Chocolate Case

<Issue 1> Whether Red Corp. ("Red") is under obligation to reimburse US$1 million to Blue Inc. ("Blue").

-Red's Claim-

Red is not under obligation to reimburse US$1 million to Blue.

-Expected Claim of Blue-

Blue is expected to claim that Red is under the obligation because of the non-performance of Article ("Art.")1 and Art.3.2 of the sales agreement dated December 10, 2013 ("Contract").

-Legal Basis-

<u>Obligation stipulated in Art.3.2 of the Contract</u>

I. According to Art.3.2 of the Contract, Red had an obligation to ship the Chocolate worth US$3 million ("the Goods") no later than January 10.

II. In this case, Red did not fail to perform its obligation, based on UNIDROIT Principle ("U") 5.3.1.

<u>Obligation stipulated in Art.1 of the Contract</u>

I. According to Art.1, Red had an obligation to deliver the Goods to Blue.

II. Red performed its obligation, based on Art.3.1 of the Contract.

III. Even if Red did not perform its obligation, Red is not liable for the non-performance based on Art.6 of the Contract.

<u>Obligation stipulated in Art.3.2 of the Contract</u>

I. According to Art.3.2 of the Contract, Red had an obligation to ship the Goods no later than January 10.

II. In this case, Red did not fail to perform its obligation, based on U5.3.1.

1. According to U5.3.1, *"…a contractual obligation may be made conditional upon the occurrence of a future uncertain event, so that the contract or the contractual obligation only takes effect if the event occurs (suspensive condition)…"*

2. Art.3.2 of the Contract has a condition that the letter of credit ("L/C") is advised enough before the deadline of shipment to perform the obligation, based on U4.1 and U4.3.

   (1) According to U4.1 (1), *"A contract shall be interpreted according to the common intention of the parties."*

   According to U4.3, in applying U4.1, regard shall be had to all the circumstances, including items listed in U4.3 (a) to (f).

(d) the nature and purpose of the contract

Based on Art.2 of the Contract, the payment transaction was supposed to be made by L/C. In a payment transaction by L/C, L/C works to secure the payment to the exporter by getting commitment from a bank. Judging from the nature of the transaction, shipment should be made after L/C is advised.

In addition, 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" (Exhibit 9). Similar precedents are seen in U.S. and Japan.

These precedents also prove the nature of L/C as stated above.

(a) preliminary negotiations between the parties

Secondly, in the negotiation for this transaction, Red and Blue chose payment by L/C over by remittance after the receipt of the goods (¶ 29). Judging from the fact, both Red and Blue had understood the nature of L/C above.

Thus, Red and Blue had the common understanding that L/C shall be advised before the deadline of shipment.

(2) Hence, based on the common understanding, Red's obligation as stipulated in Art.3.2 of the Contract has the condition that L/C is advised enough before January 10 to perform the obligation.

3. In this case, the condition did not occur.

   L/C was advised on January 10 (¶ 31). Judging from the fact that it takes two full days from the receipt of L/C to the completion of loading (¶ 31), L/C was not advised enough before January 10 to perform the obligation.

4. Therefore, Red did not fail to perform the obligation stipulated in Art.3.2 of the Contract.

<u>Obligation stipulated in Art.1 of the Contract</u>

I. According to Art.1 of the Contract, Red had an obligation to deliver the Goods to Blue.

II. Based on the interpretation of Art.3.1 of the Contract, Red performed its obligation.

   1. According to Art.3.1 of the Contract, Red's obligation to deliver the Goods was fulfilled when Red handed over the Goods to the carrier in a transport by aircraft.

According to Art.3.1 of the Contract, the trade term is CFR (Incoterms ® 2010), Port of Abab.

According to A4 of CFR, Incoterms® 2010, *"The seller must deliver goods either by placing them on board vessel…"*

According to GUIDANCE NOTE of CFR® 2010, "*When CPT, CIP, CFR, or CIF are used, the seller fulfills its obligation to deliver when it hands over to the carrier in the manner specified in the chosen rule and not when the goods reach the place of destination."*

Thus, the term "by placing them on board the vessel" in A4 of CFR has a meaning that the seller's obligation to deliver is fulfilled when the goods are handed over to the carrier.

Hence, if CFR is used for the transport by aircraft, in which the goods are handed over to the carrier before they are placed on board, it is appropriate for the purpose of CFR, to think that the seller fulfilled its obligation when the goods are handed over to the carrier.

2. In this case, Red and Blue agreed on transport by air cargo (¶ 32), and Red handed the Goods over to the carrier of air cargo. (¶ 33)

3. Therefore, Red performed its obligation.

III. Even if Red did not perform its obligation, Red is not liable for the non-performance based on Art.6 of the Contract.

1. According to Art.6 of the Contract, neither party shall be liable for failure to perform any obligation under the Contract to the extent that such failure is attributable to force majeure that is beyond the reasonable control of the party affected.

2. In this case, Red could not deliver the Goods because half amount of the Goods were struck by lightning while they were in cargo warehouse due to the mechanical problem of aircraft (¶ 33).

3. Lightning and the mechanical problem are beyond the reasonable control of Red.

   Lightning is a kind of natural disasters and Red could not do anything to prevent the mechanical problem nor the temporary storage of Negoland Air.

4. Hence, Red's failure is attributable to force majeure.

5. Thus, Red is not liable for its non-performance based on Art.6 of the Contract.

Therefore, Red is not under obligation to reimburse US$1 million to Blue.

<Issue 2>Whether Blue is under obligation to pay US$1.5 million for the chocolate and US$500,000 under the Contract.

-Red's Claim-

Blue is under two obligations under the Contract: to pay US$1.5 million for the chocolate and to pay US$500,000 under the Contract.

-Legal Basis-

Obligation to pay US$1.5 million for the chocolate

I. Art.2 of the Contract stipulates Blue's obligation to pay US$3 million for the Goods.

II. In this case, Blue did not perform the obligation.

III. Thus, based on Art.2 of the Contract, Red demands Blue to pay US$1.5 million to Red.

Obligation to pay US$500,000

I. According to Art.5 of the Contract, Blue has an obligation to reimburse the freight rate for air cargo worth US$500,000 within a reasonable time after demand.

II. In this case, Blue did not perform the obligation.

III. Thus, based on Art.5 of the Contract, Red demands Blue to pay US$500,000 to Red.

Obligation to pay US$1.5 million for the chocolate

I. Art.2 of the Contract stipulates Blue's obligation to pay US$3 million for the Goods.

II. In this case, Blue did not perform the obligation.
Despite the obligation, Blue only paid US$1.5 million to Red (¶34). Therefore, Blue did not complete its obligation stipulated in Art.2 of the Contract.

III. Thus, based on Art.2 of the Contract, Red demands Blue to pay US$1.5 million to Red.

-Expected Counterargument of Blue-

I. Blue is expected to claim that Blue is not under the obligation because of the termination of the Contract based on U7.3.1.

II. However, such claim is not acceptable by following reasons:

1. As stated above, Red did not fail to perform its obligation to deliver the Goods, based on Art.3.1 of the Contract.

2. Even if Red did not perform the obligation, Blue may not rely on Red's non-performance based on U7.1.2.
   (1) "*A party may not rely on the non-performance of the other party to the extent that such non-performance was caused by…another event for which the first party bears the risk.*" (U7.1.2)
   (2) In this case, Red failed to deliver the Goods to Blue because of the lightning.
   (3) Blue shall bear the risk of lightning, based on the understanding of CFR.

   Art.3.1 of the Contract stipulates that trade term is CFR (Incoterms ® 2010).

   As stated above, according to CFR, the risk of damage to the Goods was transferred from Red to Blue when the Goods are handed over to the carrier.

   In this case, the Goods were handed over to the freighter, Negoland Air (¶ 33).

   Thus, Blue shall bear the risk of lightning.

3. Hence, based on U7.1.2, Blue may not rely on Red's non-performance.

Therefore, Blue's counterargument is not acceptable.

<u>Obligation to pay US$500,000</u>

I. According to Art.5 of the Contract, Blue has an obligation to reimburse the freight rate for air cargo worth US$500,000 within a reasonable time after demand.

1. Art.5 of the Contract stipulates Blue's obligation to reimburse any new freight rates to Red within a reasonable time after demand.

2. In this case, Red paid US$500,000 for the freight charge for air cargo in order to deliver the Goods to Blue (¶33).

3. The cost for the air cargo shall be deemed to be a new freight rate stipulated in Art.5 of the Contract.
   (1) Red and Blue first supported transport by vessel when the Contract was terminated. However, through the conversation between Swan and Emerald, they finally agreed to use the air cargo as means to deliver the Goods (¶ 32).
   (2) As a result, the freight rate for air cargo was newly incurred by Red to deliver the

Goods.

(3) Thus, the cost for air cargo shall be deemed to be the new freight rate stipulated in Art.5 of the Contract.

4. Therefore, Blue has an obligation to reimburse to Red US$500,000, the amount Red incurred for air cargo, within a reasonable time after demand.

II. In this case, Blue did not perform the obligation.
Blue did not reimburse to Red US$500,000 within the reasonable time after demand as stipulated in Art.5 (Exhibit 9).

III. Thus, based on Art.5 of the Contract, Red demands Blue to pay US$500,000 to Red.

Therefore, Blue is under obligation to pay a total of US$2 million.

M&A Case

＜Issue 1＞ Whether Blue is in breach of its obligation stipulated in Art.4 of the Stock Purchase Agreement ("SPA") dated December 15, 2012 in connection with its representations and warranties, and how much should be the amount of damages if Blue was in breach.

-Red's Claim-

Blue is in breach of its obligation stipulated in Art.4 of SPA with representations and warranties, and the damages amount to US$30 million.

-Legal Basis-

I. Art.4.1 (xiii) of SPA stipulates that Blue shall represent and warrant that no adverse change is threatened to Blue Drink Inc. ("TARGET") or its business as of the execution of SPA.

II. In this case, Blue breached its obligation stipulated in Art.4.1 of SPA.

III. Based on Art.4.2 of SPA, Red demands Blue to pay US$30 million to Red.

I. Art.4.1 (xiii) of SPA stipulates that Blue shall represent and warrant that no adverse change is threatened to the TARGET or its business as of the execution of SPA.

II. In this case, Blue breached its obligation stipulated in Art.4.1 (xiii) of SPA.

1. Revocation of "Designated Health Food" status ("Status") shall be deemed to be the adverse change of the TARGET.

Blue Slim got the Status when it was released in 2010. This status may have contributed to healthy sales of the product in Arbitria (¶ 9).

Hence, the revocation of the Status has a negative effect on the sales of Blue Slim, which is the main business of the TARGET.

2. There was a threat of revocation of the Status as of the execution of SPA.

   In this case, the TARGET had received complaints from select consumers linking overconsumption of Blue Slim to stomach problems since early 2012, which is before the execution of SPA (¶ 39).

   Receiving similar complaints, Arbitria's Ministry of Health and Welfare ("Ministry") also warned the TARGET that the Ministry would keep an eye on any new development (¶39).

   As a result, it was reported to the board of directors of the TARGET that it would need to monitor the matter carefully, fearing that the Ministry could take away the Status from Blue Slim by siding with consumers suggesting any possibility of upset stomach (¶ 39).

3. Therefore, Blue breached the representation and warranty stipulated in Art.4.1 (xiii) of SPA.

III. Based on Art.4.2 of SPA, Red demands Blue to pay US$30 million to Red.

1. Red reasonably specified the contents of claim by a letter dated June 10, 2014 (Exhibit 14).

2. Thus, based on Art.4.2 of SPA, Blue shall bear the responsibility.

   The revocation of the Status caused Red the loss of the sales amount totaling US$300 million which resulted in the loss of profit of US$30 million at least (Exhibit 14).
   Three years have not passed from January 15, 2013.

Therefore, based on Art.4.2 of SPA, Blue is under obligation to pay US$30 million to Red.

<Issue 2> Whether Blue is in breach of Art.9 of SPA and is obliged to pay US$500,000 as damages. Whether Blue has to revoke the investment of US$5 million to Arbitria Coffee ("AC").

-Red's Claim-

Blue is in breach of Art.9 of SPA and is obliged to pay US$500,000 as damages. Blue has to revoke the investment of US$5 million to AC.

-Legal Basis-

I. According to Art.9.1 (i) of SPA, Blue has an obligation not to directly or indirectly participate in or perform service for a business similar to or competitive with a business conducted by the TARGET for a period ending on the 5th anniversary of the Closing Date.

II. Blue breached its obligation.

III. Based on Art.9.2 of SPA, Red demands Blue to revoke the investment of US$5 million to AC and pay US$500,000 as liquidated damages.

I. According to Art.9.1 (i) of SPA, Blue has an obligation not to participate in or perform service for a business similar to or competitive with the business conducted by the TARGET for a period ending on the 5th anniversary of the Closing Date.

II. Blue breached its obligation.

In this case, Blue invested US$5 million to AC and became a shareholder of AC (¶ 36).
Blue also let AC use the research facility of Central Research Center for the R&D of a coffee beverage with weight loss benefit ("Product") from February to August 2014 (¶ 36).

Those actions of Blue shall be deemed to be violation of Art.9.1 of SPA for the following reasons:

1. The business of AC is competitive with the business of the TARGET.

No competition provision in a stock purchase agreement was set forth to prevent the buyer from managing a business competitive with the business transferred from the seller to the buyer, and harming the seller in the market. Thus, "competitiveness" shall be judged based on whether there is a fear of conflicts of interest between business of the seller and the buyer in the market.

In this case, the Product is supposed to be sold in Arbitria so as Blue Slim (¶36). Additionally, the Product has similar benefits and price range to Blue Slim (¶36).

Judging from those facts, the Product and Blue Slim are compared by the customers in Arbitria who consume beverages for weight loss within the same price range. Thus, the sales increase of the Product can lead to the sales decrease of Blue Slim, which means there is a fear of conflicts of interest.

Hence, the Product, a business of AC, is competitive with Blue Slim, which is the main business of the TARGET.

2. Blue performed service for R&D of the Product.

   Blue accepted the investment of US$5 million to AC when Jackson, the CEO of AC, asked Blue for the fund to embark on the serious R&D of the Product (¶ 36).

   Blue also let AC use the research facility of the Central Research Center, which gave AC the ideal condition for the development for the Product (¶ 36).

   Thus, Blue helped AC develop the Product.

3. Blue indirectly participates in the business of AC.

   Blue invested US$5 million to AC and became its shareholder and one non-executive board member joined the board from Blue in exchange of the investment (¶ 36).

   Thus, Blue is in a position able to indirectly manage the business of AC by attending shareholder meeting and to participate in the management of AC through the board member.

Therefore, Blue breached its obligation as stipulated in Art.9.1 of SPA.

III. Based on Art.9.2 of SPA, Red demands Blue to revoke the investment of US$5 million to AC and to pay US$500,000 as liquidated damages.

1. *"In the event BLUE violates any of its obligations under this Article 9, RED…shall be entitled…to…final injunctive relief against BLUE...to prevent any violations of this Article 9…"* (Art.9.2 of SPA)

   As stated above, Blue breached its obligation under Art.9 of SPA.
   To prevent the violation, Blue shall revoke the investment of US$5 million to AC.

2. *"…RED is entitled to request BLUE to pay US$500,000 as liquidated damages."* (Art.9.2 of SPA)

Therefore, based on Art.9 of SPA, Red demands Blue to revoke the investment of US$5 million to AC and pay US$500,000 as liquidated damages.

<Issue 3> Whether Red is under obligation to pay an additional Stock Purchase Price as stipulated in Art.2.2 of SPA, and how much should be the amount if such payment is found to be due.

-Red's Claim-

Red is not under obligation to pay an additional Stock Purchase Price as stipulated in Art.2.2 of SPA.

-Expected Claim of Blue-

Blue is expected to demand Red to pay US$200 million based on Art.2.2 and Art.8 of SPA.

-Legal Basis-

I. According to the provision of Art.8 of SPA, Red may make any reasonable business judgment to operate the TARGET after the Closing Date.
II. In this case, Red's operations shall be deemed to be reasonable business judgments.
III. Therefore, Red is not liable to pay US$200 million to Blue.

I. According to the provision of Art.8 of SPA, Red may make any reasonable business judgment to operate the TARGET after the Closing Date.

According to Art.8 of SPA, *"RED shall not operate…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."*

Thus, Red does not violate Art.8 of SPA to the extent that Red makes reasonable business judgment to operate the TARGET.

II. In this case, Red's operations shall be deemed to be reasonable business judgments.

Red made two business judgments: distributor contract at 40% of standard price, and acceptance of Orange's resignation.

1. Distributor contract at 40% of standard price

Red made contract with Nego Drink for the distributor of Red Energy and Red Slim on condition of 40% of standard price and a two-year contract(¶25).

(1) Red chose Nego Drink as its distributor over Negoland Bottlers.

Nego Drink is a leading beverage company in Negoland with strong vending machines sales (¶23), while Negoland Bottlers is a leading beverage distributor that has a network with retailers such as supermarkets (¶24).

Red considered it more important for its long-term interest to achieve popularity than to sell at higher price (¶25).

In order to achieve popularity, it is better to rely on vending machine sales in Negoland, because soft drink vending machines are everywhere in Negoland, where soft drink sales through vending machines account for a high percentage (¶23).

Thus, it was reasonable that Red chose Nego Drink over Negoland Bottlers.

(2) Red agreed with Nego Drink on the 40% of standard price.

As stated above, Red considered it more important for its long-term interest to achieve popularity than to sell at higher price (¶ 25).

By providing the drinks in low price, it is more likely that the distributor would increase the purchase volume, leading to the increase in the quantity throughout the market. This reflects Red's intention to achieve high popularity.

Thus, it was reasonable that Red agreed on the condition of 40% of standard price and a two-year contract.

2. Acceptance of Orange's resignation

Orange resigned because his claim of extension of research period and increase of budget was not accepted by Joe Lee, the CEO of the TARGET, and Crane, Director of Corporate Planning at Red (¶ 35).

Significant amounts of funds were needed in 2013 and 2014 to launch production and management facilities in Negoland, in addition to massive advertising promotions among others (Exhibit 4).

Thus, Red could not afford to make the research period any longer nor increase the budget for R&D.

Hence, it was reasonable that Joe Lee and Crane refused the extension of the research period and the increase of budget, and let Orange resign.

Consequently, Red's operations of TARGET shall be deemed to be reasonable business judgments.

III. Therefore, Red is not liable to pay US$200 million to Blue.