

## 13<sup>th</sup> Intercollegiate Negotiation Competition

### Problem

(October 1 Version)

1. Negoland is a republic with a population of about 60 million occupying some 500,000 square kilometers of land. Thanks to its vast land and bountiful natural resources, Negoland is a world-renowned producer and exporter of agricultural and agri-food products. Winemaking, in particular, has been thriving for decades with wineries producing high-end wines scattered across the country. Negoland also boasts robust automotive, chemical, pharmaceutical, cosmetics and tourism sectors, and together with agriculture, the nation generated a GDP of about US\$2 trillion in 2013. From the 16<sup>th</sup> century to the 19<sup>th</sup> century, Negoland actively explored overseas territories and achieved colonial expansion, resulting in a number of colonies under its control around the world by the 19<sup>th</sup> century. With a newly found sense of nationalism, however, all of its colonies gained independence in the 20<sup>th</sup> century. Negoland has been in close and cordial terms with most of its former colonies. Many of them enjoy solid economic growth, which owes partially to active investment by Negoland-based companies and the economic assistance offered by the government of Negoland. Active trading between Negoland and its former colonies, which are now developing nations, also contribute to the stable economic development of Negoland. The citizens of Negoland are strongly interested in environmental issues. Negoland's environmental regulations are considered strict by any international measure. Negoland has rolled out a series of strict laws and ordinances to combat environmental pollution caused by corporations, which now face exorbitant fines if the new, tighter standards for air pollution and water discharges from factories are not met. The government may even press criminal charges against senior management if they willfully disregard a corrective order by the government and continue to pollute air and discharge waste water beyond the levels allowed by the standards. One act also requires current owners to bear the cost of soil de-contamination, if soil is contaminated by factory operations.
2. Arbitria is a republic with a population of about 80 million and a land size of about 300,000 square kilometers. Its key industry is manufacturing. Arbitria is home to a number of companies with world-renowned technology in the chemical, mechanical, automotive, electronic and pharmaceutical sectors, as well as others. Arbitria's citizens enjoy a high standard of living, as attested by its GDP of about US\$3 trillion (as of 2013). In the early 20<sup>th</sup> century, Arbitria waged war against neighboring nations in an attempt to conquer them by force and was defeated. The war caused serious damage and sorrow

to Arbitria and its neighbors. Arbitria has acted on the lessons learned, and its constitution upholds the fundamental principle of pacifism and renounces the use of armed forces for war or as a means of settling international disputes. Recently, the environmental regulatory agency of Arbitria submitted a new regulatory proposal requiring thermal power plants and large factories in the county to cut their CO2 emissions by 30 percent from the current level by 2030. About 60 percent of the citizens support this initiative, but the industrial sector criticizes this proposal as creating too great a burden on the industrial sector of Arbitria, which in turn may trigger an economic slowdown. Another issue faced by Arbitria is its shrinking, aging population with a low birth rate. Its population began to diminish in 2012, creating concerns over the negative effects that loom on its horizon, such as a slowdown in domestic demand and labor shortages.

3. Negoland and Arbitria are situated about 5,000 kilometers apart from each other separated by a sea. The two countries enjoy good relations, as evidenced by active exchanges of goods and services in addition to mutual investment. Although they do not belong to the same free trade or economic partnership agreements, discussions aimed at a bilateral economic partnership were initiated in 2012. The predominant view is that the two are likely to reach an agreement by the end of 2015.
4. Red Corp. is a company in Negoland that makes and sells beverages. It was established in 1980 by Pat Red, a Nego national. Pat Red was born into an extremely wealthy family in Negoland. Upon graduating summa cum laude with a degree in Agriculture from Negoland University, the most difficult school to get into in the nation, Pat joined Negoland Pharmaceuticals, the leading pharmaceutical company in Negoland, in 1965. At Negoland Pharmaceuticals, Pat belonged to the R&D Department. When his parents passed away in 1979, leaving behind a significant estate, Pat decided to put his college-time dream of “making people happy through food” into practice and went on to establish Red Corp. in 1980 by investing his own funds. He decided to stake his life on chocolate production, simply because he loved chocolate, and embarked on research on chocolate, beginning with in-depth studies of the production of cacao beans -- the main ingredient of chocolate. A few college friends of Pat’s offered help. Three years later, Pat succeeded in the production of chocolate, which was not only extremely delicious but did not cause weight gain. In 1983, Red Corp. began marketing this product as “R-Choco” bars in Negoland. Sales of R-Choco, however, were lackluster. Red Corp. only sold one million R-Choco bars in 1983. Pat’s subsequent attempts at improving flavors and changing package designs were not fully translated into a substantial increase in sales, which in 1984 amounted to 1.5 million bars. R-Choco was loved by a select segment of consumers in Negoland, but its sales remained in the vicinity of 1.5 million to 2 million bars.

5. A major turning point occurred in 1987, when two employees joined Red Corp. They were George Sullivan, 10 years younger than Pat, and Carolina Chen, 12 years Pat's junior, both hailing from the same alma mater as Pat. Chen demonstrated the confectionery mastery she had gained while being trained under a famed pâtissier in Negoland, and successfully transformed Red Corp.'s plain, dull chocolate bars into an artistic line of chocolate with appealing flavors and tastes as well as colors and shapes. Sullivan too made a strong contribution to the company by utilizing his exceptional marketing savvy. In 1989, Pat, Chen and Sullivan worked together to come up with a series of products known as "R-Choco Neo," each of which was based on a slightly different formula. The line included, among others, a chocolate designed to boost the brain's ability and improve concentration, great for study or work, and a chocolate that relieves stress. Later on, each function-specific chocolate evolved into its own series offering a variety of flavors and tastes. The range of chocolate offerings too was broadened from relatively inexpensive chocolate bars to high-end bonbons. Chocolate bars were priced at US\$2 to US\$3 per bar, while bonbons were sold at US\$1 to US\$4 apiece. High-end, handmade chocolate was marketed under the "R-Choco Premium" brand. To aggressively market the products beyond Negoland, Red Corp. approached department stores in Japan and United States and heavily promoted its products by running massive ads in magazines. As a result of these efforts, the R-Choco Neo and R-Choco Premium lines posted explosive sales after 1990 in the United States and Japan, not to mention in Negoland. Even after their success, Red Corp. remained committed to improving chocolate flavors and tastes year after year, which helped R-Choco rise to its current prominence as an internationally renowned chocolate brand.
6. Red Corp. grew significantly by riding on the success of its R-Choco Neo and R-Choco Premium products. Red Corp. is not a listed company and no financials are disclosed, but Red Corp. is believed to be highly profitable. After 2000, the profits reaped from the R-Choco Neo and the R-Choco Premium lines were used to finance the acquisition of companies in a variety of business sectors. The acquisitions were Pat's idea. He wanted to diversify Red Corp.'s business, in an attempt to reduce its reliance on the chocolate business and to accelerate Red Corp.'s growth by expanding into areas with growth potential through aggressive investment. Specifically, it bought 100% shares of Nego Wine Co., a well-known wine concern of long standing in Negoland, and made it a subsidiary of Red Corp. in 2000. Nego Wine Co. is an internationally known wine and cheese dealer, and the takeover attracted much media attention worldwide. In 2003 Red Corp. bought Nego Dairies Inc., a leading producer of milk and dairy products in Negoland. Now a subsidiary of Red Corp., Nego Dairies Inc. holds a 20 percent share of the domestic milk and dairy market. It does not export its products overseas. Further in 2007, Red Corp. acquired 100% shares of Spirit Corp., a European company known

internationally as a sportswear and athletic gear manufacturing brand. All M&A's by Pat turned out to be extremely successful, as demonstrated by the solid operating results of its subsidiaries. The Red Group is outlined in Exhibit 1.

7. Blue Inc. is an Arbitrian company that engages in food and pharmaceutical businesses. Established in 1917 by George Blue, grandfather of the current CEO, it initially made toffees and cookies and expanded into milk production and sales in 1940. Blue Inc.'s milk is immensely popular in Arbitria and has contributed to the company's growth. In 1950, Blue Inc. launched a snack product line, which also recorded robust sales. Further expansion followed with the production and marketing launch of yogurt in 1971 and ice cream in 1980. Known for high quality and low prices, Blue Inc.'s snack products are widely popular among Arbitrian consumers. Since 1990, Blue Inc. has been active in seeking overseas sales expansion for its snack and dairy products, focusing its efforts on Alpha and Beta, two neighboring countries of Arbitria, for exports and local production of select products.
8. Blue Inc. has been listed on the Arbitrian Stock Exchange since 1985. It entered the pharmaceutical business in 1990. The pharmaceutical division produces mouthwash and antibacterial agents, among others. Its current focus is on the development and production of generic drugs in a move to capture opportunities that opened up in 2008 when the Arbitrian government began promoting the accelerated use of generic drugs. Since the generic drug market of Arbitria is highly competitive, Blue Inc. has yet to establish itself as a major force in the field. However, its sales are growing at a consistent pace, albeit slowly.
9. Another business area Blue Inc. ventured into was the beverage business. The sector is notorious for intense competition and the short product life cycle of beverages, and from the start in 2000 Blue Inc. found it difficult to come up with successful products on a consistent basis. The pattern changed in 2008 when Blue Inc. introduced the Blue Energy sports drink, which helps people replace water and minerals lost during exercise, and its sales in Arbitria have been stable. In 2010, Blue Inc. rolled out Blue Slim, a beverage that helps block fat absorption and helps dissolve and burn fat in the body. Arbitria's Ministry of Health and Welfare has a program of designating foods and beverages whose health benefits are scientifically confirmed as "Designated Health Foods" and Blue Slim became a Designated Health Food when it was released in 2010. This designation may have contributed to healthy sales of the product in Arbitria. However, Blue Inc. has no other long-lasting hit products other than Blue Energy and Blue Slim.
10. Instrumental in the R&D work for both Blue Energy and Blue Slim was Bob Orange, who was the director in charge of R&D. Orange was class valedictorian of the University of Arbitria, a prestigious university in Arbitria, and is an exceptionally gifted scientist with an ardent passion for laboratory work and research. Orange joined Blue Inc. in 2006.

Orange and the CEO of Blue Inc. met at an alumni association function of the university. Although Orange is younger than the CEO, the two, who grew up in the same part of the country, hit it off quite well and established a close personal bond. The CEO of Blue Inc. took advantage of this relationship to successfully persuade Orange to join his company.

11. In 2010, Blue Inc. underwent an organizational split, creating four subsidiaries, each responsible for a specific line of business, i.e., confection, dairy, pharmaceuticals and beverages. The four subsidiaries, namely Blue Sweets (confection), Blue Dairy (dairy products), Blue Medicine (pharmaceuticals) and Blue Drink (beverages) were wholly owned by Blue Inc. In addition to these lines of business, Blue Inc. also imports food products from abroad, and the head office of Blue Inc. is in charge of this business. Blue Inc. is outlined in Exhibit 2.
12. In the second half of 2011, Red Corp. decided to look into the possibility of further business expansion. Red Corp. had expanded by taking over companies through M&A's. Therefore, for the new wave of business expansion, Red Corp.'s basic action principle called for the acquisition of companies through M&A's, targeting business concerns not engaged in the same business lines as Red Corp.'s existing businesses but poised to create new synergies. Based on this principle, Red Corp. shortlisted several candidate companies after internal discussions, with the help of advice given by the M&A Advisory Division of Negoland Bank, the largest bank in Negoland, with which Red Corp. had a business relationship. It was then decided that Red Corp.'s first pick would be Blue Drink of Arbitria. Red Corp. had had no business dealing with Blue Inc. but Red Corp. singled out Blue Drink as its first choice because Blue Drink's Blue Energy sports drink and the sportswear and sporting gear lines handled by Spirit Corp., a Red company, would mutually help expand each other's customer bases. In addition, the target customer group of Blue Slim, which helps dissolve and burn fat, is identical with the customer base of the R-Choco Neo series, whose selling point is various health benefits, including, among others, weight reduction. On top of these reasons for interest, Negoland Bank informed Red Corp. that Blue Inc. might let go of Blue Drink, one of Blue Inc.'s four subsidiaries, as Blue Drink had failed to achieve strong sales growth and suffered from rising R&D expenditures, compounded by dwindling profitability. According to Negoland Bank, Blue Inc. might be interested in selling off Blue Drink to re-allocate its corporate resources to the remaining three subsidiaries with better growth potential.
13. Red Corp. asked Negoland Bank to approach Blue Inc., to initiate an exploratory dialogue. Negoland Bank contacted Blue Inc. through its branch office in Arbitria. Blue Inc. replied that it would consider selling Blue Drink, if the terms and conditions were acceptable to it. On January 16, 2012, the CEO of Red Corp. and the CEO of Blue Inc. held a conference at the head office of Blue Inc. to discuss the transaction. Blue Inc.

selected Arbitria Securities, the leading investment bank in Arbitria, as its financial advisor for the transaction.

14. The conference between Red Corp. and Blue Inc. took place at Blue Inc. on January 15, 2012. Red Corp. sent, among others, Pat Red, CEO; Tim Houck, CFO; and K. Nomura of Negoland Bank. Blue Inc. was represented by Kelly Blue (Kelly Blue is the son of George Blue), CEO; Ali Diamond, CFO; and Yuki Ohta of Arbitria Bank.

15. The following exchanges took place during the meeting on January 15, 2012:

Red: Thank you very much for meeting with us.

Blue: Thank you very much for coming all the way.

Red: As Negoland Bank already informed you, we are interested in buying Blue Drink, one of your subsidiaries. We have no experience handling beverages. However, we are planning business expansion for further growth of our group and the beverage business is a strong candidate for our new business. We believe Blue Drink's key products, Blue Energy and Blue Slim, are sure to create synergies with our existing sporting goods and food divisions. Also, on this occasion, we would like to expand our business relationship.

Blue: I see. After Negoland Bank contacted us, we carefully considered your offer. To be honest, it will all depend on the terms of your offer. Our beverage business is doing well, with two key products – Blue Energy and Blue Slim – on the market. They have potential for doing even better with further R&D and expanding delivery channels. As you may know, we have other businesses to attend to, like confection, dairies and pharmaceuticals, and your offer came in at the right time, as we are considering a reshuffling of our entire range of businesses to concentrate our resources on the confection, dairy and pharmaceutical products. I think you're right to assume that you will gain synergies if you buy Blue Drink. Probably, you may be better positioned than us to help unleash the potential of Blue Drink.

Red: I agree with you. We believe we are ready to create greater value out of Blue Drink, if Blue Drink becomes a part of our group. Given the potential of Blue Energy and Blue Slim, we would like to produce them at our plants in Negoland as well, and eventually sell them in overseas markets.

Blue: Thank you for thinking so highly of our Blue Drink and its potential, and I don't mind considering your offer with a future-oriented viewpoint.

Red: So, may I assume you are ready to talk about specifics of the sale?

Blue: Yes.

Nomura: Since Red Corp. and Blue Inc. have agreed to take the discussion to the next level, let me explain what I will do. I will prepare a non-disclosure agreement, which must be signed by both Red Corp. and Blue Inc. I will

then submit to Blue Inc. a list of information Red Corp. needs. Upon review by Red Corp. of the information furnished by Blue Inc., I will prepare and submit to Blue Inc. a draft letter of intent. Any problem?

Ohta: Then, we at Arbitria Securities will work out details with Negoland Bank to decide on what forms to use and how information will be communicated.

16. After the non-disclosure agreement was signed by Red Corp. and Blue Inc., Red Corp prepared and submitted to Blue Inc. a list of basic information on Blue Drink required by Red Corp. Blue Inc. prepared and forwarded the requested information to Red Corp., which examined it. On March 15, Red Corp.'s team visited Blue Inc. and interviewed Diamond, President of Blue Inc., and Ruby, CEO of Blue Drink. After reviewing the findings in the submitted written information and the results of the interviews, Red Corp. prepared a draft letter of intent upon consulting with Negoland Bank. The draft letter of intent, as shown in Exhibit 3, was sent by Negoland Bank to Arbitria Securities on April 16.

17. On April 20, Ohta of Arbitria Securities phoned Nomura of Negoland Bank.

Ohta: We received the draft letter of intent. We studied it with Blue Inc.'s team. Red Corp.'s low valuation of Blue Drink really shocked us. We had the impression that Red Corp. thought very highly of Blue Drink, but the offer Red Corp. made more than canceled out the good rapport that seems to have been going on. Blue Inc. is not desperate, and it would be extremely difficult to finalize the deal at that price.

Nomura: I believe the valuation was made after careful examination of the information submitted by Blue Inc. But Blue Inc. has not reviewed the detailed materials on Blue Drink and there should be some room for negotiation. How about discussing the pricing issues further after the letter of intent is signed by the two parties and due diligence is completed?

Ohta: All right. But please inform Red Corp. that it needs to offer a lot more before the deal becomes acceptable to Blue Inc.

18. Due diligence was performed between May 25 and September 30. Red Corp. reconsidered the enterprise value of Blue Drink based on the results of the due diligence. On October 15, Red Corp. held a meeting with Blue Inc. Participants were Pat Red (CEO) and Tim Houck (CFO) and K. Nomura (Negoland Bank) representing Red Corp. and Kelly Blue (CEO), Ali Diamond (CFO) and Yuki Ohta (Arbitria Securities) representing Blue, Inc.

19. The following conversation took place during the meeting on October 15:

Red: Thank you for helping us do our due diligence.

Blue: You're more than welcome. Did your due diligence find any significant issues with us?

Red: We didn't find any issue that stands in our way. We studied the pricing once again with the result of our due diligence, etc., and we would now like to offer you US\$800 million. ,

Blue: What are the reasons for US\$800 million?

Red: We decided the price after we considered various elements such as the result of the discount cash flow analysis and EBITDA multiple method.

Blue: We valued Blue Drink by using the discounted cash flow method based on future cash flows of Blue Drink, which was further based on the hypothetical premise that Blue Drink would remain under Blue Inc.'s control, and our estimate was more than US\$1 billion through this method. If you acquire Blue Drink and reap synergies, Blue Drink's values will be sure to rise even more.

Red: Our valuation is based on our business plan for Blue Drink, which is outlined in Exhibit 4, and this business plan was based on the medium-term business plan prepared by Blue Drink. We at Red Corp. plan to move right ahead into full-fledged production of Blue Energy and Blue Slim in Negoland after purchasing and quickly converting the idle factories on the premises of Nego Dairies Inc. to make them ready for the production of the two drinks. For sales in Negoland and overseas, we plan to tweak the flavors and formulas of the two drinks and market them under the product names of Red Energy and Red Slim.

Blue: It seems to me that your business plan doesn't fully reflect the synergies that you expect to gain.

Red: It's not easy to estimate the extent of synergies. Besides, everyone has a different view on synergies.

Ohta: How about agreeing on the upfront price of US\$900 million and a certain contingent payment, which will be payable if Blue Drink does better than the figures indicated in Exhibit 4?

Red: This could be a solution to consider, if you can't agree on future cash flows of Blue Drink.

Nomura: How about an upfront price of US\$800 million and not US\$900 million? If you insist on US\$900 million, we'll have to consider a mechanism that allows us to request a refund if it underperforms.

Blue: All right. We can go with the upfront price of US\$800 million plus contingent payments of some sort.

Ohta: US\$800 million is about 8.42 times of EBITDA. Therefore, may I propose to that, for 2013 and 2014, if EBITDA exceeds US\$110 million, Red Corp. will pay the amount obtained by multiplying 8 to the excess amount.



Red: Your proposal for the contingent payment is acceptable.

Blue: I hope you won't manipulate operating results just because better performance means higher contingent payments.

Red: Never. But please understand that substantial initial investment is required in the form of facilities and advertising in order to start a new business in Negoland.

Kelly: We won't make a fuss about your reasonable investments.

20. Other topics covered during the discussion were as follows:

Red: I have a special request to you regarding Mr. Bob Orange, who is in charge of Blue Drink's R&D Department. Our management interview results indicate that his presence is extremely critical to the future of Blue Drink. In the past, Mr. Orange led the product development for Blue Energy and Blue Slim. He is working on improving those products and I expect he will do so in the future. The beverage market is filled with competitors, and Blue Energy and Blue Slim will need improvements at some point or another. Also, the products require some taste and formula tweaking to better appeal to Negoland's market and overseas. Plus, new products must be developed. With all these requirements in mind, it is crucial for us and for the successful consummation of this transaction to have Mr. Orange remain on the Blue Drink team. We will give him the same level of work environment, at least, or a better one if possible.

Blue: Orange and I are both alumni of the University of Arbitria, and I'm very fond of him. I want to respect his decision. If he decides to remain with Blue Drink, I hope you'll give him adequate budget for his R&D work and an appropriate work environment to support him.

Red: Of course, we will.

Nomura: Red Corp. is willing to close the deal, only if Bob Orange agrees to continue working for Blue Drink. Would it be possible for you, Mr. Blue, to ask Bob Orange to submit a letter confirming his intention to continue working for Blue Drink?

Blue: We'll ask Orange about what he wants to do. I can assure him that the R&D budget and the work environment you will give him will not be anything less than what Blue Inc. offers now, correct?

Red: Yes.

Kelly Blue met Orange and discussed the issue. "It is very sad to leave Blue Inc., but Blue Energy and Blue Slim are my brainchildren," Orange said. "I will remain with Blue Drink to make my children even better, as long as adequate budget and work environment are provided." Orange then signed the letter, confirming his intention to

- continue working for Blue Drink for at least 3 years after the acquisition by Red Corp.
21. After the October 15<sup>th</sup> meeting, negotiations on details of the stock purchase agreement were held between Red Corp. and Blue Inc. Parallel to the discussions, the two parties had to obtain their respective internal approvals to go ahead with the agreement. Both parties successfully completed these internal approval procedures, and on December 14, 2012, they signed the agreement shown in Exhibit 5. The closing was scheduled for January 15, 2013. On that day, a closing ceremony was held at Blue Inc. and all shares of Blue Drink were transferred from Blue Inc. to Red Corp.
  22. Effective January 15, 2013, Red Drink, formerly known as Blue Drink, became the official name of the company. In Arbitria, Blue Energy and Blue Slim continued to be distributed under their old names, while the products were to be marketed as Red Energy and Red Slim in other countries. The existing production facilities on the premises of Nego Dairies Inc. in Negoland was sold to Red Drink and refitted, which went into operation on April 15 for the production of Red Energy and Red Slim. Red Corp. leveraged its existing sales network, conducted sales promotions directed to the customer base of Spirit, and commenced massive ad campaigns in Negoland.
  23. Nego Drink, a beverage concern in Negoland, heard about the forthcoming release of Red Slim and Red Energy in Negoland and contacted Red, expressing its interest in distributing them as an agent through its own sales channels established for its own products. Nego Drink wanted to distribute the product to retailers through its own distribution channels and to sell it through vending machines it owned. Soft drink vending machines are everywhere in Negoland, where soft drink sales through vending machines account for a high percentage. Nego Drink is a leading beverage company in Negoland, with its vending machines all over the country, and its vending machine sales are by far the highest in the country. Nego Drink demanded that it be the sole distributor in the territory of Negoland (Note: Red Corp. is still entitled to sell the product directly to consumers): that the product should not be made available for vending machines owned by companies other than Nego Drink; that the unit wholesale price charged by Red Corp. would be 60 percent off the standard retail price in light of the mass purchases to be made by Nego Drink; and that the contract should be good for five years. In a way, Nego Drink's proposal sounded attractive to Red Corp., where the issue of building its own sales channels for the beverage product was under discussion. However, Red Corp. was concerned about the little profit it would make at the price of 60 percent off the standard retail price as proposed by Nego Drink. In addition, Red Corp. hesitated to sign a five-year contract, as it would be more comfortable signing a shorter contract, given the uncertainty of Nego Drink's ability to sell Red Slim, which may be categorized as health foods. Red Corp. decided to make a counter-proposal, which included, among others, a two-year term of the contract, the unit price at 50 percent off

the standard sales price and a minimum purchase volume of 500,000 units per year for the initial period. Nego Drink agreed to the length of the contract and the minimum purchase volume, but it insisted on a 60-percent discount from the standard retail price for the unit price payable by Nego Drink.

24. Then, there was a new offer, from Negoland Bottlers Inc., for distribution of Red Slim and Red Energy. Negoland Bottlers Inc. is a leading beverage distributor of the same scale as Nego Drink. It has an excellent network with retailers such as supermarkets, and in the beverage industry, it has been considered to have a sales force that is approximately equal to Nego Drink. For terms and conditions, Negoland Bottlers offered 2 years contract, 50% of the standard retail price and a minimum purchase volume of 400,000 units per year. However, Negoland Bottlers said it would be ready to compromise a little more about the minimum purchase amount.
25. Both Nego Drink and Negoland Bottlers requested to be the sole distributor in Negoland, and there was no room to compromise on this point. In Red Drink, there were opinions that there should be a competition between the two companies. But, after all, competition was not made and it was decided to appoint Nego Drink as the distributor by the voice of authority of Pat Red. The contract terms were 40% of the standard retail price, minimum purchase volume of 500,000 units per year and 2 years contract. Pat Red's following comment was decisive: "I know the president of Nego Drink very well. He was my classmate in the university. We can rely on him. Though the sales price in the first two years is low, it will be more important for our long-term interest to achieve high popularity and penetrate the market with using Nego Drink, a trustworthy distributor."
26. On March 5, 2013, Red Drink signed a distributorship agreement with Nego Drink, and in accordance with the agreement, from May 15, Red Energy and Red Slim went on sale at retailers on Nego Drink's distribution routes and at vending machines owned by Nego Drink.
27. Sales of Red Energy and Red Slim grew steadily thanks to the powerful sales channels of vending machines of Nego Drink, as well as its sales savvy. In October 2013, the growth began to stop. Nego Drink, which tried to identify the reason for such brake on the growth, produced survey results indicating that the flavor and taste of Red Energy and Red Slim were slightly off the mark to fit the preferences of the Nego people. The CEO of Nego Drink informed Red Corp. that in his opinion, the ad campaigns run by Red Corp. combined with the strong vending machine network of Nego Drink would have driven sales even higher, and he concluded that the factor in the way of elevating sales to an explosive level must be the flavor. In fact, Red Drink received comments from many consumers suggesting their preference for "a lighter, more refreshing taste." Red Drink addressed the issue in October, and its R&D team headed by Bob Orange took up the

challenge of coming up with an improved flavor in three months.

28. The M&A transaction centering on Blue Drink as described above led to a new transaction between Red Corp. and Blue Inc. This concerned the importation and sale of Red Corp.'s chocolate by Blue Inc. for the Arbitrian market. Prior to that, Red Corp.'s chocolate had been featured in some informational magazines in Arbitria, despite the absence of shops well-stocked with Red Corp.'s line of chocolate items there. Red Corp., for its part, targeted Japan and the United States rather than Arbitria as the promising overseas markets for its chocolate, but it was contemplating entering the Arbitrian chocolate market eventually. The absence of chocolate in the range of food products produced by Blue Inc.'s confectionery division also supported the deal, as Red Corp.'s chocolate would not directly compete with any of Blue Inc.'s food products. Red Corp. and Blue Inc. started discussing the importation of Red Corp.'s chocolate in November 2013.
29. Blue Inc. first approached some leading department stores in Arbitria with which it had business relationships (supply of confectionery products) to sound them out. All of them expressed interest in carrying Red Corp.'s chocolate products and stocking Red Corp.'s chocolate in time for the St. Valentine's Day candy giving season, if at all possible (Note: In Arbitria, there is a custom of St. Valentine's Day similar to that in Japan, that is, females gift chocolate to males on February 14 each year). On December 10, 2013, it was agreed, albeit on rather short notice, that Blue Inc. would import chocolate worth US\$3 million in wholesale price from Red Corp. (primarily high-end products priced at US\$3 to US\$4 apiece) and sell it to leading department stores in Arbitria for their St. Valentine's Day candy giving season. It was further agreed that the deadline for shipping goods would be no later than January 10, to ensure the delivery of chocolate to the department stores on or before January 31, as promised by Blue Inc. to allow ample time of sales for the department stores. The shipping deadline of January 10 made sense as it normally takes approximately 15 days for goods to travel from Negotown, the capital city of Negoland, to Abu-Abu, the capital city of Arbitria, by sea (both cities face on ports). Terms of trade were CFR (Incoterms® 2010), payment by L/C. Blue Inc. decided to ask Arbitria Bank, with which it had a business relationship, to issue the letter of credit. Red Corp. told Blue Inc. that Negoland Bank should be the advising bank for the purpose of the letter of credit to facilitate the transaction. When Blue Inc. was informed the desire of Red Corp., it replied that it usually uses NegoNego Bank as an advising bank when there is no specific request, but it will make Negoland Bank the advising bank, since Negoland Bank was a correspondent bank of Arbitria Bank. The agreement signed by Red Corp. and Blue Inc. regarding the sale of chocolate is given in Exhibit 6.
30. Red Corp. manufactured chocolate marked for the sale to Blue Inc. The chocolate was a

custom-made, limited production St. Valentine's Day version, specially manufactured for exports to Blue Inc. For transportation of the goods, Red Corp. made arrangements for a regularly scheduled ship scheduled to depart Negotown on January 10 and arrive at the Port of Abu-Abu on January 20. Meanwhile, Blue Inc. requested Arbitria Bank to issue a letter of credit on December 19. Then Blue Inc. informed Red Corp. that a request to issue a letter of credit had been filed with Arbitria Bank. On December 20, Arbitria Bank issued the letter of credit, which is shown in Exhibit 7, and advised Negoland Bank of the issuance. At Negoland Bank, the experienced clerk who normally handled correspondent tasks was by chance on sick leave, and an inexperienced clerk, who received the advice instead, put away all related documents in his desk without performing any needed tasks. Because businesses in Negoland were closed for Christmas from December 21 to December 26 and again for the New Year's holidays from December 30 to January 3, no one noticed that the advice of the letter of credit had not been processed

31. Busy preparing the chocolate for shipment to meet the obligations under the contract, Red Corp. did not notice until January 7 that the letter of credit has not been advised yet. On January 8, Red Corp. contacted Negoland Bank to find out whether it had received the letter of credit. Negoland Bank could not find the letter of credit right away. Negoland Bank could not find the letter of credit right away. On January 9, Red Corp. pressed Negoland Bank to look for the missing letter of credit once more after presenting the copy of Blue Inc.'s application for the letter of credit that Blue Inc. had filed with its bank, a copy of which Blue Inc. had sent to Red Corp. After all these hassles, the letter of credit was finally advised from Negoland Bank on January 10. It takes two full days at least from the receipt of the letter of credit to the completion of loading. Consequently, Red Corp. missed the regularly scheduled ship that left Negoland on January 10, for which it had booked a space. To aggravate the problem, the next regularly scheduled ship was scheduled for January 20 departure and February 3 arrival. Red Corp. could not charter a ship for delivery to be made before the end of January either.
32. On January 11, Swan, who was in charge of the matter at Red Corp., contacted Emerald, his counterpart at Blue Inc., to discuss how to address the issue. It was through this phone conversation that Blue for the first time knew the fact that the advice of the letter of credit was delayed.

Swan: We have a serious situation here. We planned to ship out the chocolate on this regularly scheduled vessel scheduled for January 10 departure but we missed the ship due to a delay in receiving the letter of credit advice. The next regularly scheduled boat will depart here on January 20, but this won't arrive at the Port of Arbitria until February 3.

Emerald: Really? Why didn't you consult with us earlier? Our delivery to the

department stores would have to be pushed back to February 5 or later, and we would be delayed for the promised delivery date. We would face substantial penalties to the department stores. Once we are forced to pay penalties, we will ask you to compensate us.

Swan: How much are the penalties?

Emerald: A total of US\$2 million according to the contracts.

Swan: In order to meet the delivery date to the department stores, we need to use air cargo, but the freight charge would cost an additional US\$500,000.

Emerald: It would be better than your paying \$2 million in penalties, would it not? Red Corp. failed to meet the shipping deadline, so you should deal with this trouble on your responsibility. It is the fault of Negoland Bank that caused your failure to meet the shipping deadline; later you can seek damages from Negoland Bank, which was responsible for the delay.

Swan: You may be right. I'll arrange for air cargo right away. We will need to book two flights to ship the entire supply.

33. Red Corp. made an arrangement with Negoland Air for two flights to transport the chocolate. Red Corp. paid the freight charge cost US\$500,000 in total to Negoland Air. The first batch was scheduled to leave January 15 and the second batch on January 17. It was decided that the chocolate would be equally divided (i.e., US\$1.5 million worth of chocolate in each flight). The first shipment travelled to Arbitria safely and was handed over to Blue Inc. by Negoland Air on January 18 after successfully going through customs clearance. For the second batch, Red Corp. handed over the chocolate to Negoland Air on January 17 and the chocolate was taken into an aircraft. However, due to a mechanical problem of the aircraft, it became necessary to replace the aircraft. The chocolate was then removed from the aircraft and taken into the cargo warehouse for storage. While the chocolate was in storage, the warehouse was struck by lightning, damaging all the chocolate. All the chocolate totally lost its commercial value. According to the freight agreement between Red Corp. and Negoland Air, the airline is not liable to Red Corp. in a situation like this and the freight charge is not refunded to Red Corp. And neither Red Corp. nor Blue Inc. had taken out insurance covering a case like this. The chocolate was custom-made for Blue Inc. and Red Corp. did not have any suitable chocolate in stock that could replace the destroyed chocolate. As a result, Red Corp. failed to deliver to Blue Inc. the chocolate worth US\$1.5 million, and Blue Inc. was forced to pay US\$1 million in penalties to the department stores. (In accordance with the laws of Arbitria, which govern the contracts between Blue Inc. and the department stores, Blue Inc. may not refuse to pay the penalties.)
34. Blue Inc. sent Red Corp. a letter (shown in Exhibit 8) demanding reimbursement of the penalties amounting to US\$1 million, which Blue Inc. had paid to the department stores.

Red Corp. sent a letter (shown in Exhibit 9) in response, indicating its refusal to comply with the demand and demanding a reimbursement of the charge Red Corp. had incurred for air cargo arrangements (US\$500,000). This was followed by another letter from Blue Inc. to Red Corp. (shown in Exhibit 10). The parties attempted to resolve the issue through negotiations but they have not reached an agreement thus far. The issues presented here will be collectively referred to as the Chocolate Case.

35. Around the same time, a series of problems arose between Red Corp. and Blue Inc. surrounding the M&A. Bob Orange, the head of the R&D department of Red Drink, submitted a letter of resignation effective November 11, 2013. The cause behind his resignation was discord that developed between him and Jo Lee, the new CEO of Red Drink. Jo Lee took over the position on October 15, 2013, because the physical condition of his predecessor had deteriorated. Joe Lee is an elite employee who has attained experience in the personnel department, business promotion department, and planning department of the head office, and it was thought that he would become a senior executive in the near future; but he has almost no experience working in the front line of production and sales. Orange was conducting R&D to improve the flavor of Red Energy and Red Slim to fit them to the preferences of Nego consumers. While Lee insisted that the new, improved Blue Slim to be ready for shipment by early 2014, Orange vowed to spend as much time as needed for repeated lab testing to come up with an acceptable flavor, implying his work would not be completed before the end of 2013. Lee instructed Orange to complete his flavor tweaking work by the end of November 2013, at the latest, for the first shipment of the product to go out as scheduled in early 2014. "Budget has its limits and we can't afford to support your plan of an endless search for perfection," Lee said. Orange told Lee the promise made by Red Corp. that he could do enough R&D work. "I never heard such a promise was made, and besides, you know quite well that everything has its limits," Lee replied. "Don't be like a child. Get back to work now and get your job done by the end of November." Lee's comment infuriated Orange. "Without me, Blue Energy and Blue Slim wouldn't be on the market," Orange retaliated. "I don't need to listen to the silly nonsense of a science moron like you." Orange ignited the CEO's anger. "I am the CEO, and I am ordering you to follow my instructions," Lee declared loud and clear. "Did it ever occur to you that Blue had to sell Blue Drink because you spent too much on your R&D and drove the bottom line down? If you don't follow my instruction, you must resign." "All right, then," Orange replied. "I quit!" Orange wrote his resignation letter on the spot, gave it to Lee and left the office for good. Crane, Director of Corporate Planning at Red Corp., met with Orange to try to win him back. At the meeting, as a condition to withdraw his resignation, Orange sought additional research and development costs and said, "If the budget for the research and development is increased by about 20 percent, I am confident to achieve the satisfactory

result by the end of the year." However, Crane refused the offer and said "you have already sufficient amount of budget for research and development and any increase of the budget is not acceptable." Crane tried to persuade Orange to continue R&D using the available budget effectively, but he didn't change his mind and resigned. As a result of Orange's departure, Red Drink's plan of improving the flavor of Red Energy and Red Slim to realign it with the Negro consumers' taste buds fell through, and no new attempt to change the flavor has been made to date. Moreover, the news of Orange's resignation quickly circulated within the trade, creating a negative impression of Red Energy and Red Slim. This was translated at least partially into lackluster sales of the two products in 2014.

36. In January 2014, Orange joined Arbitria Coffee, a beverage maker in Arbitria. It is the leading maker of coffee-based beverages in Arbitria with US\$1.5 billion sales in 2013 million and a capital of US\$20 million. There, Orange is now charged with the development of diet coffee drinks. Kelly Blue learned of Orange's new job from Sam Jackson, CEO of Arbitria Coffee, at a gathering of Arbitrian business owners. Kelly Blue had known Sam Jackson for a long time. The following conversation took place between Blue and Jackson.

Jackson: Arbitria Coffee hired Orange in a move to focus on the development of a coffee beverage with weight loss benefits, despite a limited R&D budget. For the success of this project, we need additional funding. Would it be possible to get your cooperation in this regard?

Blue: Your project sounds very interesting for our company, which has a pharmaceutical division. Let us help your organization and Mr. Orange develop a diet coffee drink. Blue Inc. may invest US\$5 million in your organization.

Jackson: That would be very helpful. You may have read this in newspapers but we've lost lots of money in overseas ventures lately. Without your help, we wouldn't be in a position to embark on serious R&D. Your investment will resolve such financial problem

Blue: OK, we will consider the investment of 5 million dollars. When we make such investment, we would like to send one person to your Board of Directors.

Jackson: I understand. Thank you by all means. There is one more request. It will take about half a year for us to prepare necessary R&D facilities. During that period, could you kindly allow us to use the research facility of the Central Research Center of your company? Mr. Orange said it would be ideal if we could use the facility of your Central Research Center for the development of new products. Of course, we will pay a fee for use.



Blue: I see. I want to assist Mr. Orange. I will lend you part of the facilities of the Central Research Center.

As a result of the above communication, Blue made US\$5 million investment in Arbitria Coffee and allowed it to use a part of the facility of the Central Research Center. There had been 5 directors in the board of directors of Arbitria Coffee and one board member from Blue Inc. joined the board.

37. The news traveled to Red Corp., which then sent a letter (Exhibit 11) to Blue Inc. Blue retorted in a letter to Red Corp. (Exhibit 12). Please note that the Companies Act of Arbitria defines the term “subsidiary” as a “company whose stock is more than 50% owned by another company or the management of which is substantially controlled by another company,” and the term “affiliate” as a “company on which another company may exercise substantial influence over financial and business policy decisions.”
38. Another issue surfaced. The government of Arbitria revoked the “Designated Health Food” status of Blue Slim. On April 30, 2014, Arbitria’s Ministry of Health and Welfare announced the revocation, which was based on its “finding that overconsumption of the product may prevent the correct functioning of the stomach.” In late March, the Ministry contacted Red Drink and confided the move. Although Red Drink requested the Ministry for an opportunity to have the products re-tested for verification with the involvement of Red Drink before the Ministry’s decision would become final, the Ministry rejected Red Drink’s request and went ahead with the above announcement. Red Drink’s inability to appeal to the Ministry was attributable, in part, to Orange’s departure, as the remaining R&D team was not equipped to effectively deal with the Ministry, let alone convince it to reverse its view. As a result of the revocation, Blue Slim’s sales plummeted to 2/3 of the previous year’s level after May 2014.
39. Later, Red Corp. learned, from Red Drink’s employees, that Blue Drink began receiving complaints from select consumers linking overconsumption of Blue Slim to stomach problems in early 2012. Arbitria’s Ministry of Health and Welfare informed Blue Drink in April 2012 of similar complaints the Ministry received from select consumers. It warned Blue Drink that the Ministry would keep an eye on any new development. From April to May 2012, Blue Drink ran a series of rigorous tests on Blue Slim. It did not confirm any particular stomach problem linked to overconsumption, even when substantial amounts of Blue Slim were consumed day after day. It was reported to the board of directors of Blue Drink that it will need to monitor the matter carefully, fearing that the Ministry of Health and Welfare could take away the “Designated Health Food” label from Blue Slim by siding with consumers suggesting any possibility of upset stomach. It turned out that the existence of such complaints by consumers, as well as the Ministry’s communication with Blue Drink regarding the possible revocation, had been disclosed to Red Corp. in the process of due diligence that started in May 2012.

The due diligence report prepared by Red Corp.'s advisor also contained some statements of relevance as indicated in Exhibit 13. Since Red Corp.'s takeover, it has received similar letters of complaint occasionally but has never been contacted by the Ministry of Health and Welfare.

40. Red Corp. sent a letter to Blue Inc. regarding the revocation of the Designated Health Food status of Blue Slim (shown in Exhibit 14) and Blue Inc. sent its written reply (Exhibit 15).
41. Meanwhile, Blue Inc. sent a letter to Red Corp., indicating its discontent caused by Red Corp.'s failure to make Contingent Payment to Blue Inc. as set forth in the Stock Purchase Agreement, which Red Corp. allegedly escaped by unreasonably suppressing Blue Drink's sales and profits through its decision to sell Red Energy and Red Slim at a 60% discount of the standard retail price for a two-year period and through driving Bob Orange into resignation (shown in Exhibit 16). Please note that Red Drink's sales figures, actual and planned, for 2013 and 2014, in addition to retrospective projections based on hypothetical scenarios, are given in Exhibit 17. The issues relating to the takeover of Blue Drink will be referred to as the "M&A Case."

<Round A>

42. Red Corp. and Blue Inc. negotiated with each other in an effort to settle both the Chocolate Case and the M&A Case, but could not reach an agreement. The parties decided to bring the two cases to arbitration. Their respective claims and contested issues with respect to the two cases are summarized in Exhibit 18. Please note that interest on any amount due need not be considered for either of the cases. Red Corp. and Blue Inc. have both agreed that the arbitration would be governed by the UNIDROIT Principles of International Commercial Contracts 2010.

<Round B>

43. Arbitration for the Chocolate Case and the M&A Case came to an end when Red Corp. and Blue Inc. reached a settlement. One year later, Pat Red passed away due to an illness, and the post of CEO was succeeded by his only son, Ethan. Ethan Red, upon graduating from Negoland University, studied Pedagogy in the United States and then worked for a toy company in Europe for five years. He subsequently received his MBA in the United States and joined Red Corp. five years ago as the head of Treasury Department. After his appointment as CEO, Ethan has steered the Company without major flaws by sticking to the business principles established by his father. In the past, his comments spurred speculation that Ethan was interested in education-related business and wanted to make it one of the core businesses of Red Corp. Please note that as soon as Ethan became the CEO, he made the chocolate division, which had been operated directly by Red Corp. proper, a wholly owned subsidiary of Red Corp. known as Red Chocolate, just like Red Corp.'s wine and sporting goods subsidiaries. Red Corp. is the holding company for them.
44. At Blue Inc., Larissa Young was named CEO after Kelly Blue's retirement. Young wanted to strengthen the three business segments Blue Inc. kept, namely, the foods, dairies and pharmaceuticals divisions, more than ever. In particular, the absence of chocolate in the offerings of its confectionery division made her feel a crucial element was missing. Young talked about her frustration of Blue Inc. not carrying its own chocolate line to Satoko Hotta, an officer at Arbitria Securities, over a meal. "Rumor has it that Red Corp. is considering selling its chocolate business," Hotta informed Young. Although Blue Inc. continued to import chocolate from Red Corp. and sell it in Arbitria even after the "Chocolate Case," the chocolate transaction was more of an accessory nature as far as Blue Inc. as a whole was concerned.
45. Young asked Hotta to approach Red Corp. to explore if it was truly ready to part with its chocolate division. Red Corp. expressed its willingness to meet with Young to discuss the issue. The following discussion took place in the meeting held between the two companies at the head office of Red Corp. Red Corp. was represented by Ethan (CEO) and Houck (Director of Corporate Planning) in addition to Nomura of Negoland Bank. Blue Inc. was represented by Young (CEO) and Diamond (Director of Corporate Planning) in addition to Ohta of Arbitria Securities.

Young: Thank you for taking the time to hear us out. As you may have heard from Arbitria Securities, we are interested in your chocolate division. As you know, our confectionery division enjoys a certain level of recognition globally, but we do not have any chocolate products in our offerings. To take our confectionery division to a higher level, we are interested in acquiring your

chocolate division. We at Blue Inc. have been importing and selling your chocolate in Arbitria for some years and we are very familiar with your chocolate products. By combining your chocolate division with our confectionery division, we'll be able to offer a full range of confectionery products on a one-stop basis, and I believe this will open up new possibilities and we'll reap greater values by putting them together.

Ethan: Thank you for your positive view of our chocolate division. In fact, our key business domains now are dairy products and sporting goods. And we are stepping up efforts to develop our beverage business, too, which was transferred from your organization a few years back. Besides, we are also interested in exploring other business opportunities of various kinds. For us, a lot of sentimental value is attached to the chocolate business -- it was the very first business my father, Pat Red, undertook. But I believe it's time to move on to a new stage by selling the division and using the proceeds for other business ventures. In other words, I would consider selling the division to you under the right terms and conditions.

Young: Well, then, this will be a win-win transaction for both of us. I am thrilled to know your strong interest. Let's move right ahead and work out details.

46. After the meeting, the two parties signed a non-disclosure agreement and exchanged related documents. They agreed on the fundamental scheme of the sale, which would require Blue Inc. to acquire all the shares of Red Chocolate in exchange for a cash payment, and a letter of intent was prepared (see Exhibit 19). Please note that the business forecasts (projections based on the hypothetical assumption that Red Chocolate continues to be managed by Red Corp. in the way it has done) and balance sheets of Red Chocolate, were submitted by Red Corp. to Blue Inc., as shown in Exhibit 20.
47. Due diligence was performed, followed by negotiations based on due diligence reports to work out details of the stock purchase agreement. Topics of discussion centered primarily on the sale price, treatment of Red Chocolate's current officers, representations and warranties concerning the factory site owned by Red Chocolate in relation to the Environmental Act, representations and warranties concerning transactions with the nation of Zeta, and the breakup fee.
48. Blue Inc. proposed US\$70 million as the price of the shares based on due diligence results. Red Corp. wanted US\$120 million. During previous negotiations, Blue Inc. made the following arguments:
  - In the opinion of Blue Inc. the reasonable price would be US\$70 million, based on the business projections and balance sheets given in Exhibit 20. The price also reflected the results of due diligence and corporate valuation analyses using the discounted cash flow method and EBITDA multiple

method.

Red Corp., in response, told the following to Blue Inc.:

- The business projections presented in Exhibit 20 are conservative estimates that do not account for synergies. Sales are expected to reach US\$125 million in a year if synergies are considered, and incremental sales increases of about US\$10 million per year are also expected.
- With such sales increase taken into consideration, the price of US\$120 million should be the reasonable amount.

Exhibit 20 shows how the enterprise value would change depending on the business projection and discount rate under the discounted cash flow method.

49. The most critical personnel issue concerns Red Chocolate's two current officers, George Sullivan and Carolina Chen. The two supported Pat from the inception of Red Corp. and, even after Pat's death, the two are very much engaged in the business of Red Chocolate and both receive US\$1 million as salary each year. Sullivan is the director in charge of sales and Chen is the director in charge of R&D. Blue Inc. wants to retain Chen to head R&D after the acquisition, but it plans to replace Sullivan with its own sales staff, as Blue Inc. has a number of outstanding sales professionals on its team. Red Corp. disapproves of Blue Inc.'s plan, arguing that Sullivan has been a central figure in driving Red Corp.'s growth and it could not accept such plan as may disparage him. In addition, Red Corp. told Blue Inc. that Chen would not move to Blue Inc. without Sullivan and that it would continue to employ both Sullivan and Chen if Blue Inc. didn't welcome both.
50. With respect to the representations and warranties to be included in the stock purchase agreement, Blue Inc. is seeking the inclusion of a clause to the effect that the land owned by Red Chocolate is free of environmental contamination and a covenant by Red Inc. that it will bear full cost of soil decontamination whenever contamination is found, in line with the Environmental Act of Negoland requiring the owner of the land to bear such cost. Red Corp. explained to Blue Inc. that the land in question was purchased from a manufacturer 15 years ago, when strict environmental laws were not in place, and that Red Corp. can give its word that Red Corp. has caused no environmental pollution since the land purchase and that soil contamination was never found at the time of the land purchase and has never been discovered to date. However, Red Corp. is still unwilling to accept the inclusion of the representation and warranty proposed by Blue Inc., on the ground that the risk of hidden contamination caused by the seller not known or disclosed at the time of the land transaction and not discovered until now is not completely nil. It is the expert's view that, considering from the past cases, the cleanup cost would be between US\$5 million and US\$30 million if contamination is found.
51. Another key issue that needs to be addressed in connection with the

representations/warranties clause concerns Red Corp.'s business with Zeta. The nation of Zeta is a developing country which was a colony of Negoland, and after its independence, a military regime with a radical ideology has been established. The nation of Zeta is considered by the Arbitrian government as a nation supporting terrorist activities, and it has ordered Arbitrian corporations and their subsidiaries (including overseas subsidiaries) not to enter into any direct transactions with the nation of Zeta, any Zeta corporations, or any corporations substantially controlled by the nation of Zeta, Zeta corporations or Zeta nationals (collectively, "Zeta related parties"). Also, even if none of the counterparties to a transaction is a Zeta related party, transactions such as those in which goods would be resold to Zeta related parties and benefit them are prohibited (such transactions are referred as "indirect trade"). If such a transaction is uncovered, the transaction must be stopped immediately, and large fines may be imposed in malicious cases. Blue Inc. is seeking a representation from Red Corp. to the effect that Red Corp. does not trade directly or indirectly with Zeta related parties. Red Corp. is reluctant to include this representation and warranty sought by Blue Inc. on the ground that it is excessive extraterritorial application of Arbitrian law to unilaterally enforce Arbitrian law in relation to a Negoland corporation. In addition, Red Corp. argues it has not checked if there is any indirect trade with Zeta related parties, though it is sure of the absence of any direct trade with Zeta related parties.

52. Red Corp. requests the inclusion of a provision in the agreement to the effect that Blue Inc. will pay to Red Corp. a breakup fee equivalent to 3 percent of the sales price in the event of the termination of this Agreement for reasons not attributable to Red Corp. (For instance, the stock purchase agreement provides that Blue Inc. may terminate this agreement if it is unable to secure necessary funding or if its board of directors doesn't approve the deal). Blue Inc. is not happy about the inclusion of the breakup fee clause, arguing that it is not always customary to agree on such a breakup fee.
53. It was decided that the two parties will negotiate on the above topics on November 30. Red Corp. plans to send its executive vice president, CFO and the head of its legal department, among others, to the meeting on November 30. From Blue Inc., its Executive Vice President, CFO and the head of its legal department, among others, are scheduled to attend the same. While topics other than the above are not entirely precluded from discussion on that day as long as they contribute to the two parties' business, the participants are required to fully present their respective arguments on all issues described above and come up with a certain direction for the future courses of actions to be taken, regardless of whether the negotiation results in an agreement or ends in a breakup. Please note that an economic report on Negoland and the chocolate sector (shown in Exhibit 22) prepared by a reliable analyst is available for your review.

## Red Corp. at a glance

Name: Red Corp.

Location of Head Office: Negotown, Negoland

CEO: Pat Red:

Shares: 100% held by Pat Red

(Consolidated)

(US\$ Millions)

Group's Management Indicators		2008	2009	2010	2011	2012	2013
Sales	Chocolate	100	110	110	115	115	115
	Wine & Cheese	100	100	100	100	100	100
	Dairy	1,000	1,000	1,000	1,000	1,000	1,000
	Sporting Goods	1,500	1,500	1,500	1,500	1,500	1,500
	Other	20	20	20	20	20	20
	Total	2,720	2,730	2,730	2,735	2,735	2,735
Operating Income		500	550	500	450	500	500
Net Income		350	360	360	320	340	330

(Exhibit 2)

Blue Inc. at a glance

Name: Blue Inc.

Location of head office: Abu Abu, Arbitria

CEO: Kelly Blue

Shares: Listed on Arbitria Stock Exchange

(Consolidated)

(US\$ Millions)

Blue's Management Indicators		2008	2009	2010	2011	2012	2013
Sales	Confectionery	3,100	3,300	3,600	3,800	4,000	3,900
	Dairy	3,350	3,700	4,500	4,700	4,900	5,100
	Pharmaceutical	350	400	400	450	500	550
	Beverage	800	900	900	900	900	900
	Other	100	100	100	100	100	100
	Total	7,700	8,400	9,500	9,950	10,400	10,550
Operating Income		800	900	1,000	1,050	1,100	1,150
Net Income		550	580	630	675	700	730

○ Blue Drink in 2013

Sales US\$900 million

Operating Income US\$80 million

EBITDA US\$95 million



Letter of Intent (DRAFT)

The purpose of this letter of intent is to set forth certain non-binding understandings and certain binding commitments between Red Corporation (“Buyer”) and Blue Inc. (“Seller”), the owners of 100% of the capital stock of Blue Drink Co. (“Target”), with respect to a proposed transaction in which the Buyer, or its affiliate, will purchase all of the capital stock of the Target.

1. Subject to the satisfactory results of a due diligence by the Buyer, the ability of the Buyer to secure adequate debt financing to acquire the capital stock for the purchase price and the conditions, agreements, and undertakings referred to below in this letter of intent, the Buyer will purchase all of the issued and outstanding capital stock of the Target held by the Seller. The purchase price will be US\$700 million, which may be adjusted in accordance with the results of the due diligence.

2. The current CEO and Director of Corporate Planning of the Target will resign at the closing of the transaction and will be replaced by members of Red Corporation. The current employees of Blue Drink will be retained on the current terms, if they wish to remain.

...

[End]

## Business Planning for Blue Drink

## &lt;Basic Policy&gt;

- Focus will continue to be on Blue Energy and Blue Slim, two long-selling products, as the core products, while embarking of the development of new products in an attempt to come up with the next generation of core products.
- The current merchantability of Blue Energy and Blue Slim will be maintained, while improvements in terms of quality, etc. will be made. From the second half of fiscal 2013, the products will be marketed in Negoland and other countries.
- The supply of Blue Energy and Blue Slim to Arbitria will continue. For Negoland and countries other than Arbitria, the products will be marketed under the Red Energy and Red Slim brands, and flavors and formulas will be adjusted to suit these countries.
- The idle factories on the premises of Nego Dairies Inc. in Negoland will be purchased and converted for the production of Red Energy and Red Slim. The refit work is expected to take about two months. The production in Negoland will be primarily for distribution in Negoland and exports to other countries.
  - In Negoland and other key markets such as Japan and the United States, massive ad promotions will be launched through various media, including TV and newspapers, along with special events aimed at instant profile-raising in an effort to achieve market penetration.

## &lt;Business forecasts&gt;

- Stable sales in Arbitria are expected in the future.
- Sales are expected to rise in the spring of 2014 and onward, attributable to the launch of distribution in Negoland and exports; however the increase in sales will not be translated directly into higher cash-flow in Year 1 and Year 2 at least, given the significant amounts of funds needed to launch production and management facilities in Negoland, in addition to massive advertising promotions among others.
- Substantial increases in sales and profits are expected in Year 3 and beyond, as the level of recognition in Negoland, the United States and Japan rises.

(US\$ Millions)

	2013	2014	2015	2016
Sales in Arbitria	900	900	1,000	1,000
Sales in Negoland	300	500	600	800
Export Sales	100	300	500	700
EBITDA	100	110	120	130

## STOCK PURCHASE AGREEMENT

This Stock Purchase Agreement is made as of December 15, 2012 by and between Blue, Inc., a corporation organized and existing under the laws of Arbitria (“BLUE”) and Red Corporation, a Negoland corporation, a corporation organized and existing under the laws of Negoland (“RED”).

### WITNESSETH:

WHEREAS, the entire issued and outstanding capital stock of Blue Drink, Inc., an Arbitrian corporation, (“TARGET”) consists of one Thousand (1,000) shares of stock (the “Stock”) and BLUE is the sole shareholder of TARGET; and

WHEREAS, RED and BLUE (each a “Party”, collectively the “Parties”) have agreed that BLUE shall sell, and RED shall purchase from BLUE, the Stock as provided below in this Agreement.

NOW THEREFORE, the Parties hereto agree as follows:

#### ARTICLE 1. Sale and Purchase.

Subject to the terms and conditions set forth herein, on January 15, 2013 (the “Closing Date”), BLUE shall (a) sell to RED, and RED shall purchase from BLUE, the Stock, and (b) deliver to RED the original share certificate(s) representing the Stock (the “Share Certificates”), together with any other instruments (if any) necessary for the sale and purchase of the Stock in exchange for the payment by RED to BLUE of the Purchase Price. (The sale and purchase of the Shares set forth in this Article shall be hereinafter referred to as the “Transaction”).

#### ARTICLE 2. Purchase Price.

1. The purchase price for the Stock shall be US\$800,000 per share and an aggregate purchase price (the “Purchase Price”) shall be US\$800,000,000.
2. In case the EBITDA of the TARGET in the fiscal year of 2013 and/or 2014 exceeds US\$110,000,000, RED shall pay to BLUE the amount equals (EBITDA – US\$110,000,000) × 8 as the contingent payment of additional purchase price within three (3) months after the end of the fiscal year.

ARTICLE 3. Closing Location; Payment.

1. The consummation of the Transaction as contemplated in Article 1 (the “Closing”) shall take place at the office of BLUE at 10:00 a.m.; provided that consummation of the Transaction shall be subject to the completion of the conditions set forth in Article 6 hereof.
2. On the Closing Date, the Transaction is to be consummated through the following actions by parties at the same time:
  - (i) BLUE shall deliver the Share Certificates to RED without any security interest or other limitation of the right thereon;
  - (ii) RED shall effect payment of the Purchase Price by paying such amount to the bank account designated by RED by bank remittance to BLUE and delivering a document certifying the payment of the Purchase Price by RED pursuant to the terms and conditions set forth in Article 1.1 above;
  - (iii) BLUE shall deliver accurate copies of documents which are adequate to certify the completion of internal procedures required for the Transaction, such as an accurate copy of minutes of the Board of Directors’ meeting of BLUE in which the Transaction was approved; and

ARTICLE 4. Representations of BLUE.

1. BLUE hereby represents and warrants to RED the correctness of the matters described in the items below as of the execution of this Agreement, except as set forth in the notice delivered by BLUE to RED on the date hereof. Unless otherwise notified by BLUE in writing, BLUE shall be deemed to have represented and warranted that the matters described in the items below are correct as of the Closing Date.
  - (i) (Incorporation and Valid Legal Existence) TARGET is a corporation duly organized and validly existing under the laws of Arbitria and has all requisite power and authority to own, lend, borrow and manage properties and Schedule1 is a bona-fide and accurate copy of the articles of incorporation of TARGET;
  - (ii) (Execution of and Performance under this Agreement) BLUE is a corporation duly organized, validly existing and in good standing under the laws of Arbitria and has all requisite corporate power and authority to enter into this Agreement and to

consummate the Transaction;

- (iii) (Validity and Enforceability of this Agreement) The execution of this Agreement by BLUE will have been duly and effectively authorized by all requisite corporate action, and this Agreement has been duly executed and delivered by BLUE and constitutes the legal, valid and binding obligation of BLUE, enforceable in accordance with its terms;
  
- (iv) (Ownership Interests in TARGET) All of the Stock is owned, of record and beneficially, by BLUE, free and clear of and otherwise unaffected by any lien, adverse interest, charge, claim, restriction on transfer, mortgage, pledge, security interest, title retention agreement, voting rights agreement, conditional assignment, put, call or other encumbrance, agreement or commitment of any kind or nature whatsoever (hereinafter collectively “Liens”), and, against payment therefor on the Closing Date pursuant to the terms of this Agreement, BLUE will transfer to RED, and RED will acquire from BLUE, valid title to the Stock, free and clear of and otherwise unaffected by any and all Liens. All of the Stock is validly issued, fully paid and nonassessable. Other than the Stock, there are no other shares of capital stock or other equity securities of TARGET outstanding; there are no outstanding options, warrants or other rights to purchase or acquire any shares of capital stock or other equity securities of TARGET, and no shares of capital stock or other equity securities of TARGET are reserved for issuance for any purpose; and there are no contracts, commitments, agreements, understandings, arrangements or restrictions of any kind by which TARGET is bound to issue any additional shares of capital stock or other equity securities or, other than this agreement, by which BLUE is bound to sell any of the Stock in TARGET or cause TARGET to issue any of its shares of capital stock or other equity securities. The Share Certificate(s) are true and authentic and duly represent the Stock;
  
- (v) (Filings and Approvals) No approval, authorization, consent or order or action of or filing with any court, administrative agency or other governmental or regulatory authority is required for the execution and delivery by BLUE of this Agreement or the consummation by BLUE of the Transaction;
  
- (vi) (No Breach or Violation) The execution, delivery and performance of this Agreement and the consummation of the Transaction will not (a) violate any provision of the articles of incorporation or other charter or company formation documents of BLUE, (b) violate, conflict with or result in a breach of or default under any contract

or agreement to which BLUE is a party or by which it or any of its assets or properties is bound, (c) violate any order, judgment, injunction, award or decree of any court, arbitrator or governmental or regulatory authority against or binding upon BLUE, (d) violate any statute, law or regulation of any jurisdiction as such statute, law or regulation relates to BLUE, or (e) result in the creation or imposition of any Lien upon any of the assets or properties of BLUE;

- (vii) (Financial Statements) BLUE has delivered to RED true and complete copies of the balance sheets and profit and loss statements (hereinafter collectively “Financial Statements”) of TARGET as of the end of the each of TARGET’s last five (5) fiscal years and as of December 31, 2011. The Financial Statements have been prepared from and are in accordance with the books and records and fairly present the financial position of TARGET as of the respective dates thereof, and the related results of operations and changes in financial position, all in accordance with generally accepted accounting principles in Arbitria consistently applied throughout the periods involved, except as may be otherwise indicated therein;
- (viii) (Taxes and Tax returns) All necessary taxes and other returns and reports respecting taxes required to be filed prior to the Closing Date by TARGET have been properly filed with the appropriate authorities and each such return and report was complete, true and correct at the time of filing;
- (ix) (Undisclosed Liabilities) TARGET has no liabilities or obligations, whether accrued, absolute, contingent or otherwise including but not limited to guaranty for any liability or obligation of any third party.
- (x) (Labor Unions and Labor Relationships) There are no union activities or collective bargaining agreements involving TARGET or any of the employees of TARGET. There is no pending, threatened strike, picketing, work stoppage, work slowdown or other similar labor trouble, claims, or complaints with respect to the employees of TARGET.;
- (xi) (Key Employees) All of the key directors and employees as listed in Schedule 2 (the “Key Employees”) has agreed to continue to work for TARGET even after the Closing Date under the same terms and conditions as currently applied to each individual;
- (xii) (Actions and Proceedings) There are no (i) outstanding orders, judgments, injunctions, awards, decrees of any court, governmental or regulatory body or

arbitration tribunal against or involving TARGET or (ii) claims, actions, suits or legal, administrative or arbitration proceedings or investigations against TARGET. There is no basis for any such action, suit, proceeding or investigation;

(xiii) (No Adverse Change) Since December 31, 2011 there has been no adverse change on the condition, financial or otherwise, of TARGET or its business or the assets of TARGET, and no such change is threatened to TARGET or its business; and

(xiv) (Full Disclosure) None of the written information or documents which have been furnished by BLUE to RED in connection with the Transaction is false or misleading or contains any misstatement of fact or omits any fact necessary to be stated in order to make the statements therein not misleading.

2. In the event that RED raises a written claim against BLUE, for reason of a violation of the representations or warranties set forth in Paragraph 1 hereof, which reasonably specifies the contents of claim, BLUE shall bear the responsibilities for such violation of the representations and warranties only for three (3) years from the Closing Date; provided, however that BLUE shall bear the responsibilities for such violation of the representations and warranties set forth in item (iv) of the preceding paragraph indefinitely.

#### ARTICLE 5. Representations of RED.

1. RED hereby represents and warrants to BLUE the correctness of the matters described in the items below as of the execution of this Agreement. Unless otherwise notified by RED in writing, RED shall be deemed to have represented and warranted that the matters described in the items below are correct as of the Closing Date.

(i) (Execution of and Performance under this Agreement) RED is a corporation duly incorporated and validly existing under the laws of Negoland and has all requisite corporate power and authority to enter into this Agreement and to consummate the Transaction; and

(ii) (Validity and Enforceability of this Agreement) The execution of this Agreement by RED will have been duly and effectively authorized by all requisite corporate action, and this Agreement has been duly executed and delivered by RED and constitutes the legal, valid and binding obligation of RED, enforceable in accordance with its terms.

2. In the event that BLUE raises a written claim against RED, for reason of a violation of the

representations or warranties set forth in Paragraph 1 hereof, which reasonably specifies the contents of claim, RED shall bear the responsibilities for such violation of the representations and warranties only for three (3) years from the Closing Date.

ARTICLE 6. RED's Conditions to Closing.

The obligation of RED to consummate the Transaction at the Closing is subject to the completion of all of the following events:

- (i) the completion of all of BLUE's internal procedures such as approval of the Board of Directors' meeting regarding the Transaction, etc; and
- (ii) the representations and warranties by BLUE set forth in Article 4 hereof being true and correct in all material respects when made and as of the Closing Date as if made thereon.

ARTICLE 7. BLUE's Conditions to Closing.

The obligation of BLUE to consummate the Transaction at the Closing is subject to the completion of all of the following events:

- (i) the completion of all of RED's internal procedures such as approval of the Board of Directors' meeting regarding the Transaction, etc;
- (ii) the representations and warranties by RED set forth in Article 5 hereof being true and correct in all material respects as of the Closing Date as if made thereon; and
- (iii) execution and delivery by all of the Key Employees of a letter providing that they will continue to be employed by the TARGET for at least three (3) years from the Closing Date.

ARTICLE 8. RED's Covenants.

RED shall not operate, instruct, influence or exercise its voting right of the TARGET in such manner as may materially harm the interest of BLUE in the additional payment as stipulated in Article 2; provided, however, that RED may make any reasonable business judgment to operate the TARGET after the Closing Date.



ARTICLE 9. No Competition.

1. BLUE covenants and agrees that, for a period ending on the 5th anniversary of the Closing Date, BLUE shall not and BLUE shall not allow its affiliates to:
  - (i) directly or indirectly own, manage, operate, control, participate in, perform services for, or otherwise carry on, a business similar to or competitive with the business conducted by the TARGET in Arbitria or Negoland ; or
  - (ii) induce or attempt to persuade any employee, agent or customer of the TARGET to terminate such employment, agency or business relationship in order to enter into any such relationship on behalf of any other business organization in competition with the business conducted by RED or the TARGET on the date hereof.
  
2. In the event BLUE violates any of its obligations under this Article 9, RED or the TARGET shall be entitled, in addition to other remedies that it may have, to a temporary restraining order and to preliminary and final injunctive relief against BLUE or such affiliate of BLUE to prevent any violations of this Article 9. In addition, RED is entitled to request BLUE to pay US\$500,000 as liquidated damages.

ARTICLE 10. Confidentiality.

The parties hereto shall keep the contents of the Transaction and this Agreement, such as the Purchase Price, confidential for five (5) years after the Closing Date, except for the cases as (i) disclosure of such information required by any laws, regulations, or rules of a securities exchange, or at the direction of public authorities concerned or a securities exchange; (ii) disclosure required in the procedure of a lawsuit or arbitration; or (iii) disclosure agreed upon in writing by the parties hereto.

ARTICLE 11. Arbitration.

Any disputes related to this Agreement or the Transaction shall be finally settled by arbitration in Tokyo, in accordance with UNCITRAL Arbitration Rules.

ARTICLE 12. Governing Law.

This Agreement shall be governed by and construed in accordance with UNIDROIT Principles of International Commercial Contracts (2010).

ARTICLE 13. Expenses.

Except as otherwise specifically set forth in this Agreement, the Parties hereto shall bear their respective expenses incurred in connection with the preparation, execution and performance of this Agreement and the Transaction, regardless of whether the Closing shall occur hereunder.

IN WITNESS WHEREOF, this Agreement has been duly executed and delivered by the duly authorized officers of RED and BLUE as of the day and year first above written.

RED: Red Corporation

BLUE: Blue, Inc.

By \_\_\_\_\_

By \_\_\_\_\_

Name:

Name:

Title:

Title:

[Schedule 1 is omitted.]

Schedule 2

Bob Orange

## CONTRACT

THIS CONTRACT is made as of December, 10, 2013 by and between Red Corporation (“Seller”) and Blue, Inc. (“Buyer”).

THE SELLER AND BUYER AGREE AS FOLLOWS:

### Article 1 GOODS

The Seller shall sell and deliver to the Buyer, and the Buyer shall purchase from the Seller the Chocolate (“Goods”) produced by the Seller whose details are as specified in Exhibit 1.

### Article 2 PAYMENT

The Buyer shall pay to the Seller US\$3,000,000. for the Goods by a letter of credit issued by a first ranked bank in Arbitria for the benefit of the Seller.

### Article 3 TRADE TERMS AND SHIPPING

1. The trade term is CFR (Incoterms ® 2010), Port of Abab.
2. Shipping shall be made by the Seller by January 10 at the Port of Negotown.
3. Time of shipment or delivery is of the essence of this Contract.
4. Partial shipment is not allowed. Transshipment is not allowed.

### Article 4 WARRANTY

The Seller makes no warranty or condition, expressly or impliedly, including without limitation warranty as to the fitness of the Goods for any particular purpose or the merchantability thereof.

### Article 5 INCREASED COST

Any new, additional or increased freight rates, surcharges, taxes, custom duties, export or import surcharges or other governmental charges or insurance premium or any other reasonable costs incurred by the Seller with respect to the Goods after the conclusion of this Contract, shall be for the account of the Buyer and shall be reimbursed to the Seller by the Buyer within a reasonable

time after demand.

Article 6 FORCE MAJEURE

Neither party shall be liable for failure to perform or delay in performing any obligation hereunder to the extent that such failure or delay is attributable to force majeure. The term force majeure shall mean such acts, happenings, causes or circumstances as, including, but not limited to, war, civil disturbance, labor difficulties or direction of a governmental authority which are beyond the reasonable control of the party affected.

Article 7 GOVERNING LAW

This contract shall be construed in accordance with and governed by UNIDROIT Principles for International Commercial Contracts 2010.

Article 8 ARBITRATION

Any dispute arising out of or under this contract shall be settled by arbitration in accordance with UNCITRAL Arbitration Rules, in the edition current at the date of this contract, such Rules forming part of this contract and of which both parties hereto shall be deemed to be cognizant.

Article 9 ENTIRE AGREEMENT AND MODIFICATION

This Agreement sets forth the entire agreement between the parties hereto with respect to the subject matter hereof and is intended to supersede all prior negotiations, understandings and agreements. No provision of this Agreement may be waived or amended, except by a writing signed by the parties hereto.

Red Corporation  
By \_\_\_\_\_

Blue, Inc.  
By \_\_\_\_\_

[Exhibit 1 is omitted.]

FROM ARBITRIA BANK, INTERNATIONAL BUSINESS OPERATION DEPT

DATE: DECEMBER 20, 2013

IRREVOCABLE DOCUMENTARY CREDIT NO 123456

ADVISING BANK: NEGOLAND BANK, HEAD OFFICE

BENEFICIARY: RED CORPORATION

APPLICANT: BLUE, INC.

DATE OF EXPIRY: JANUARY 30, 2014

AMOUNT: USD 3,000,000.00

PARTIAL SHIPMENT NOT ALLOWED

TRANSSHIPMENT NOT ALLOWED

SHIPMENT FROM PORT OF NEGOTOWN TO PORT OF ABAB NOT LATER THAN JANUARY 10, 2013

CREDIT AVAILABLE BY NEGOTIATION BY ANY BANK AGAINST PRESENTATION OF THE DOCUMENTS DETAILED HEREIN AND OF YOUR DRAFT AT SIGHT FOR 100 PCT OF INVOICE VALUE DRAWN ON US.

SIGNED COMMERCIAL INVOICE IN 3 COPIES INDICATING L/C NO.

PACKING LIST IN 3 COPIES INDICATING QUANTITY AND PACKING CONDITIONS.

FULL SET OF ORIGINAL CLEAN ON BOARD OCEAN BILLS OF LADING ISSUED TO ORDER AND BLANK ENDORSED MARKED "FREIGHT PREPAID" AND "NOTIFYING BLUE, INC".

DISCRIPTION OF GOODS: RED'S CHOCOLATE

TERMS OF DELIVERY: CFR PORT OF ABAB

. . .

EXCEPT SO FAR AS OTHERWISE EXPRESSLY STATED THIS CREDIT IS SUBJECT TO THE UNIFORM CUSTOMS AND PRACTICE FOR DOCUMENTARY CREDIT (2007 VERSION) ICC PUBLICATION NO.600.

THIS IS AN OPERATIVE INSTRUMENT NO MAIL CONFIRMATION TO FOLLOW.

PLS ADVISE THIS CREDIT TO THE BENEFICIARY WITHOUT ADDING YOUR CONFIRMATION.

(Exhibit 8)

Letter from Blue Inc. to Red Corp. dated April 5, 2014

Red Corp. failed to deliver its chocolate worth US\$1.5 million to Blue Inc. in breach of the obligations set forth in the sales agreement between us dated December 10, 2013, under which Red Corp. was required to deliver chocolate worth US\$3 million to Blue Inc. before January 31. This resulted in a serious consequence. We at Blue Inc. were forced to pay a total of US\$1 million in penalties to our department store customers in Arbitria. The penalties arose from Red Corp.'s breach of the aforementioned sales agreement, and hence, we request your prompt reimbursement of US\$1 million to us.

[End]

Letter from Red Corp. to Blue Inc. dated April 15, 2014

We received your letter dated April 5, 2014. We regret that the case in question was the result of a series of unfortunate events. However, after consulting with our lawyers, we concluded that we have no legal obligation to reimburse the US\$1 million you requested.

We did successfully complete the preparation for the shipment in time for the shipping deadline of January 10, as stipulated in the agreement. We were unable to put the chocolate on board the ship due to the failure by Negoland Bank, the notifying bank in this case, to advise us of the letter of credit. A final and binding legal precedent in Negoland holds that “if the seller and the buyer agree to settle a transaction by a letter of credit, the seller, in the absence of any special provision, may refuse to perform its obligations thereunder until a letter of credit is advised,” and in light of this precedent, Red Inc. did not commit any non-performance. For later shipment of chocolate by air, Red Corp. did hand over the goods to the freighter and hence, we performed our necessary obligations. Therefore, no failure to fulfill obligations is found on our part. You are responsible for your own loss, which you may be able to recoup by filing a legal claim against Negoland Bank, among other means.

In this connection, I would like to remind you that we made arrangements for the air cargo upon your special request, and we hereby request your reimbursement of US\$500,000 to us for the cost of air freight.

[End]

Letter from Blue Inc. to Red Corp. dated April 25, 2014

We received your letter dated April 15. The arguments you presented are not acceptable to us. The use of a letter of credit for the settlement of the transaction was your idea in the first place. And Negoland Bank, which you designated to serve as the correspondent bank for the transaction, committed an error that led to undesired consequences. The damage that arose out of Negoland Bank's error (i.e., penalties Blue Inc. paid and \$500,000 in air freight charges) ought to be borne by you. For the air cargo, it is not permissible to request our reimbursement at this late stage, especially in light of the fact that you told us that you would invoice the amount to Negoland Bank.

In addition, the lightning strike on the warehouse was part of the risks you bore, according to our understanding of Incoterms' CFR terms.

We therefore request once again for your payment of US\$1 million as stated in our letter dated April 5.

[End]



Letter from Red Corp. to Blue Inc. dated February 15, 2014

As you know, Bob Orange, who served as the director of R&D of Red Drink, resigned and subsequently joined Arbitria Coffee. He is reportedly undertaking the development of a coffee beverage with weight-loss effects. And we came across the news that Blue Inc. had invested US\$5 million in and sent one board member to Arbitria Coffee. It has turned out that Blue Inc. allows Arbitria Coffee to use the facilities of your Central Research Center.

We believe that the investment you made in support of the endeavor by Orange and Arbitria Coffee to develop a coffee beverage offering weight-loss benefits constitutes a violation by you of the non-competition obligations under Article 9 of the Stock Purchase Agreement. We request your payment of damages amounting to US\$500,000 pursuant to Article 9 of the Agreement.

[End]

Letter from Blue Inc. to Red Corp. dated February 20, 2014

We read your letter dated February 15. We did invest US\$5 million in Arbitria Coffee, but Blue Inc. and Arbitria Coffee are separate corporate entities and Arbitria Coffee is not a subsidiary of Blue Inc. Furthermore, the business domain of Red Slim is different from that of coffee beverages; hence, we believe our contractual non-competition obligations do not apply to the case in question.

Therefore the request made in your letter dated February 15 is groundless, and we decline to comply with the request.

[End]

Due Diligence Report (an Excerpt)

3.5 Risks relating to the Designated Health Food status of Blue Slim

At the moment, Blue Slim is designated by the Ministry of Health and Welfare of Arbitria as a “Designated Health Food,” and this status plays a part in contributing to the sales of the product to an extent.

In early 2012, however, complaints from consumers indicating stomach problems associated with overconsumption of Blue Slim began to arrive at Blue Drink as well as Arbitria’s Ministry of Health and Welfare. Further, in April 2012, the said Ministry contacted Blue Drink to inform it that the Ministry was closely monitoring the situation. Should the Ministry conclude that Blue Slim has, indeed, health issues, the Ministry could proceed to revoke the Designated Health Food status (Note that the Ministry can revoke the Designated Health Food status at its discretion).

In response, Blue Drink conducted full tests from April to May 2012, but according to Blue Drink, it did not find any phenomenon of overconsumption leading to stomach problems, contrary to the allegations made in such complaints.

Letter from Red Corp. to Blue Inc. dated June 10, 2014

On April 30, 2014, Red Drink was informed by Arbitria's Ministry of Health and Welfare of its decision to revoke the Designated Health Food status of Blue Slim. We have confirmed that you were aware of the reason for the revocation as early as April 2012, that is, cases of stomach problems arising from overconsumption of Blue Slim.

However, the written communication from Blue Inc. to Red Corp., which was attached to the Stock Purchase Agreement dated December 15, 2012, did not mention any circumstances surrounding the stomach problem issue described above

This signifies a misrepresentation on your part with respect to Article 4 of the Stock Purchase Agreement, and under the Agreement, we are entitled to claim compensation for the damages we suffered as a result thereof. The revocation of the Designated Health Food status has caused us US\$30 million in damages at least. We request your payment of US\$30 million to cover our damages for now. We may request additional compensation, if we find the extent of damages to be larger than what we know now.

[End]

Letter from Blue Inc. to Red Corp. dated June 20, 2014

We read your letter dated June 10. We are sorry that the Designated Health Food status of Blue Slim was revoked. We are willing to extend cooperation to you as much as practically possible, if you wish to aim for re-designation.

However, we do not believe we have obligation to pay damages to you under the Stock Purchase Agreement dated December 15, 2012 in connection with this case. In fact, when we entered into the Stock Purchase Agreement, you should have known that there were complaints from consumers claiming stomach problems following overconsumption of Blue Slim. Please note that this fact is not one that could have significant adverse impact on the business of Blue Drink as of May 2012.

Therefore, we are under no obligation to pay damages.

[End]

Letter from Blue Inc. to Red Corp. dated October 30, 2014

Article 2.2 of the Stock Purchase Agreement stipulates that, if the amount of EBITDA of Red Drink in fiscal 2013 and 2014 exceeds US\$110 million, Red Corp. will be under obligation to pay an additional stock purchase price equivalent to the amount obtained by multiplying 8 to the amount of such excess. EBITDA in fiscal 2013 was US\$110 million, and EBITDA for fiscal 2014 is expected to be US\$80 million. The above appears to suggest that no additional stock purchase price would be due from Red Corp. under Article 2.2 of the Agreement with respect to fiscal 2013 and 2014.

Let us point out, however, that operating income for fiscal 2013 and 2014 has been low, because Red Drink resorted to nonsensical business practices including, among others, sales to Nego Drink at an excessively low price in violation of Article 8 of the Stock Purchase Agreement and unfair treatment of Mr. Orange, which in effect chased Mr. Orange away. It is indisputable that EBITDA in fiscal 2013 would have been US\$120 million and EBITDA for 2014 would become US\$125 million, had it not been for such nonsensical practices.

Based on the above, Blue Inc., pursuant to Article 2.2 of the Stock Purchase Agreement, requests your payment of US\$80 million for 2013 and US\$120 million for 2014, which is the amount of additional payment that would have been paid by Red Drink, had it not been for your nonsensical practices (For fiscal 2014, we will bill you when the amount is finalized.)

[End]

Red Drink's Business Performance and Forecasts

\*For the purpose of this competition, participants are not prevented from accepting or rejecting the validity of the numbers given in the tables below (i.e., numbers based on hypothetical "what-if" scenarios and the numbers for fiscal 2014), and may argue thereon .

Red Drink's Operating Results (US\$Millions)

Year 2013	Forecast	Actual	If sales had been made at 50% of standard price to Nego Drink
Sales in Arbitria	900	900	
Sales in Negoland	300	300	
Exports	100	100	
EBITDA	100	100	+20

Year 2014	Forecast	Actual	If sales had been made at 50% of standard price to Nego Drink	If Orange had not quit	If Designated Health Food status had not been revoked
Sales in Arbitria	900	600			+300
Sales in Negoland	500	300		+200	
Exports	300	200		+100	
EBITDA	110	80	+15	EBITDA rise by 5 if sales increase by 100	

\* This table shows how much EBITDA would have increased if the conditions in the upper column had existed.

\*Based on given circumstances, it is not plausible to consider sales to Nego Drink at a price in excess of 50% of the standard price.

## Chocolate Case

<Claims made by the parties>

Blue Inc. seeks:

Payment by Red Corp. of US\$1 million to Blue, Inc.

Red Corp. seeks:

Payment by Blue Inc. of US\$500,000 to Red Corp.

<Issues>

1. Whether Red Corp. is under obligation to reimburse to Blue Inc. the amount Blue Inc. paid to its department store clients (i.e., US\$1 million in penalties)
2. Whether Blue Inc. is under obligation to pay US\$500,000 to Red Corp. under the agreement between Red Corp. and Blue Inc. for the amount Red Corp. paid to Negoland Air

## M&A Case

< Claims made by the parties >

Red Corp. seeks:

Payment by Blue Inc. of US\$30.5 million to Red Corp.

Blue Inc. seeks:

Payment by Red Corp. of US\$200 million to Blue Inc.

<Issues>

1. Whether Blue Inc. is in violation of the non-competition clause stipulated in Article 9 of the Stock Purchase Agreement dated December 15, 2012
2. Whether Blue Inc. is in violation of its obligation stipulated in Article 4 of the Stock



Purchase Agreement dated December 15, 2012 in connection with its representations and warranties

3. Whether Red Corp. is under obligation to pay an additional Stock Purchase Price as stipulated in Article 2.2 of the Stock Purchase Agreement dated December 15, 2012, and how much should be the amount if such payment is found to be due. (In preparing for negotiation with respect to the amount due for fiscal 2014, participants are not precluded from using the forecasted figures that prevail now as the base.)

Letter of Intent

The purpose of this letter of intent is to set forth certain understandings between Blue, Inc. (“Buyer”) and Red Corporation (“Seller”), the owners of 100% of the capital stock of Red Chocolate Co. (“Target”), with respect to a proposed transaction in which the Buyer, or its affiliate, will purchase all of the capital stock of the Target. All terms set forth herein are legal non-binding except those provided in Clause 4, 5 and 6.

1. Subject to the satisfactory results of due diligence by the Buyer, the ability of the Buyer to secure adequate debt financing to acquire the capital stock for the purchase price and the conditions, agreements, and undertakings referred to below in this letter of intent, the Buyer will purchase all of the issued and outstanding capital stock of the Target held by the Seller. The purchase price will be determined in the purchase agreement to be mutually agreed upon by the parties.

2. The parties will negotiate the terms and begin preparation of the purchase agreement and other necessary agreements (collectively “Definitive Agreements”) that will govern the Buyer’s proposed acquisition of the capital stock. To the extent appropriate for transactions of this type and size, the Definitive Agreements will contain customary representations, warranties, covenants, indemnities, and other agreements of the parties.

3. The Definitive Agreements shall include customary conditions precedent generally applicable to an acquisition of the nature and size of the transactions contemplated by this letter of intent, each of which must be satisfied prior to the consummation of the transactions contemplated thereby.

4. From the date of acceptance by the parties of the terms of this letter of intent, until the negotiations are terminated, the TARGET will give the BUYER and the BUYERS’s management personnel, legal counsel, accountants, and technical and financial advisors full access and opportunity to inspect, investigate, and audit the books, records, contracts, and other documents of the TARGET as it relates to TARGET’s business and all of TARGET’s assets and liabilities. The TARGET further agrees to provide the BUYER with such additional information as may be reasonably requested pertaining to TARGET’s business and assets to the extent reasonably necessary to complete the Definitive Agreements.

5. Each party will keep each other confidential information strictly secret and will not reveal the existence of this letter of intent to any third party without the other party’s approval in advance.

6. Any party to this letter of intent may unilaterally withdraw from negotiation or dealing at any time for any or no reason at the withdrawing party's sole discretion by notifying the other party of the withdrawal in writing.

RED CORPORATION

BLUE, INC.

\_\_\_\_\_  
By:

\_\_\_\_\_  
By:

Financial Condition of Red Chocolate

## Business Forecasts for Red Chocolate

(US\$ thousands)	This Year	Year 1	Year 2	Year 3	Year 4	Year 5
Sale	115,000	120,000	125,000	130,000	135,000	140,000
Cost of Goods	66,700	69,600	72,500	75,400	78,300	81,200
Cost of Administration	40,250	42,000	43,750	45,500	47,250	49,000
Operating Income	8,050	8,400	8,750	9,100	9,450	9,800
Income Tax	2,415	2,520	2,625	2,730	2,835	2,940
Income After Tax	5,635	5,880	6,125	6,370	6,615	6,860
Depreciation and Amortization	1,691	1,764	1,838	1,911	1,985	2,058
Capital Expenditures	1,800	1,800	1,800	1,800	1,800	1,800
Free Cash Flows	5,526	5,844	6,163	6,481	6,800	7,118

## Red Chocolate's Assets (US\$ millions)

Assets			Liabilities and Equity		
Current Assets	Cash and Deposits	95	Current Liabilities	Accounts Payable	50
	Accounts Receivables	337		Accounts Payable - Other	40
	Other	50		Other	50
	Total	482		Total	140
Fixed assets	Buildings	100	Long-term Liabilities		60
	Machinery and equipment	100	Equity	Capital	100
	Land	100		Surplus	110
	Other	50		Retained Earnings	422
	Total	350		Total	632
Total Assets		832	Total Liabilities and Equity		832

\*The amount of interest bearing debt is US\$30 million.

## (Exhibit 21)

Table A (US\$1,000)		Year 1	Year 2	Year 3	Year 4	Year 5	Terminal Value		Total	
Free Cash Flow		5,844.0	6,162.5	6,481.0	6,799.5	7,118.0	1%	2%	1%	2%
Discount Rate (WACC)	10%	5,312.7	5,093.0	4,869.3	4,644.1	4,419.7	45,090.1	51,228.5	69,428.9	75,567.4
	9%	5,361.5	5,186.9	5,004.5	4,816.9	4,626.2	53,583.4	61,844.5	78,579.4	86,840.5
	8%	5,411.1	5,283.4	5,144.8	4,997.8	4,844.4	64,720.0	76,254.3	90,401.6	101,935.8

Table B (US\$1,000)		Year 1	Year 2	Year 3	Year 4	Year 5	Terminal Value		Total	
Free Cash Flow		6,162.5	6,799.5	7,436.5	8,073.5	8,710.5	1%	2%	1%	2%
Discount Rate (WACC)	10%	5,602.3	5,619.4	5,587.2	5,514.3	5,408.5	55,178.0	62,689.8	82,909.7	90,421.5
	9%	5,653.7	5,723.0	5,742.3	5,719.5	5,661.2	65,571.6	75,680.9	94,071.3	104,180.6
	8%	5,706.0	5,829.5	5,903.3	5,934.3	5,928.2	79,199.8	93,314.6	108,501.1	122,615.9

\*The numbers in Table A and Table B are based respectively on the business forecasts given in Exhibit 20 and on the business forecasts that factored in the synergies as claimed by Red Corp.

\*All parties are unanimous in their view that the discount rate (WACC) used must be 8%, 9% or 10%.

\*All parties are unanimous in their view that the cash flow growth rate for Year 6 and beyond used for the calculation of termination value (going-concern value, residual value) must be either 1% or 2%.

\*The numbers presented under the "Total" column represent corporate value based on the discounted cash flow method.

Economic Analyst Report

<General Condition of Negoland's Economy>

The economy of Negoland will continue to grow at the annual rate of around two percent, which owes to the firmness of its core industries, i.e., agriculture, automotive, chemicals, pharmaceuticals, cosmetics and tourism. Its former colonies are also expected to record stable growth, and the trade relationships with these nations are believed to contribute to the stable growth of Negoland in part. However, Negoland will not be immune from the consequences of a global economic crisis, and it will suffer potential impact if any hidden risks surrounding the world economy come into the open.

<Chocolate Industry>

Negoland's chocolate market is near maturity and sales by domestic makers have virtually plateaued over the past few years. A future jump in demand is not expected either. However, the trade as a whole is not very susceptible to the effects of an economic slowdown, which owes partially to effective measures taken by each chocolate maker to cope with the changing economy and social environment.

. . .

The chocolate business of Red Corp., while being stable, will have to rely on overseas sales as the key driver to ensure growth, given the flat demand for chocolate in Negoland. For sustained growth in Negoland and overseas, Red Corp. will also need to step up efforts to come up with new products that capture the fancy of consumers in order to address the issue of its recent inability, compared with its competitors in Negoland and abroad, to release innovative products, as pointed out by some market observers.