Problem for Second Annual Intercollegiate Negotiation Competition
(October 15 version)

1.

Red Pharmaceuticals Co., Ltd. (Red Co.) is a manufacturer and distributor of pharmaceuticals located in the nation of Negoland.

Negoland is a developing nation with a population of approximately 300 million (300,000,000). In 1990, the gross national income (GNI) of Negoland was approximately $150 billion ($150,000,000,000) (US); but in recent years Negoland has experienced very rapid economic growth and by 2002 the GNI had risen to approximately $300 billion (US) ($300,000,000,000). Until recently the major industries of Negoland were agriculture and mining, but at present manufacturing and service industries of all types are developing rapidly. Particularly in the cities, the standard of living has been rising at an amazing rate; at present, the standard of living in the large cities has reached the level of developed nations. In some regions, however, water and sewage facilities are inadequate, and, especially in remote mountainous regions, living standards remain low.

Red Co. was established in 1960 by Juan Red Takedia, who served as the company's first president. Juan is a member of a famous and wealthy Negoland family. After completing medical studies at Negoland University, he went to the United States for graduate study and earned a doctorate there. After working for a US pharmaceuticals company for five years, he returned to Negoland and, with support from his family, started Red Co.

A brief overview of Red Co. is set forth below.

[Red Co.]

Official name in English:	Red Pharmaceuticals Co., Ltd.
Date of establishment:	September 1960
Capital:	50,000,000,000 Negos (the official currency of Negoland) (in Japanese yen, equivalent to ¥5,000,000,000) (privately held)
Number of employees:	150

Subsidiary:	Red Pharmacies (wholly-owned subsidiary, share Capital: ¥1,000,000,000)		
Sales (consolidated basis):	Year	Total Sales	Annual Profit
	2000	¥10,000,000,000	¥60,000,000
	2001	¥18,000,000,000	¥30,000,000
	2002	¥20,000,000,000	¥70,000,000

(Note: All the above sales figures and other figures set forth below are expressed as what they would be equivalent to in Japanese yen.)

2.

For a pharmaceuticals company, Red Co. is relatively small, but it has focused its strength in certain fields and is known worldwide for its high-level research. In particular, in the area of anti-cancer drugs on which Alex's own research has focused, Red Co. owns several leading drugs and has achieved steady sales. Red Co. has placed great weight on its research efforts; half of Red Co.'s employees are researchers, for example, and 15% of total sales amounts are allocated to research expenses. Red Co. also recognized from an early date the potential for manufacturing pharmaceutical products utilizing genetic technology and is pursuing research in that field; and recently Red Co. has begun to devote efforts particularly to the development of genetically modified human growth hormone derivatives.

In 1999, the presidency of the company shifted to the next generation; Juan's child Alex took over as president. From 1985 through 1989, Alex studied in Japan at Sakura University; and then spent the subsequent two years as a trainee at a Japanese pharmaceuticals manufacturer. So as to ensure that Red Co. rides the wave of growth in the Negoland economy and expands even further, Alex felt that it was not enough for Red Co. just to continue with research and development of pharmaceutical products, but rather the company must devote efforts to retail sales of drugs and other products. Accordingly, in 2001, after Alex took over as president, Red Co. acquired, for ¥1,000,000,000, a major chain of stores, which at the time was experiencing business difficulties, and turned the store chain into a 100% wholly-owned subsidiary of Red Co. The chain was renamed Red Pharmacies. Red Pharmacies were renovated as a retail drug store chain, along the model of chains that are now popular in Japan. In addition to medical products manufactured by Red Co., the store chain sells a broad range of other products.

Red Co.'s sales have not changed much over the past three years. On a consolidated basis, profits for the year 2001 declined substantially, but this was related to the acquisition of Red Pharmacies. In 2002, profits improved thanks to sales of a drug for treatment of influenza, described in more detail below.

3.

Blue Technology, Inc. (Blue Inc.) is a manufacturer of chemicals and pharmaceuticals, located in the nation of Arbitria.

Arbitria is a developed nation with a population of 50 million and a gross national income (GNI) of approximately $700 billion ($700,000,000,000) (US). Manufacturing and service industries are strong in Arbitria; and, in recent years, the government has been providing national support for the acquisition, by Arbitrian companies, of intellectual property rights in biotechnology and other cutting-edge fields. For the past five years, the Arbitrian economy has experienced a severe downturn; in the past three years alone, stock values have declined by an average of nearly 30%.

Blue Inc. was established in 1915 as a nationally owned chemicals manufacturing company; but the company was privatized in the 1930s, during a wave of privatization of government-owned enterprises, and was listed on the stock exchange in 1935. Initially, the major products of Blue Inc. were vinyl and synthetic resins; but from the 1970s Blue Inc. diversified, entering the fields of synthetic fibers, materials for electronics, foodstuffs and medicines. In addition to receiving attention for development of a fast-acting, orally administered influenza medicine, Blue Inc. has produced a series of hit products, including an anti-baldness drug and diet foods.

Based on the financial statement filed by Blue Inc. with the securities exchange, a brief overview of Blue Inc. is set forth below:

[Blue Inc.]

Official name in English:	Blue Technology, Inc.
Date of establishment:	1915
Capital:	3,000,000,000 Arbs (the official currency of Arbitria)

	(in Japanese yen, equivalent to ¥30,000,000,000)
Number of employees:	3000
Places of business/factories:	Six places of business in Arbitria, including one factory for manufacture of influenza medicine. In addition, a total of ten research facilities and factories in the United States, Australia, and Malaysia, and an office in Japan.
Subsidiary:	Black Plastic (Located in Australia. Joint venture with All Black Techno Co., Ltd., of Australia. Blue Inc. holds a 40% share.)

Performance (consolidated basis):

Year	Total Sales	Annual Profit
2000	¥300,000,000,000	¥10,000,000,000
2001	¥250,000,000,000	¥8,500,000,000
2002	¥230,000,000,000	¥4,500,000,000

Breakdown of Sales by Sector

Year	Vinyl/Synthetic Resins	Synthetic Fibers/ Materials for Electronics	Foodstuffs/ Medicines
2000	¥150,000,000,000	¥50,000,000,000	¥100,000,000,000
2001	¥100,000,000,000	¥40,000,000,000	¥110,000,000,000
2002	¥ 90,000,000,000	¥30,000,000,000	¥110,000,000,000

(<u>Note</u>: All the above sales figures and other figures set forth below are expressed as what they would be equivalent to in Japanese yen.)

4.

Blue Inc. traditionally has placed considerable weight on its own research and registers approximately 100 patents every year. Research expenses total approximately 5-7% of total sales amounts. Since the last half of the 1990s, Blue Inc. has devoted efforts to biotechnology for foodstuffs and medicine. Among these efforts, in the field of foodstuffs, Blue Inc.'s efforts related to the development and production of genetically modified soybeans and other crops have met with considerable success. In the field of medicines, Blue Inc. has been giving attention to the potential for genetically modified human growth hormone derivatives, but Blue Inc. does not have sufficient researchers or research facilities to pursue such research on its own, and had been hunting for an appropriate joint venture partner.

Recently, due to the impact of the recession in Arbitria, Blue Inc.'s performance has been weak. The profitability of the Vinyl/Synthetic Resins sector had been declining for some time, and sales also declined markedly. In contrast, the Foodstuffs/Medicines sector is solid; that sector is what has been supporting Blue Inc.'s performance.

5.

In 2001, Alex, president of Red Co., visited Japan for the first time in a number of years, to attend a class reunion at Sakura University. At that time, Alex met Dale Owen, who had been on the volleyball team at Sakura with Alex. Alex had heard that Dale had returned home to the country of Arbitria, but had not been in touch with Dale for a long time. While chatting with Dale at the reunion, Alex learned that Dale had become president of Blue Inc. The two then discussed the possibility of collaboration between the two companies. In their discussions, the two quickly discovered that both companies were engaged in research and development related to genetically modified human growth hormone. While Red Co. possessed an excellent research staff and had already achieved advances in research, it faced limitations on its ability to fund the research. In contrast, Blue Inc. did not possess a particularly strong research staff in this field, nor had it achieved any significant research advances. Both companies had a strong desire to focus efforts on the genetically modified products sector, but neither had achieved any major product successes to speak of. Both Alex and Dale agreed that, if the two companies cooperated, their respective strengths would offset their respective weaknesses.

In a separate point, Blue Inc.'s anti-baldness drug and diet foods were very popular products; they were in short supply throughout the world, and it was very difficult to obtain them in Negoland. Alex felt that, if these products could be sold through the Red network at Red Pharmacies, sales figures for Red Pharmacies would strengthen. At the same time, Blue Inc. already had been investigating the possibility of making a major push into Negoland, which had been experiencing dramatic economic growth and had a very large untapped market. Dale felt that, if Blue Inc. could utilize the Red marketing network to sell Blue products, it would be much easier to open up the Negoland market.

Alex and Dale had been on the volleyball team together, and their discussions proceeded without a hitch. At both Red Co. and Blue Inc., the views of the person at the top carried great weight; and, in March 2002, the two companies entered a collaborative relationship along the following lines:

① Red Co. and Blue Inc. will establish a joint venture company in Negoland for the purposes of research and development of genetically modified human growth hormone derivatives, sale of newly developed medicines, and management of intellectual property.

② Blue Inc. will supply its products to Red Co. on a stable basis, and Red Co. will exercise efforts to market Blue Inc.'s products in Negoland.

The major points of the collaboration contract are as set forth in Attachment 1. (Other than those points set forth in the Attachment, there are no relevant provisions of the collaboration contract that need to be considered in connection with this matter.)

6.

In December 2002, Yellow Co. was established in Negoland, as a joint venture of Red Co. and Blue Inc. Yellow Co. was capitalized at ¥1,000,000,000, contributed 30% by Red Co. and 70% by Blue Inc. The employees of Yellow Co., and in particular the research staff, consisted primarily of employees seconded from the genetic modification technology division of Red Co. Research and development of genetically modified human growth hormone derivative was undertaken in the form of a continuation of the existing research conducted by Red Co. Initially, a portion of the facilities of Red Co. were used as Yellow Co.'s research facilities. (Subsequently, Yellow Co. acquired its own facilities.) Up until the establishment of Yellow Co., Red Co. was only able to afford about ¥500,000,000 per year in research expenses for the genetically modified human growth hormone derivative, but, given the large infusion of funds from Blue Inc. to Yellow Co., it became possible to increase research expenses for the project to ¥4,000,000,000 per year.

As to the other aspect of the collaboration, sales of Blue Inc. products at Red Pharmacies commenced in September 2002. Red Co. imported Blue Inc.'s products and then resold them to Red Pharmacies, which marketed them to the public through the chain of retail drug stores. As anticipated, the anti-baldness drug and diet foods sold so well they seemed to fly off the shelves. Furthermore, in late 2002 and early 2003, Negoland experienced an influenza epidemic. The Blue Inc. influenza medicine, for which Red Co. served as the importer, proved highly effective in treating the influenza, and sales of that medicine exploded. In just three months, from December 2002 through February 2003, sales of that medicine amounted to ¥3,500,000,000. For the first half of fiscal year 2002, Red Pharmacies suffered a loss of ¥30,000,000; in the second half of that fiscal year, sales of the influenza medicine exploded, and consumers who came for the medicine bought many other products as well, leading to a profit of ¥60,000,000 for the second half of fiscal year 2002. In the second half of fiscal year 2002, profits on general retail sales accounted for seventy percent of Red Pharmacies' total profit, profits from sale of the anti-influenza medicine accounted for the remaining thirty percent.

7.

Another influenza epidemic was predicted for the winter of 2003 in Negoland, so in August 2003 Red Co.'s vice president and the head of Red Co.'s medical products department visited Blue Inc. for talks on how to meet the anticipated needs. The Red Co. representatives explained that, according to forecasts by experts in Negoland, this year's influenza was expected to be Type X influenza, the same type as in 2002, and the 2003 outbreak was expected to be about as severe as that in 2002. Accordingly, the representatives explained, Red Co. wished to order the same amount of anti-influenza medicine from Blue Inc. as in the prior year, ¥3,500,000,000 worth of the medicine. Blue Inc. responded that it would exert its utmost efforts to fulfill Red Co.'s order. The two companies pledged to maintain close communication with regard to such matters as forecasts concerning the scope of the epidemic and concrete steps to meet the needs.

8.

In October 2003, the Ministry of Public Health in Negoland issued an official statement, announcing that this year's outbreak of influenza was expected to be of Type X, but since its level of contagiousness was not so high, this year's epidemic was only expected to be about half as severe as that of 2002. Based in part on this announcement, in October 2003, the head of Red Co.'s medical products department visited Blue Inc. During that visit, Red Co. and Blue Inc. executed a contract for the sale by Blue Inc. to Red Co. of 100,000 cases of medicine for Type X influenza, at a total price of ¥2,000,000,000. (Pursuant to the contract between Red Co. and Blue Inc., each case of medicine was priced at ¥20,000 throughout the entire period involved in this problem.) According to the contract, this medicine was due to be delivered at the end of November. The major points of the contract are as set forth in Attachment 2. (Other than those points set forth in that Attachment, there are no relevant provisions of the contract that need to be considered in connection with this matter.)

Thereafter, at the end of October, the Ministry of Public Health issued an updated announcement containing a forecast based on the most recent research. According to this announcement, the 2003 influenza was expected to consist of a new variant of Type X influenza (New Type X), which is about twice as contagious as the existing Type X, so a major epidemic was foreseen. Based on this updated announcement, the responsible official at Red Co. sent Blue Inc. the fax appended as Attachment 3. Blue Inc. then sent back the response contained in Attachment 4.

9.

In early November, Arbitria experienced an abnormal weather pattern, with a major cold wave. Tied to that cold wave, Arbitria suffered an outbreak of New Type X influenza that began about November 10, 2003. Since Arbitria had not suffered a serious influenza outbreak in recent years, most people lacked immunity, and the outbreak escalated into a major epidemic in the blink of an eye. At the time, the only effective influenza medicine available in Arbitria was that of Blue Inc., and Blue Inc. was quickly flooded with orders for its medicine. In a very short period of time, over 1000 people died from the influenza; and the Arbitria government advised Blue Inc. to devote all of its efforts to supplying medicine needed to meet domestic needs within Arbitria. Blue Inc. responded by putting its factory on a 24-hour-a-day production schedule; but on about November 15 it became clear that, given existing manufacturing capacity, even taking into account all existing stores of the medicine and the new production resulting from the expanded operations, the total quantity of medicine that could be supplied would amount only to the equivalent of 400,000 cases of medicine. At the very least, domestic demand within Arbitria was expected to reach 350,000 cases, so it would be impossible to fully satisfy those needs and still fill the entire order from Red Co.

Blue Inc. promptly undertook discussions of how to deal with this situation, including investigations of such measures as the possibility of further increasing production by immediately shifting another existing factory from the production of other medicines to the production of the influenza medicine. In addition, on November 16, Blue Inc. informed Red Co. of the situation in the fax appended hereto as Attachment 5. At the same time, it had become evident that Negoland also was certain to experience a major influenza epidemic; and on November 17 Red Co. sent Blue Inc. a fax (appended hereto as Attachment 6), requesting confirmation of the certain fulfillment of the existing contract for 100,000 cases of the medicine, and requesting an additional 150,000 cases.

During this period, President Dale of Blue Inc. met personally with Arbitrian government officials and endeavored to obtain their understanding of Blue Inc.'s obligation to supply Red Co., but the officials advised Dale in no uncertain terms that Blue Inc. should place first priority on supplying domestic needs. (The officials' advice has no formal statutory basis, but it was implicitly hinted that, if Blue Inc. does not comply, there is a strong likelihood the company's application for a ¥10,000,000,000 government grant to support research will be turned down. This research was extremely important to Blue Inc.'s future development.) Moreover, since Arbitria had not experienced a major influenza epidemic in recent years, it was difficult to predict just how great the demand for the medicine will be. Accordingly, Blue Inc. made up its mind to endeavor to obtain Red Co.'s understanding that Blue Inc. had met unavoidable circumstances, and decided to use its entire stock of influenza medicine, including medicine that had been produced for the purpose of fulfilling Red Co.'s order, to supply domestic needs within Arbitria.

In the end, notwithstanding Red Co.'s repeated requests, Blue Inc. was unable to make delivery at the end of November. Blue Inc. finally concluded that it would be able to deliver 100,000 cases of medicine at the end of December. In the fax appended hereto as Attachment 7, Blue Inc. inquired whether Red Co. wished to have that shipment, of 100,000 cases of medicine, made; and, as set forth in the fax appended hereto as Attachment 8, Red Co. requested the delivery.

During the interim period when Blue Inc.'s medicine was not available, however, Red Co.'s competitors had begun marketing medicines produced by other companies. Although those medicines were not as effective as Blue Inc.'s medicines, they did cost about the same amount. As a result of these sales, Red Co.'s market share dropped dramatically, and Red Co. was left with 25,000 cases of unsold inventory.

According to a report produced by a reliable market analyst, the sales situation for influenza medicines in Negoland in the years 2002 and 2003 was as follows:

	Red Co. (sales of Blue Inc. medicine)	Other companies (sales of other medicines)
Fiscal Year 2002	¥3,800,000,000	¥1,200,000,000
Fiscal Year 2003	¥1,500,000,000	¥6,000,000,000

10.

Red Co. demanded damages from Blue Inc. for failure to perform the contract. The assertions of Red Co. were as follows. (Note: Although Red Co. and Red Pharmacies are separate corporations, there is no need to take that fact into account in connection with this matter; all profits and losses belong to Red Co.)

(1) A sales contract for a total of 250,000 cases of medicine had been established between Red Co. and Blue Inc.

(2) If Blue Inc. had fulfilled its obligation to deliver 250,000 cases of medicine at the end of November, Red Co. would have had sales of ¥5,000,000,000, but instead Red Co.'s sales only amounted to ¥1,500,000,000.

(3) Since each ¥100,000,000 in sales results in profits of ¥1,000,000, Red Co. lost ¥35,000,000 in profits as a result of Blue Inc.'s failure to perform the contract.

(There is no dispute regarding the fact that each ¥100,000,000 in sales results in profits of ¥1,000,000. For purposes of simplification, in the calculation of sales and profits for this problem, it is assumed that total sales are equal to the number of cases sold multiplied by the price per case between Red Co. and Blue Inc. (i.e., ¥20,000 per case), and that each ¥100,000,000 in sales (i.e., each 5000 cases sold) results in profits of ¥1,000,000. There is no need to take into consideration the distribution costs, advertising expenses, etc., of Red Co. or Red Pharmacies. For purposes of simplification, it is assumed that the price at which the medicine is ultimately sold to consumers is identical to the price at which Red Co. purchases the medicine from Blue Inc.).

(4) Furthermore, 25,000 cases of medicine were left unsold, but the expiration date for the medicine has already passed and it must be destroyed. The fact

the medicine could not be sold is the result of Blue Inc.'s failure to perform the contract, so Blue Inc. should bear the ¥500,000,000 loss.

(5) Accordingly, Blue Inc. must pay Red Co. damages of ¥535,000,000.

In response, Blue Inc. made the following assertions:

(1) A contract was only established with respect to 100,000 cases of medicine. No contract of any sort was established by the faxes of October 30 and November 5.

(2) Even with regard to the 100,000 cases of medicine, the relevant events were caused by an unforeseeable calamity and, furthermore, resulted from guidance by the government of Arbitria, so Blue Inc.'s inability to deliver at the end of November was unavoidable and Blue Inc. bears no legal liability.

(3) Even assuming Blue Inc. might be found to bear some sort of legal liability with regard to the 100,000 cases of medicine, the limit of liability is at most the ¥5,000,000 in potential profits on the 25,000 cases that went unsold.

(4) The fact that 25,000 cases of medicine remained unsold is a result of Red Co.'s mistaken judgment in accepting delivery of 100,000 cases at the end of December, and has no connection to any failure in performance by Blue Inc.

11.

The two sides have undertaken a series of negotiations but have failed to make any headway. Alex and Dale have met face-to-face and considered various possible methods of breaking the deadlock, but the outside counsel for Blue Inc. was adamant that if the parties appear to be too conciliatory, Alex and Blue Inc.'s directors may be faced with a shareholders derivative suit. Accordingly, the outside counsel has recommended that the parties resolve the matter in accordance with the decision of a third party, through arbitration. In the end, Alex and Dale, after confirming that nothing would disrupt the mutual trust of their two companies, agreed to treat this as a purely legal matter on which they would defer to the judgment of a third party, through arbitration, while maintaining the collaborative relationship between the two companies.

ROUND A (Arbitration)

The arbitration of this matter will be conducted in accordance with UNCITRAL arbitration rules. In advance of the hearing, the arbitrators have directed each party to submit statements (not to exceed 2000 words), on or before a date to be designated separately, setting forth that party's assertions and the reasons for those assertions, with regard to the following three points:

1. What sort of contract was concluded between Red Co. and Blue Inc. with regard to the sale of influenza medicine?
2. Should Blue Inc. be excused from liability for failure to perform the sales contract referred to in the preceding question?
3. Assuming Blue Inc. is not excused from liability, what is the amount of damages for which Blue Inc. is liable?

At the hearing, the arbitrators first will receive opening statements of 15 minutes each from the two parties, beginning with Red Co., followed by Blue Inc. Thereafter, the hearing will focus on the above points. (At the hearing, the parties are free to refer to matters or arguments other than those set forth in their submitted statements, if they choose to do so.)

ROUND B (Negotiation)

1.

In the end, the arbitration shifted to mediation partway through, and the two companies agreed to a resolution in which they shared the sacrifices. Three years have elapsed since then; and it is now the year 2007. Yellow Co.'s research and development activities related to genetically modified human growth hormone derivatives have not achieved any earth-shattering breakthroughs, but those activities have resulted in a number of modest advances. One of these is the development of a substance that increases the effectiveness of Blue Inc.'s influenza medicine. Yellow Co. obtained a patent for that substance, and Blue Inc. successfully used it to develop a new medicine.

In another matter, in 2005, when Red Co. was suffering financial difficulties, Yellow Co. acquired 50% of the shares in Red Pharmacies, and the pharmacies were placed under the Yellow Co. umbrella. The name of the chain was changed to Yellow Pharmacies, and management of the chain was placed under an official sent from Blue Inc. At the time, sales figures at Yellow Pharmacies remained strong.

In 2006, however, trade friction between Negoland and Arbitria came to a head.

The background of the trade friction between the two nations is rather complicated. Fifty years ago the two nations had a war in which many people on both sides suffered. In Negoland, some media outlets have carried reports of xenophobic attitudes toward foreign culture in Arbitria. Arbitrian businesses have rushed headlong into new fields of medical technology, including experiments with human subjects, sales of body organs, in-vitro fertilization, and even cloning; this has stirred up feelings of unease and ill will among the conservative people of Negoland. These and other factors underlie the trade friction.

None of the above factors is really new; they all already existed when Red Co. and Blue Inc. began their collaboration. Over the past two or three years, however, exports of automobiles, steel and other products from Arbitria to Negoland have increased dramatically. In the automobile and steel sectors, in particular, numerous Negoland companies have gone bankrupt and many people have lost their jobs. The Negoland government implemented safeguards to limit imports of automobiles, steel and other products; but the Arbitrian government has denounced the safeguards and the dispute between the two nations has been taken to the WTO.

The governments in both nations have used the mass media to denounce the other side, and hostile attitudes toward the other nation have heightened among the people in both Negoland and Arbitria. Within Negoland, a boycott campaign against Arbitrian businesses was started. Because Yellow Pharmacies was under the umbrella of an Arbitrian company, it became one of the targets of the boycott. As a result, Yellow Pharmacies' performance has deteriorated. In 2006, Yellow Pharmacies suffered major losses, and major losses are again foreseen for 2007. Yellow Co. itself has also begun to come under severe scrutiny, and it has become difficult to procure some of the material needed for research in Negoland. The morale of Yellow Co. employees has suffered. A number of researchers have requested that they be allowed to return to Red Co. right away; and several researchers have been recruited away from Yellow Co. by competing companies. As a result, it has become impossible for Yellow Co. to continue its research and development activities.

Meanwhile, at Blue Inc., Dale resigned to take responsibility for a failed project in the United States. Dale's replacement as president is Jamie Miller. Alex met with Jamie, and they agreed that liquidation of Yellow Co. was unavoidable. They have directed the officials responsible at their respective companies to undertake negotiations to work out the concrete details of the liquidation. (Note: The president of Blue Inc. is different for Round A and Round B. However, the same team member should play the role of president in both Rounds, serving as Dale for the arbitration in Round A and as Jamie for the negotiation in Round B.)

The balance sheet of Yellow Co. immediately prior to liquidation, as prepared jointly by Red Co. and Blue Inc., is as follows:

Million Yen

Assets			Liabilities		
Current assets		2,300	Current liabilities		3,500
(Breakdown)	Cash and deposits	200	(Breakdown)	Accounts payable	1,000
	Accounts receivable	1,000		Short-term loans	2,500
	Inventory & materials	1,000		Other	320
	Other	100			
Fixed assets		2,320	Fixed liabilities		1,800
(Breakdown)	Real property	1,000	(Breakdown)	Long-term loans	1,800
	Machines & equipment	800	Capital		(-1,000)
	Patents	10	(Breakdown)	Capital	1,000
	Investment in securities	500		Earned surplus	(-2,000)
	Other	10			
Total assets		4,620	**Total liabilities and capital**		4,620

Notes Short-term loans and long-term loans are all from Blue Inc.

Accounts receivable are all from a major US pharmaceuticals company.

The breakdown of Inventory & materials is as follows: inventory of finished products 700, inventory of unfinished products 150, materials 150.

Investment in securities consists entirely of stock in Yellow Pharmacies. That investment is valued at the acquisition price.

2.

First, one problem is how to deal with the stock of Yellow Co. Furthermore, as one can see from the above balance sheet, Yellow Co. has many debts, and another serious problem is how to allocate those debts between Red Co. and Blue Inc.

3.

The initial negotiation session between the representatives of the two companies has taken place. Initially, they held discussions aimed at determining what matters need to be agreed upon between the parties in connection with the liquidation of Yellow Co. In that regard, in addition to the abovementioned problems of the disposition of Yellow Pharmacies and the allocation of debts, other problems requiring resolution included the treatment of about fifty remaining researchers and the disposition of the results of research.

With regard to the reasons why Yellow Co. has not produced any path-breaking research results and why Yellow Co. was burdened with major losses and thereby forced to liquidate, the positions of the two sides were sharply opposed.

According to Red Co.'s position, the few Blue Inc. employees who were dispatched to Yellow Co. were primarily administrators who never sought to learn the language of Negoland and were overbearing in their personnel management. Through their actions and attitudes, these Blue Inc. administrators offended the employees seconded from Red Co., who made up the bulk of the Yellow Co. workforce, and undermined the morale of the Yellow Co. workforce. Moreover, a weekly magazine carried a report, written by one of employees seconded from Red Co., about the discriminatory treatment and oppression of Nego employees by the administrators dispatched from Blue Inc. This unfair treatment of Nego employees seems to be one of the reasons Yellow Co. was targeted by the anti-Arbitria movement. Accordingly, responsibility for the losses that have forced Yellow Co. to liquidate lies with Blue Inc.

In contrast, Blue Inc.'s position is that it entered into the collaboration with Red Co. from a long-term perspective, seeking to establish a foothold for entry into the huge Negoland market, and at the time the two companies entered the collaboration it was unforeseeable that anti-Arbitria sentiment would grow this strong and lead to severe trade friction. The employees sent by Blue Inc. to Yellow Co. reported that the researchers who came from Red Co. acted as though they had been demoted and were unmotivated; Red Co. should have sent better researchers, they said. Moreover, the facilities provided for or arranged by Red Co. were somewhat obsolete; the additional costs needed to undertake cutting-edge biotech research and production of drugs vastly exceeded original projections. The above conduct by Red Co. violated the contract connected with the establishment of Yellow Co.; and Red Co. bears responsibility for the fact Yellow Co. was not able to achieve adequate results and thereby was forced into liquidation.

The first negotiation session between the parties was occupied completely by the above points, and no substantive discussions have occurred with regard to any other matters.

4.

So as not to delay the liquidation, it has been agreed that the two parties will undertake a comprehensive negotiation of all issues at one time, including the abovementioned disposition of Yellow Pharmacies and the allocation of debts, the treatment of the remaining researchers, the disposition of all assets and liabilities, and any other matters requiring resolution. It has been agreed that, from each company respectively, the president and vice president, the head of the medical products department, the head of the research and development department, the head of the intellectual property department, and the head of the legal department will all meet together in Japan to conduct the negotiations. At the conclusion of the negotiations, a memorandum of agreement is to be prepared and signed by the presidents of both companies.

Attachment 1 (Excerpts from Joint Venture Agreement)

Cross-border Joint Venture Agreement

THIS AGREEMENT made as of March 1, 2002 by and between
Red Pharmaceuticals Co., Ltd., a corporation duly incorporated and existing under the laws of Negoland, having its principal place of business at….., Negoland ("Red") and Blue Technology, Inc., a company duly incorporated and existing under the laws of Arbitria, having its principal place of business at …., Arbitria ("Blue").

Witnesseth:

WHEREAS Red is engaged in the business of research and production of medicines and has a subsidiary which is engaged in the business of retail store of medicines and other convenience goods in Negoland,
WHEREAS Blue is engaged in the business of research, production and sales of chemical products, foods and medicines, and
WHEREAS Red and Blue wish to cooperate in development and production of medicines, especially medicines using genetic engineering, as well as in marketing of products of Blue in Negoland, to further the common interests of the parties,

THE PARTIES AGREE as follows:

1. Definitions

1.1 In this Agreement, a) words in singular number include the plural and in the plural include the singular unless the context otherwise requires and b) words of masculine gender include feminine, and words of feminine gender include masculine, when circumstances so require.
1.2 In this Agreement, "Technology" means any design, invention, development, improvement, process, know-how, data, formula, technical information, system and/or software relating to medicine possessed by the parties and/or any of their subsidiaries as well as Yellow and protected or capable of being protected as intellectual property.

2. Joint Venture Company

2.1 By the end of December 2002, Red and Blue shall cause incorporation and commencement of operations of a joint venture company in Negoland, to be named Yellow Co., Ltd. ("Yellow").

2.2 The aim of Yellow is to research, develop and produce new medicines, especially medicines using genetic engineering.

2.3 Red will provide staff, Technology, equipment and facilities and Blue will provide funds necessary for Yellow to commence highly advanced research.

3. Incorporation of Yellow

3.1: The objects of Yellow are to engage in i) development and production of medicines, especially genetically modified medicines, and ii) other business relating or incidental to the foregoing.

3.2 The initial paid-in capital of Yellow shall be Yen 1,000,000,000. Red shall contribute Yen 300,000,000 and Blue shall contribute Yen 700,000,000.

3.3 Transfer of Yellow shares shall be subject to the approval of the Board of Directors of Yellow.

4. Corporate Governance of Yellow

4.1 As the organs of the company, Yellow shall have 1) Meeting of Shareholders, 2) Board of Directors, 3) Representative Director and 4) Statutory Auditor.

4.2 The number of the members of the Board of Directors shall be four. Two directors shall be nominated by Red and the remaining two by Blue.

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6. Important Corporate Actions of Yellow

6.1 The following actions shall require an affirmative vote of a Meeting of the Board of Directors:

a) Adoption and modification of annual business plans, budgets and capital expenditure budgets;

b) Borrowing, lending or extending credit, at any one time, in excess of Yen 10,000,000;

c) A transaction which would cause the total borrowing, lending, credits, guaranty and indemnity outstanding to exceed Yen 110,000,000;
d) Entering into agreements to employ a person for a remuneration in excess of Yen 50,000,000 per year;
e) Any agreement relating to intellectual property rights;
f) Initiating or terminating litigation, arbitration or administrative proceedings;
g) Any decision which would materially affect the scope of business of Yellow or which would materially affect the financial condition of Yellow.
6.2 The following actions shall require unanimous vote of the shareholders of Yellow:
a) Amendment to the Articles of Incorporation;
b) Change in the number of shares Yellow is authorized to issue;
c) Creating different classes of shares including preferred shares;
d) Listing and delisting of the shares of Yellow on a stock exchange;
e) Sale, transfer or disposal of a material part of the business or assets of Yellow;
f) Dissolution or liquidation of Yellow.

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8. Transfer of Shares

8.1 Either Red or Blue may sell all of its shares in Yellow (and only all of its shares) to the other party. The offer shall be in writing and shall set forth the price. The offeree shall have an exclusive option for a period of 45 days to buy the shares at a price not lower than the offered price.
8.2 In the event the offeree fails to exercise its option within the applicable period above, and only in that event, the offeror shall be free to sell all the offered shares to a third party at a price not lower than the price earlier offered to the other party. If sale does not take place within forty days following the expiration of the abovementioned applicable period, the offeror shall forgo the sale or this Agreement shall terminate.
8.3 In the event of the sale of shares by either party, Yellow shall change the name of the company to reflect the change in ownership.
8.4 Neither party may pledge any shares of Yellow without the prior written approval of the other party.

9. Business Plan and Budget

9.1 The Representative Director each year shall submit to the Board of Directors detailed reports of the business activities and financial conditions of the company and shall also submit for approval a business plan and budget for the following year. If the parties fail to agree on the business plan and budget for the following year, the dissatisfied party may propose purchase of that party's entire share by the other. Unless the offeree promptly responds favorably, the process provided for dealing with deadlock shall be followed as expeditiously as possible depending on the urgency of the matter.

. . .

11. Deadlock

11.1 If a decision is not made at a Meeting of Shareholders or by the Board of Directors because of a tie vote, the representatives named thereat, possibly including an outside director, shall seek to find a way of resolving the relevant issues. If they are not successful after three business days, the matter shall be referred to a meeting of the top managements of the parties. If the meeting of the top managements fails to resolve the deadlock expeditiously, this Agreement shall at that point terminate.

. . .

14. Marketing

14.1 Red shall cooperate to promote the sale of products of Blue in Negoland.

14.2 Red shall cause its subsidiary, Red Pharmacy, to sell some products of Blue in its stores and to exert its best efforts to increase the sale of those products in Negoland.

14.3 Blue shall give orders by Red first priority and shall exercise its best efforts to meet the requirements of Red.

14.4 The products to be handled by Red Pharmacy shall be decided by mutual agreement by Red and Blue, but shall include hair tonic and diet foods.

. . .

15. Technology

15.1 Red and Blue mutually shall fully disclose all Technology which may be necessary for research and development by Yellow.
15.2 Unless otherwise provided in the ancillary agreement on intellectual property, any Technology developed by Yellow shall be freely used by the parties

16. Confidentiality
16.1 Each party shall keep in confidence and shall bind all the employees of Red, Blue and Yellow to keep in confidence all Technology disclosed to it other than information
a) which is generally available to the public at the time of disclosure;
b) which has become generally available to the public through no fault of the receiving party;
c) which the receiving party can show was in its possession before the disclosure; or
d) which the receiving party can show was received from any person without an obligation of confidentiality.

17. Force Majeure
17.1 In the event of any failure or delay in the performance of this Agreement due to war, civil commotion, labor dispute, fire, natural disaster, or any other cause whatsoever beyond the reasonable control of a party so affected, said party shall not be liable for such failure or delay, or results thereof. Upon the occurrence of any of the above events, the party affected by such event shall, without delay, notify in writing the other party of the same, and the parties hereto shall meet and discuss appropriate or necessary steps or actions to be taken to cope with the situation.

18. Assignment
18.1 Attempted assignment of any right or obligation under this Agreement without prior written approval of the parties shall be void.

19. Termination of the Agreement
19.1 This Agreement shall terminate when:
a) Sale of shares has failed and the offeror chooses to terminate;
b) Failure to agree on the business plan and budget has occurred and the effort to resolve deadlock has not been successful;

c) Material breach of this Agreement is not cured within 30 days and the party not in breach chooses to terminate;
d) Red and Blue agree on termination;
e) Material change in the ownership or control of either of the parties occurs;
e) Liquidation of Red or Blue voluntarily or otherwise; insolvency or bankruptcy of Red or Blue; or
f) Any resolution of the Meeting of Shareholders requiring termination.

20. Settlement of Disputes and Governing Norms

20.1 Any dispute, controversy or difference which may arise between the parties out of or in relation to or in connection with this Agreement or for the breach thereof shall be amicably settled by consultation among the parties.
20.2 All such disputes, controversies and differences, if not settled amicably, shall be finally settled by arbitration to be held at Tokyo under UNCITRAL Arbitration Rules by two arbitrators.
20.3 In resolving disputes, the arbitrators shall take into consideration the UNIDROIT Principles of International Commercial Contracts and shall apply rules of reason that the arbitrators find applicable.

21. Miscellaneous

21.1 This Agreement does not limit either party from independently engaging in activities involving the same subject matter as the present joint venture.

• • •

IN WITNESS WHEREOF,

Red Pharmaceuticals Co., Ltd.	Blue Technology, Inc.
By:	By:

Attachment 2 (Excerpts from Sales Contract)

CONTRACT

THIS CONTRACT is made as of the 10th day of October, 2003 by and between Red Co., Ltd., a corporation duly incorporated and existing under the laws of Negoland, having its principal place of business at….., Negoland ("BUYER") and Blue Technology, Inc., a company duly incorporated and existing under the laws of Arbitria having its principal place of business at …., Arbitria ("SELLER")

TNE BUYER AND SELLER AGREE AS FOLLOWS:

1. The SELLER shall sell and deliver to the BUYER, and the BUYER shall purchase from the SELLER the medicine for influenza produced by the SELLER as more fully described in Exhibit A, which is attached hereto and made an integral part hereof (the "Medicine").
2. The SELLER shall deliver 100,000 cases of the Medicine on CIF port of Discour, Negoland, by 30 November, 2003.
3. The price of the Medicine shall be Yen 2,000,000,000. The Buyer shall pay the Seller the price of the Medicine by way of remittance to the bank account designated by the Seller.

• • •

7. Neither the SELLER nor the BUYER shall be held responsible or deemed in default for any failure or delay in performance of this Contract due to cause or causes beyond the responsible control of such party, including, but not limited to, acts of God or the public enemy, strikes, labor disturbances, or compliance with any national or local law or regulation.

• • •

10. This Contract shall not be assigned by either party without prior written approval of

the other party.

11. (a) All disputes, controversies and differences, which may arise between the parties hereto out of or in relation to or in connection with this Contract, shall be finally settled by arbitration to be held at Tokyo under UNCITRAL Arbitration Rules by two arbitrators.

(b)In resolving disputes, the arbitrators shall take into consideration the UNIDROIT Principles of International Commercial Contracts and apply rules of reason that the arbitrators find applicable.

IN WITNESS WHEREOF,

Red Pharmaceuticals Co., Ltd	Blue Technology, Inc.
By:	By:
Head of Medical Products Dept.	Head of Medical Products Dept.

Attachment 3

Red Co.
Head, Medical Products Department

October 30, 2003

Blue Inc.
Head, Medical Products Department

Dear Sir:

The other day, based on a forecast by the Negoland Public Health Ministry, we sent an order to you for 100,000 cases of influenza medicine (value: ¥20,000 per case). Today, however, the Public Health Ministry issued a new forecast. According to that forecast, a New Type X influenza, fundamentally of the same type as the original Type X influenza, but twice as infectious, is expected to cause a major epidemic in Negoland this year. It has been confirmed that the same medicine used to treat Type X influenza will also be effective in treating New Type X influenza, but, due to the greater infectiousness of New Type X influenza, it appears that we will have to order a substantial additional amount of your influenza medicine. We will continue to collect all possible information and will maintain close communication with you, but at the current time we would like to increase our original order by an additional 150,000 cases of medicine. We will inform you separately regarding the date for delivery. We greatly appreciate your continued cooperation.

Sincerely yours,

Attachment 4

Blue Inc.
Head, Medical Products Department

November 5, 2003

Red Co.
Head, Medical Products Department

Dear Sir:

This is in response to your fax dated October 30, 2003.

We at Blue Inc. also had obtained the forecasts issued by the Negoland Public Health Ministry. The forecast made by Blue Inc.'s own expert had matched the announcement made by the Negoland Public Health Ministry, namely, that an epidemic of New Type X influenza was foreseen. Blue Inc. has already increased production levels for the influenza medicine, and you can rest assured that we have established production capacity sufficient to meet orders from Red Co., up to approximately 300,000 cases of medicine. We await further instructions from you.

Sincerely yours,

Attachment 5

Blue Inc.
Head, Medical Products Department

November 16, 2003

Red Co.
Head, Medical Products Department

Dear Sir:

I assume you may already have heard the news, but Arbitria has suddenly been hit by a major epidemic of New Type X influenza. As a result, domestic demand for Blue Inc.'s medicine has skyrocketed. We are already exerting all of our efforts to increase production, but we must inform you that, given the current situation in Arbitria, it will be difficult for Blue Inc. to completely meet both domestic demand and the order from your company. Blue Inc. is currently investigating all possible options, including the possibility of converting one of our overseas factories to the manufacture of influenza medicine; but government authorities here in Arbitria have directed Blue Inc. to give priority to meeting domestic needs, and we foresee that there will be no way around delaying the delivery to your company scheduled for the end of November. We are extremely sorry, but we must request your understanding of the urgent situation in Arbitria.

We will continue to keep you fully informed of all developments.

Sincerely yours,

Attachment 6

Red Co.
Head, Medical Products Department

November 17, 2003

Blue Inc.
Head, Medical Products Department

Dear Sir:

We have read your fax of November 16. We are very sorry to hear of the influenza epidemic in Arbitria. We pray the epidemic will abate very soon.

That said, Negoland seems certain to face a major epidemic of its own, and we must receive performance of Red Pharmacies' recent order for 100,000 cases of influenza medicine. We understand the situation in Arbitria, but we cannot consent to any alteration in the terms of that contract, including the date for delivery.

Furthermore, it is Red Co.'s understanding that, in accordance with our fax of October 30, Red Co. has ordered an additional 150,000 cases of medicine, and that, pursuant to your fax of November 5, Blue Inc. has accepted that order.

Accordingly, we hereby request delivery of 250,000 cases of medicine no later than the last day of November.

Sincerely yours,

Attachment 7

Blue Inc.
Head, Medical Products Department

December 15, 2003

Red Co.
Head, Medical Products Department

Dear Sir:

We are very sorry for the trouble we have caused you by the delay in delivery of influenza medicine. I am writing to inform you that we at last have been able to begin production at an overseas factory, and we will be able to deliver 100,000 cases of medicine to you by the end of December.

Sincerely yours,

Attachment 8

Red Co.
Head, Medical Products Department

December 17, 2003

Blue Inc.
Head, Medical Products Department

Dear Sir:

We have read your fax of December 15, 2003. Please deliver the medicine as soon as you possibly can. Please cancel our order for the additional 150,000 cases of medicine, however, since the market conditions have changed.

As you will understand, we at Red Co. feel we have no choice but to demand compensation from Blue Inc. for all losses we have suffered on this occasion. Accordingly, we must inform you that our acceptance of the upcoming delivery does not in any way constitute an abandonment of any of our legal rights.

Sincerely yours,