [*PO 2, p. 54, para. 21*]. Pacifica Trading agreed to buy the polo shirts for USD 470,000, which was very favourable in comparison to the original purchase price USD 550,000. The amount of USD 470,000 is satisfactory especially considering the fact that the polo shirts could not have been reasonably sold in countries with strong anti-child labour policies. The Contract with Pacifica Trading Co. was performed on 20 April 2011, i.e. 12 days after the avoidance of the Contract [*AA, p. 9, para. 24*]. Therefore, Claimant was able to return the polo shirts in substantially unimpaired condition to Respondent at the time of the avoidance of the Contract.

99 Furthermore, Claimant resold the polo shirts in order to fulfil its obligation to mitigate the loss pursuant to Art. 77 CISG. If Claimant had not been actively dealing with the situation, it would have had to store the polo shirts in a warehouse and subsequently claim the storage costs. However, Claimant acted as a skilled merchant and proactively arranged a cover sale, thus in fact decreased the amount of damages Respondent is obliged to pay. Moreover, the polo shirts were fashionable goods; therefore, they would be losing on value and marketability in the passage of time.

100 Hence, Claimant respectfully requests the Tribunal to rule that by reselling the polo shirts Claimant did not waive its right to avoid the Contract and effectively mitigated the loss.

2.2. Before the avoidance of the Contract, 1,000 polo shirts were sold in the normal course of business

101 Before the television broadcast on 5 April 2011, Doma Cirun sold 1,000 polo shirts to its regular customers [*PO 2, p. 56, para. 31*]. Under Art. 82(2)(c) CISG Claimant could not avoid the

Contract unless the goods were sold in the normal course of business before Claimant discovered or ought to have discovered the breach of the Contract.

102 In the case at hand the breach of the Contract was not apparent. In fact, it was hidden. Both Claimant and Doma Cirun discovered that Respondent used child labour and breached the Contract only on 5 April 2011 once the Channel 12 documentary was broadcasted [*AA, p. 8, para. 18; CE 5, p. 18*]. Doma Cirun avoided the contract with Claimant and in turn Claimant avoided the Contract with Respondent. But the polo shirts were sold to customers before 5 April 2011 and therefore, these sales are covered by the exception in Art. 82(2)(c) CISG.

103 Under these circumstances, the Tribunal may also rely on decision in *Spanish Paprika case*. The buyer who resold paprika in the ordinary course of business before discovering that the goods contained ethylene oxide in amounts that exceeded domestic legal limits retained its right to avoid the contract. It was further held that the buyer was not obliged to reveal non-conformity if it means to employ unusual measures. Similarly, neither Doma Cirun nor Claimant could have been expected to find that child labour had been used in one of Respondent's plants. Unlike *Spanish Paprika case,* where it was at least objectively possible to examine the goods and find their non-conformity, in the present case not even the most thorough inspection of the goods would possibly reveal that Respondent used child labour.

104 To summarize, 1,000 polo shirts were sold in the normal course of business before the avoidance of the Contract. It was reasonable for Claimant to resell remaining 99,000 polo shirts to Pacifica Trading Co. after the rightful avoidance of the Contract in order to mitigate increasing damage. Because Claimant rightfully avoided the Contract, it is entitled to restitution of the purchase price it duly paid.

B. Claimant is entitled to payment of the penalty for the delay in delivery

105 Claimant and Respondent agreed on the following penalty clause "*For late delivery not exceeding 15 days, a deduction of 1 % of the contract price per day late, to a maximum of 15 %.*" [*CE 1, p. 12, para. 10*]. Respondent delivered goods 5 days after the stipulated delivery date [*CE 1, p. 12, para. 3; AA, p. 7, para. 17*]. Therefore, it is obliged to pay 1 % of the contractual price for 5 days, i.e. USD 5,500 x 5 days = USD 27,500 to Claimant because the agreed clause is a contractual penalty [**1.**] and as such it is effective even after the avoidance of the Contract [**2.**].

1. Claimant and Respondent agreed on contractual penalty for late delivery

106 Even though the Tribunal may consider the contractual provision as a price reduction, such interpretation is not possible for the following three reasons.

107 Firstly, price reduction under Art. 50 CISG only applies if the goods do not conform to the contract, not in the cases of late delivery.

108 Secondly, even if the calculation is based on the purchase price, this does not mean that the clause is price reduction. It is up to the parties to use their contractual freedom and choose whatever method to calculate penalty [*Russian case II; Milk Packaging Equipment case*]. In this case parties have simply chosen to use calculation based on the contractual price. Such method is especially useful and fair, because the penalty is based solely on the contractual price.

109 Thirdly, under Art. 8(1) CISG the intent of the parties should be taken into account. The contractual price was paid by L/C. If the clause served as a tool to calculate price reduction or increase, payments via L/C would make no sense. If the goods were delivered earlier, L/C would not suffice for payment of the increased purchase price. Similarly, in case of late delivery the bank would follow strict compliance doctrine and refuse to pay any amount. It is highly unlikely that the parties intended to negotiate such a measure.

110 For all these reasons, deduction of the price stipulated in the Contract was used as a tool not to provide discount of the purchase price for late delivery, but to calculate penalty for the delay.

2. Contractual penalty is valid and remains effective even after the avoidance of the Contract

111 The Contract is governed primarily by the CISG, supplemented by UNIDROIT Principles which are further supplemented by applicable domestic law [*CE 1, p. 13 para. 20*].

112 Though questions of validity are generally not governed by CISG [Art. 4 CISG]. Nonetheless, validity of penalty clauses should be determined exclusively by using the party autonomy doctrine [Art. 6 CISG] and general principle of compensation of losses under Art. 74 CISG [*Zeller*]. Thus, penalty clauses should be valid no matter what the otherwise applicable national law is [*Hachem; Schwenzer/Schlechtriem, p. 1104; Zeller; Foamed Board Machinery case*].

113 Such approach secures uniform interpretation of the CISG and promotes its uniformity as required by Art. 7(1) CISG and recommended in *Explanatory Note*. The purpose of CISG is better fulfilled if it is interpreted in a consistent manner in all legal systems [*Explanatory Note*], especially regarding the most common provisions in international commercial contracts, such as penalty clauses. This can be achieved only if the validity of contractual penalties is assessed in accordance

with the CISG general principles. The use of various national laws would lead to contradicting results.

114 Moreover, the parties agreed on the application of UNIDROIT Principles [*CE 1, p. 13 para. 20*] which supplement CISG [*Garro, p. 1149 et seq.*]. Art. 7.4.13 UNIDROIT Principles states that aggrieved party is entitled for sum which was agreed for non-performance irrespective of its actual harm if it is not excessive. This provision enables the parties to incorporate penalty clauses in their international sales contracts. This is by its virtue definition of penalty clause. Therefore, penalty clauses are valid pursuant to UNIDROIT Principles.

115 The Tribunal should not analyse otherwise applicable national law, because the uniform solution can be achieved both under CISG and UNIDROIT Principles [*Garro, p. 1159*].

116 Art. 81(1) CISG states that "*avoidance does not affect any provision of the contract [...] governing the rights and obligations of the parties consequent upon the avoidance of the contract.*" Therefore, despite the avoidance of the Contract the penalty clauses was not affected and remained effective [*Berger, p. 499; CISG ACO No. 9; Liu I, para. 2; Schlechtriem/Schwenzer, p. 1104; ICC case 9978; Manufactured Articles case*].

117 In conclusion, Claimant and Respondent arranged for contractual penalty for late delivery. Principles of CISG and UNIDROIT Principles give sufficient grounds to rule on the validity of such clause. Moreover, such clause was in no way affected by the avoidance of the Contract. Since Respondent delivered polo shirts late, it is required to pay the contractual penalty.

C. Claimant is entitled to all damages claimed

118 Claimant filed two claims for recovery of damages in the total amount of USD 1,550,000 which it incurred from the settlement with Doma Cirun in the amount of USD 850,000 and the settlement with Oceania Plus in the amount of USD 700,000.

119 Under Art. 74 CISG, a party has the right to be placed in the same economic position where it would have been if the Contract had been properly performed [*Saidov 2001, p. 55*]. Claimant will show that the claims for damages are legitimate under Art. 74 CISG, i.e. they arose from the breach of the Contract, represent a real loss and were indeed foreseeable. Furthermore, Claimant will also prove that the claims are reasonable [*CISG ACO No. 6*] and that it mitigated its losses [Art. 77 CISG].

120 Claimant reiterates that by using child labour Respondent fundamentally breached the Contract. Both settlements, with Doma Cirun and Oceania Plus, are direct consequences of such infringement. It is conclusive that the first two requirements of legitimate claims for damages are

met. In the following Claimant will therefore only argue that damages were foreseeable [**1.**] and claims are reasonable [**2.**].

1. Damages paid by Claimant to Doma Cirun and Oceania Plus were foreseeable

121 Under Art. 74 CISG, a party in breach is liable for the damages which it foresaw or ought to have foreseen at the time of the conclusion of the contract. It is important to state that "*foreseeability does not refer to certain sum of money* [...], *but to possibility of a loss as a consequence of the breach of contract*" [*Liu II, para. 960*]. Therefore, it is not an imperative for Respondent to have foreseen the exact amount of loss but just the possibility of loss caused by its breach of the Contract.

122 The country of Oceania prides itself on its policy of being very ethical [*AA, p. 8, para. 20*]. It is obvious that any business person connected to this country would suffer extensive losses if the public were to discover that such person is involved in operations using child labour. Due to its previous dealings with Claimant and other companies from Oceania Plus group, and due to the knowledge of their attitude towards child labour, Respondent should have foreseen that using child labour would result in significant losses to all the companies involved.

123 Furthermore, if a seller is aware the buyer intends to resale the goods, he should also foresee damages which might arise from the resale [*Russian case II*]. Respondent was aware that the goods were intended for further resale by Doma Cirun [*PO 2, p. 53–54, para. 16*]. In such situation, Respondent should have foreseen that failing to perform its obligations towards Claimant; it will have to recover the losses suffered by Claimant as a result of the settlements with Doma Cirun.

124 Loss of goodwill is always compensable if it leads to material loss [*Saidov 2008, p. 58; Video Recorded case*]. As the consequence of the child labour affair Oceania Plus' goodwill was heavily hit. This was reflected by 25 % drop in Oceania Plus' share price, wiping hundreds of millions of dollars [*AA, p. 8, para. 21*]. Respondent was very well aware of the Contract and its provisions. It follows from the "policy clause" that Respondent was a subsidiary of Oceania Plus and that Oceania Plus is highly ethical company. As a result, Respondent should have foreseen that any unethical behaviour will adversely affect Oceania Plus and its goodwill.

125 Claimant has shown that both the loss of Doma Cirun and Oceania Plus were indeed foreseeable for Respondent. The basis of the damages is therefore established.

2. The settlements of Claimant's disputes were reasonable

126 If a contractual breach results in disputes between the aggrieved party and third persons, the settlements of such disputes, if reasonable, represent legitimate damages which are to be borne by

the party in breach [*Tinplate case*]. Such approach is consistent with the number of court decisions requiring damages to be reasonable in order to be awarded under CISG, although Art. 74 does not expressly require a test of reasonableness [*Pace Review, p. 51*].

127 Because of Respondent's non-compliance with its contractual obligations towards Claimant two disputes have arisen which were ultimately settled.

128 Firstly, on 15 September 2011 Doma Cirun began arbitration proceedings against Claimant in accord with the arbitration clause in their contract [*AA, p. 9, para. 26*]. The asserted claim was for USD 1,825,000. To mitigate the possible outcome, Claimant engaged in the settlement negotiations with Doma Cirun. Eventually, on 14 January 2012, an objectively very favourable and fair agreement was reached [*AA, p. 9, para. 27; PO 2, p. 56, para. 29*]. Claimant finally settled for USD 850,000; thus, effectively reducing the potential loss to less than a half of the original claim.

129 Secondly, Oceania Plus faced law suits brought by its investors claiming USD 15,000,000 in total. It managed to settle these claims for as little as USD 700,000 which is merely a 4.6 % of the original claim [*AA, p. 9, para. 28*]. Oceania Plus in turn sued Claimant to recover this amount [*AA, p. 10, para. 29*]. After getting independent legal advice Claimant recognized its obligation and reimbursed Oceania Plus in full for this settlement [*PO 2, p. 56, para. 29*].

130 To summarize, both claims represent only a fraction of Doma Cirun's and Oceania Plus' legitimate claims; and therefore, cannot be considered unreasonable.

131 In conclusion, because Claimant has proven all necessary conditions to legitimately claim the reimbursement of its settlement with Doma Cirun as well as its settlement with Oceania Plus, it is entitled to full recovery of these damages.

Regarding the raised claims, Claimant respectfully asks the Tribunal to rule that following are substantiated. Firstly, Claimant is entitled to the restitution of the purchase price, because it rightfully avoided the Contract. Secondly, Claimant is entitled to the contractual penalty, because Respondent delivered the polo shirts late. Finally, Claimant is entitled to reimbursement of settlements with Doma Cirun and Oceania Plus, because these damages were foreseeable and reasonable.

Request for Relief

In light of the submissions made above, Claimant respectfully requests the Tribunal in this stage of proceedings to rule that:

(1) Mr. Short's witness statement is inadmissible if he does not appear at the hearing;
(2) the parties did not amend the Contract;
(3) Respondent breached the Contract by using child labour in at least one of its plants;
(4) Respondent's breach was fundamental, authorizing Claimant to avoid the Contract in its entirety;
(5) all claims raised are substantiated.

On behalf of Claimant

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MALANÍK Michal	ŠLAMPA Martin	THIELOVÁ Linda
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