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COMMITTEE ON CONSTITUTIONAL AND LEGAL MATTERS

Eighty-eighth Session

Rome, 23 - 25 September 2009

PERMANENT COURT OF ARBITRATION CASE NO. AA286 - FINAL ARBITRATION AWARD GRANUCO S.A.L. (LEBANON) V. FOOD AND AGRICULTURE ORGANIZATION OF THE UNITED NATIONS

INTRODUCTION

1. On 30 April 2009 an Arbitration Tribunal established within the Permanent Court of Arbitration (PCA) and, in accordance with the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL), delivered an arbitration award in the case of Granuco S.A.L. (Lebanon) v. Food and Agriculture Organization of the United Nations. All claims made by Granuco, in the amount of US$ 4,434,107.88 in respect of a number of Purchase Orders cancelled by the Organization, as well as claims for damages in the amount of US$ 3,000,000.00 suffered as a result of harm done to Granuco's image and reputation and loss of profit were dismissed by the Arbitration Tribunal. The Arbitration Tribunal entertained only a limited claim for damages of €45,054.90, representing 40% of some charges and expenses incurred by Granuco and attributable to the Organization, as a result of late payment of invoices and FAO's acceptance to pay for a partial consignment of goods made by FAO.

2. The matter is being referred to the Committee on Constitutional and Legal Matters (CCLM) under Rule XXXIV, paragraph 3 of the General Rules of the Organization, and in line with past practice of FAO in comparable situations. As an intergovernmental organization of the United Nations System, FAO enjoys immunity from every form of jurisdiction. Under the Conventions on the Privileges and Immunities of the United Nations and the Specialized Agencies, each organization is required to make provision for appropriate modes of settlement of disputes arising out of contracts or other disputes of a private nature to which the organizations are a party. Therefore, commercial contracts to

which FAO is a party contain a clause on settlement of disputes providing for arbitration under the United Nations Commission on International Trade Law (UNCITRAL). At present, commercial contracts include, in addition to an UNCITRAL arbitration clause, a provision on applicable law whereby contracts are subject to general principles of law to the exclusion of any national legal system[1].

GENERAL BACKGROUND

A. The Oil-for-Food Programme

3. The dispute arose in the context of the "*Oil-for-Food Programme*" established by Security Council Resolution 986 acting under Chapter VII of the Charter of the United Nations. The resolution authorized States to import petroleum and petroleum products originating in Iraq in quantities sufficient to produce a sum of US$ 1bn. every 90 days in order to finance the purchase of humanitarian goods as well as various mandated activities concerning Iraq. Payments would be effected through an escrow account established by the Secretary-General. The resolution established a number of conditions for use of the funds. The funds would be used in order to finance the purchase of humanitarian goods (medicine, health supplies, foodstuffs and materials and supplies for essential civilian needs) by the Government of Iraq. Purchases required clearance by a Sanctions Committee established earlier in 1991. A supplementary programme in the three northern Governorates of Dihouk, Arbil and Suliemaniyeh aimed at ensuring more equitable and effective distribution of humanitarian relief. A Memorandum of Understanding setting out the conditions of the intervention by the United Nations was signed between the United Nations and the Government of Iraq on 26 May 1996. The Memorandum of Understanding established special procedures for Northern Iraq whereby materials and supplies would be procured through the United Nations system.

4. In order to implement these arrangements, the United Nations concluded Memoranda of Understanding with various specialized agencies of the United Nations, including with FAO in November 1998. Under the Memorandum of Understanding with FAO, the United Nations Office of the Iraqi Programme was to provide funding to FAO, allowing FAO to carry out a number of operations in Northern Iraq[2].

5. Subsequently, on 22 May 2003, the Security Council adopted resolution 1483 which addressed a range of issues with a view to the termination in the "*most cost effective manner the ongoing operations of the Oil-for-Food Programme*". The resolution requested the Secretary-General to review, in light of the changed circumstances, the relative utility of each approved and funded contract in order to determine whether such

[1] In their latest version, FAO standard arbitration clauses provide that, prior to resorting to arbitration, a dispute must be referred for compulsory conciliation under the UNCITRAL Conciliation Rules. The standard clause on settlement of disputes was endorsed by the CCLM at Seventy-third Session held on 17 and 18 June 2002, see CL 123/5, paragraph 10. See also CL 123REP, paragraph 100.

[2] In some cases, FAO would conduct technical activities. In the case at hand, FAO was to acquire humanitarian supplies and, once clearance was obtained by the Sanctions Committee, FAO had also to obtain the necessary permits from the Iraqi authorities. FAO was responsible for ensuring that customs and registration documents, licences and operating permits were obtained in an orderly and timely manner.

contracts contained items required to meet the needs of the people of Iraq, and to postpone action on those contracts deemed to be of questionable utility until the government of Iraq was in a position to make its own determination as to whether such contracts should be fulfilled. The resolution also requested the Secretary-General to make any necessary settlement payments. The Oil-for-Food Programme was effectively terminated on 21 November 2003 and, of course, all agencies were required to return any unused funds to the United Nations.

B. Purchase Order N° 98363

6. Granuco S.A.L., a company based in Beirut, concluded a contract with FAO on 18 July 2001 for the delivery of animal feed, i.e. 4,000 metric tonnes of broiler concentrate, 560 metric tonnes of breeder concentrate and 1,000 metric tonnes of layer concentrate for poultry feed[3]. Delivery was to be made by 18 October 2001. However, Granuco did not comply with delivery terms despite reiterated requests by FAO to perform. In June 2002 a partial consignment of 322.50 metric tonnes of broiler concentrate, out of 4,000 metric tonnes to be supplied, was delivered. At the end of November 2002 the company announced a second partial consignment of 1,350 metric tonnes of broiler concentrate. Following repeated delays and a number of complaints from the authorities of Northern Iraq regarding their failure to perform, FAO served Granuco notice of termination of the contract on 4 February 2003. Subsequently, FAO refused to effect payment of this second partial consignment because the animal feed did not comply with a number of specifications under the terms of the contract. On the basis of laboratory analyses carried out by the Netherlands Superintending & Sampling Company (NSSC)[4], it appeared that the goods were not in accordance with the specifications which had originally been agreed to by Granuco. For this reason, FAO withheld payment for the consignment in accordance with the Purchase Orders. Eventually, however, FAO accepted to pay for this second partial consignment because, due to internal communication difficulties, the material had, in fact, been distributed within the Northern Governorates.

C. Purchase Orders N°s 86517/90126 and 86638

7. FAO had also purchased animal feed from another company, ARD (Unifert) under other Purchase Orders in September and December 2000 with deliveries to be made in 2001. These contracts were also terminated in February 2003 on the basis of the relevant contractual conditions regarding performance and default and such termination was accepted unreservedly and even in apologetic terms by ARD (Unifert). However,

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[3] It may be useful to clarify a few definitions, most of which are taken from the Manual of Good Practices for the Feed Industry, intended for publication by FAO and IFIF (International Feed Industry Federation): A "*feed concentrate*" is a feed used with another to improve the nutritive balance of the total and intended to be diluted or mixed to produce a supplement or a complete feed. A "*complete feed*" is a nutritionally adequate feed compounded by a specific formula to be fed as the sole ration and capable of maintaining life and/or promoting production without any additional substance except water. Broilers are meat-type chickens. A broiler is a chicken slaughtered for meat. Modern commercial broilers are specially bred for meat production and grow much faster than egg-laying breeds. Both male and female broiler chickens are slaughtered for their meat. Layers are chickens used to produce eggs. Breeders are chickens used to produce off-spring; breeder concentrate is therefore a concentrate used to feed chickens for the production of off-spring.

[4] The tests were re-done several times, including by a laboratory selected by Granuco.

subsequently, well after the termination of these contracts, Granuco, which allegedly had been producing the animal feed for ARD (Unifert), raised claims in connection with the termination of these Purchase Orders. FAO argued consistently that although there might have been a commercial relation between ARD (Unifert), as trader, and one of its suppliers (Granuco), this was wholly irrelevant from FAO's perspective.

8. While in essence the legal issues involved in the case were simple and straightforwad, the case ended up involving some complexity, both legal and practical, for several reasons.

8.1. First, the Purchase Orders were concluded under the Oil-for-Food Programme which was a programme of a complex structure. On 22 May 2003, the Security Council adopted resolution 1483 addressing a range of issues concerning the termination in the "*most cost effective manner the ongoing oprations of the Oil-for-Food Programme*". The resolution also called upon the organizations to take an active approach towards the settlement of any outstanding claims. The Oil-for-Food Programme was effectively terminated on 21 November 2003 and all agencies were required to return any unused funds to the United Nations. In order to cover potential liabilities arising from the claim, FAO had to withhold some funds from the Oil-for-Food Programme[5]. However, FAO was placed under considerable pressure to return these funds to the United Nations. The contractor seemed to have been aware of this situation and may have expected a settlement of the case, which is confirmed by the fact that he instituted arbitration proceedings only several years after the termination of the Purchase Orders.

8.2. Second, Granuco made widespread claims of wrongdoing and corruption by officials of the Organization. These claims were investigated by the FAO Office of the Inspector-General which concluded that they were baseless. The claims were eventually dismissed by the Arbitration Tribunal. Whatever the position on the substance of the allegations, in practice the very existence of such allegations limited or eliminated altogether any possibility on the part of FAO to consider any form of settlement of the case.

8.3 Third, Granuco made a grossly inflated claim in respect both of a contract concluded between FAO and that company and in respect of Purchase Orders concluded between FAO and another company, ARD (Unifert). FAO maintained consistently that these were two separate, distinct sets of contractual relationships and, in particular, that the Purchase Orders with ARD (Unifert) had not been assigned to Granuco as there were specific procedures in the Purchase Orders regarding transfers of contracts which had not been followed. This position was eventually fully accepted by the Arbitration Tribunal. Still, the alleged "fiction" that there was a single claim made the claim a rather complex one, in light of the existing case law of arbitration tribunals on assignment of arbitration clauses to third parties, and so made it more difficult for FAO to settle the case.

[5] This was strictly in accordance with the terms of the Memorandum of Understanding of November 1998 between the United Nations and FAO.

8.4. Fourth, under the relevant Purchase Order, Granuco S.A.L. was required to deliver animal feed which would meet a number of specifications, on the basis of a report by a surveillance company. The report by this company concluded that the animal feed provided did not comply with the specifications set forth in the Purchase Order and was accepted fully and unreservedly by Granuco. Eventually, this resulted in additional analyses of the goods delivered and an extensive debate on technical and scientific issues. Although the level of this claim was a limited one, this particular matter attracted much controversy.

8.5. Fifth, as in any arbitration there was uncertainty as to the outcome of the proceedings. For reasons of this nature, as well as considering the costs which were involved in an earlier arbitration, the CCLM "*emphasized that, given a number of inconveniences inherent in arbitration proceedings, including cost considerations, the Organization should, whenever possible, seek to reach out-of-arbitration settlements of contractual disputes. However, the possibility of resorting to arbitration depends on the particular circumstances of each case. As regards this particular dispute, the Committee agreed that there were issues of principle at stake and concurred with the Director-General's decision to resort to arbitration rather than seeking amicable settlement*"[6]. However, as explained above, the Organization could not settle this case.

8.6. Finally, for a substantial period of time, FAO was confronted with a situation where, on the one hand, it could not settle a long-standing claim for both practical and legal reasons as explained above and, on the other hand, was unable to return to the United Nations all funds which it held. FAO was placed under considerable pressure to release the funds which it had to hold in order to cover possible liabilities and the uncertainty of the situation was a cause of embarrassment in the relations between FAO and the United Nations.

9. It is important to keep these general considerations in mind when considering the case and the arbitration award as summarized below. Eventually, the above background as well as all legal and factual issues involved in the process made it necessary, at least for FAO, to make extensive submissions to the Arbitration Tribunal.

CONSTITUTION OF THE ARBITRATION TRIBUNAL

10. On 10 May 2004, Granuco S.A.L., a corporation registered and organised under the laws of Lebanon, sent a notice of arbitration against FAO, in accordance with the General Terms and Conditions applicable to FAO Procurement Contracts, providing for the application of the UNCITRAL Arbitration Rules. However, Granuco did not pursue the claim for several years.

11. In 2007, Granuco resumed proceedings. On 16 August 2007, Granuco appointed the first arbitrator to the arbitral tribunal, whereas FAO appointed the second arbitrator on 14 September 2007. The UNCITRAL Arbitration Rules foresee a situation where the arbitrators are unable to agree on a third presiding arbitrator. In that case, the Secretary-

[6] CL 123/5, Report of the Seventy-third Session of the CCLM, 17-18 June 2002, paragraph 10.

General of the PCA designs an appointing authority (who, in turn, appoints the presiding arbitrator), or, if the parties so agree, designs directly the presiding arbitrator. By letters dated 3 and 24 January 2008, both Parties agreed that the Secretary-General of the PCA should appoint the presiding arbitrator.

12. The First Procedural Meeting was held on 17 April 2008, wherein the parties agreed on Brussels being the place of arbitration; English to be the language of the arbitration procedure; and, that the PCA was to act as the Registry. By letter of 5 May 2008, FAO reserved its right to raise jurisdictional objections with regard to the Tribunal's examination of the claims arising from purchase orders to which Granuco was not a party.

13. At the Procedural Meeting of 17 April 2008 the Tribunal agreed to apply to the Purchase Orders and to the dispute "*general principles of law to the exclusion of any national legal system*". This contractual clause was accepted by both parties and reflects the universal and intergovernmental nature of FAO as well as its immunity from any form of national jurisdiction. In its submissions, FAO referred to relevant articles of the UNIDROIT Principles of International Commercial Contracts of 2004 and of the United Nations Conventions on Contracts for the International Sale of Goods of 1980 which are often applied in situations where contracts are governed by general principles of law, as was the case with the Purchase Orders. This was accepted by the parties and indeed followed by the Arbitration Tribunal since, in connection with a claim made by Granuco at the hearing of 1 December 2008 that its failure to deliver might have been due to a force majeure, the Arbitration Tribunal, on its own initiative, examined that claim against the UNIDROIT Principles of International Commercial Contracts of 2004 or of the United Nations Conventions on Contracts for the International Sale of Goods of 1980, exactly in the same manner as the Organization had done in its submissions, when it examined each specific claim by reference to these instruments.

14. On 30 May 2008, Granuco submitted its Statement of Claim. On 11 July 2008 FAO submitted its Statement of Defence, expanding its objections regarding the jurisdiction of the Arbitration Tribunal in respect of the Purchase Orders to which Granuco was not a party, as well as requesting that its objection be ruled on as a preliminary issue. Granuco objected to FAO's request on 7 August 2008. The Tribunal however confirmed that it would rule on its jurisdiction in the final award. On 7 October 2008, Granuco submitted its Statement of Reply, and FAO's Statement of Rejoinder was later submitted on 14 November 2008. The hearing was held on 1 December 2008 in a single procedure.

RELEVANT FACTS

A. Purchase Order N° 98363

15. On 17 October 2000, FAO issued an invitation to tender for the supply of poultry concentrate to Northern Iraq. A bid was submitted on 25 October 2000 by Granuco which expressed its acceptance of the conditions of the tender in full. Purchase Order N° 98363 for the delivery of this poultry feed was issued on 18 July 2001.

16. Meanwhile, the Council of the European Union issued, on 4 December 2000, a decision ("EU Decision") which came into force on 1 January 2001 which prohibited the

export of processed animal proteins from European Union Member States to third countries. The EU Decision was anticipated to expire on 30 June 2001, however was later extended.

17. Purchase Order N° 98363 stipulated the contractual specifications of the goods to be delivered, notably the requirement that they be "*free from indigestible animal scraps, hair, horn, nail, blood-meal and any expired ingredients*", and that the delivery of the goods be made within three months from the receipt of the Purchase Order, i.e. on 18 October 2001. Moreover, Purchase Order N° 98363 required that the goods be inspected at loading point by the Netherlands Superintending & Sampling Company (NSSC) and specified that no payments would be made unless NSSC rendered a satisfactory inspection report. On 9 August 2001, Granuco acknowledged receipt of Purchase Order N° 98363, and confirmed that the delivery would be made by the end of December 2001 (which was already a change in respect of an earlier acceptance of the delivery date of October 2001).

18. Between 18 July 2001 and 18 December 2001, NSSC attempted, on numerous occasions, to organize an inspection of the goods. However Granuco appeared to be unreachable. On 18 December 2001, FAO asked Granuco to provide it with its shipping information and pointed out that the delivery of the goods had been "*long overdue*". The following day, Granuco responded that the shipping information would be sent within two weeks; FAO did not receive the shipping information as promised. An additional request was sent to Grancuco on 11 March 2002, to which it responded that the shipping details were soon to be sent and that the delivery would be made before the end of May 2002.

19. On 22 May 2002, Granuco assured FAO that a partial shipment of approximately 8% of the total order was intended to arrive in June 2002 ("June Shipment"). On 30 May 2002, FAO asked Granuco to specify when exactly it expected to deliver the remainder of the shipment. At the end of June, Granuco replied that it needed another extension for the delivery, and informed FAO that the remainder of the shipment was to be delivered in October 2002. On 24 July 2002, NSSC released an inspection report on the June Shipment, finding that it had not conformed to the required contractual specifications, given that the animal protein was composed of 100% fishmeal, rather than the stipulated 50% fishmeal and 50% poultry waste.

20. On 25 September 2002, FAO sent a fax to Granuco regarding Purchase Order N° 98363, reminding it to "*kindly let* [FAO] *have at* [Granuco's] *earliest convenience the total volume and weight of this consignment*", and that "*if* [Granuco] *had already received* [FAO's] *notice that an import permit ha*[d] *been granted* [to] *please proceed with the shipment*", but "*not* [to] *ship the goods of the above-mentioned Purchase Order unless* [Granuco] *ha*[d] *received notice from this office that the Iraqi import permit ha*[d] *been granted*." Granuco replied on 14 October 2002 that a partial shipment of the goods was to be delivered on 25 October 2002, and that another shipment would be made by the end of November 2002. However, by 8 November 2002 FAO had still not received the shipment and inquired on its status, to which Granuco responded that the dates of delivery needed to be changed to 15 November and 11 December 2002. On 18 November 2002, following another request for shipping information by FAO, Granuco informed FAO that the partial shipment ("November Shipment") had been loaded and was being sent to Northern Iraq.

21. On 4 February 2003, following strong protests from the Northern Governorates of Iraq over the non-compliance of the November Shipment with the required contractual specifications, in addition to the large number of notices, enquiries and reminders to Granuco to perform its contractual obligations, FAO informed Granuco that it was cancelling the outstanding order "*due to the long overdue delivery*". After an unsuccessful request on the part of Granuco for FAO to reconsider its decision, Granuco acknowledged receipt of the notification of the cancellation of Purchase Order N° 98363 on 26 February 2003.

22. Shortly after the cancellation, FAO informed Granuco, on 14 March 2003, that two analyses conducted by NSSC found that the November shipment did not conform with the required contractual specifications since the broiler concentrate was not free from bacterial and fungal contamination or indigestible animal scraps, and added that if a third analysis carried out by a different laboratory found the same result, FAO would not pay for invoices 001/03 and 002/03. Eventually, the third analysis confirmed the same result. Upon request by Granuco, a fourth analysis was conducted at a laboratory of its choice, which found the sample to contain hair and blood-meal. In spite of the results, Granuco contested the analysis on 5 and 9 May 2003. A senior officer of the competent technical division at FAO also agreed that the November Shipment was not in conformity with the required contractual specifications. In reply, Granuco submitted attestations by experts in support of its position, but FAO's senior officials confirmed the previous results.

23. By 12 May 2003, FAO sent to Granuco notification rejecting the November Shipment and indicated its refusal to pay for the two invoices. However, due to a miscommunication resulting in a portion of the November Shipment being distributed on 9 June 2003, FAO accepted to pay both invoices, but specified that its payment "*should not be construed as renouncement of* [FAO's] *technical position with regards to the consignment*".

B. Purchase Orders N^os 86517/90126 and 86638

24. FAO had also issued invitations to tender for the supply of poultry concentrates to be delivered to Northern Iraq in June 2000, and accepted the bids made by ARD (Unifert) s.a.l. ("ARD"). Accordingly, Purchase Order N° 86517 was issued on 28 September 2000 followed by Purchase Order N° 86638 on 2 October 2000. Given that FAO had requested two additives to be added to Purchase Order N° 86517, Purchase Order N° 90126 was subsequently issued on 2 December 2000, causing both Purchase Orders to be jointly referred to as "Purchase Order N^os 86517/90126".

25. At the start, Purchase Order N^os 86517/90126 were to be delivered by ARD (Unifert) on 28 February 2001, while Purchase Order N° 86638 was to be delivered on 5 March 2001 also by ARD (Unifert). However, on 23 February 2001 ARD informed the Respondent that all Purchase Orders were expected to be shipped within 90 days, and that the shipment information would be submitted by the end of May or at the beginning of June 2001. Inquiries concerning the delivery of the goods were made on 21 June and 10 July 2001 by the Respondent, to which ARD replied that the goods could not be delivered before the first quarter of 2002. ARD later informed FAO that the goods were to be delivered before the end of January 2002. Despite numerous communications asking ARD to supply the shipping information, FAO was informed in June 2002 that partial

shipments of Purchase Order N^{os} 86517/90126 along with the entire shipment of Purchase Order N^{o} 86638, would be delivered later on in September 2002.

26. On 25 September 2002, FAO sent a fax reminding ARD (Unifert) to "*kindly let* [FAO] *have at* [ARD's] *earliest convenience the total volume and weight of this consignmen*t", and that "*if* [ARD] *had already received* [FAO's] *notice that an import permit ha*[d] *been granted* [to] *please proceed with the shipmen*t", however "*not* [to] *ship the goods of the above-mentioned Purchase Order unless* [ARD] *ha*[d] *received notice from this office that the Iraqi import permit ha*[d] *been granted*."

27. On 13 January 2003, FAO asked ARD (Unifert) to proceed with the shipment of Purchase Order N^{os} 86517/90126, given that the required import permit had been granted. However, ARD communicated with FAO on 30 January 2003, enumerating various impediments which were preventing the delivery of the shipment at that time.

28. Given the "*long overdue delivery*" of Purchase Orders N^{os} 86517/90126 and 86638, FAO informed ARD on 5 February 2003 of their cancellations, to which ARD acknowledged receipt of the decision on 12 February 2003. In fact, ARD (Unifert) accepted unreservedly and in apologetic terms the decision of cancellation of the Purchase Orders.

MAIN ARGUMENTS BY THE PARTIES

A. On the tribunal's jurisdiction regarding Purchase Orders N^{os} 86517/90126 and 86638

29. Granuco argued that FAO had wrongfully cancelled Purchase Orders N^{os} 86517/90126 and 86638, given that "*on February 19, 2001 ARD and the Claimant signed a contract confirming all FAO/ARD Purchase Orders, so that* [the Claimant] *became the beneficiary and the responsible of said purchase orders*". According to the Claimant, it had become the "assignee" of ARD's rights and obligations under Purchase Orders N^{os} 86517/90126 and 86638. Thus, Granuco argued that the arbitration clauses referred to in the Purchase Orders applied and gave jurisdiction to the Tribunal, and argued that it had "*made partial deliveries, received payment for such deliveries, financed quantities of concentrate, and made interest payments*".

30. Granuco argued further that FAO had been aware of the purported assignment since 19 May 2003, and had not objected to it. Granuco referred to several documents, particularly a correspondence dated 21 March 2006 by the Inspector-General of FAO which mentioned that Granuco should "*approach the Government of Iraq as the lawful successor of the 'Oil for Food' Programme and its related funds*". Therefore, Granuco sustained that the Inspector-General was aware of the purported assignments of the Purchase Orders from ARD to Granuco, and that because no objection was raised in the correspondence, FAO recognized and accepted the purported assignments.

31. In addition, Granuco alleged that FAO's lack of objection over a period of five years demonstrated its acceptance of the purported assignments, and that according to the principles of estoppel and good faith, FAO could not raise objections with regard to the jurisdiction. Moreover, Granuco argued that FAO had "*explicitly recognised the*

jurisdiction of the Tribunal" at the First Procedural Meeting and was no longer permitted to dispute its jurisdiction.

32. On the other hand, FAO submitted extensive observations that the Tribunal did not have jurisdiction because Granuco was never a party to Purchase Orders N^{os} 86517/90126 and 86638. Concerning the Granuco/ARD Agreement, brought to the knowledge of FAO only after the termination of the Purchase Orders, FAO regarded it as "*a commercial dealing between a trader and one of its suppliers*", adding that it "*did not involve any assignment whatsoever of the contracts to* [Granuco]". FAO argued that it had never been informed of the relationship between ARD and Granuco; it had never given its consent to such a purported assignment nor discharged ARD (Unifert) from its obligations under Purchase Orders N^{os} 86517/90126 and 86638. In addition, FAO submitted that, according to the General Terms and Conditions, the UNIDROIT Principles of International Commercial contracts, as well as the United Nations Convention on Contracts for the International Sale of Goods, ARD was not permitted to transfer its obligations to Granuco without FAO's prior knowledge and consent. While noting that there were instances where arbitration tribunals recognized jurisdiction in respect to parties that were not signatories to arbitration agreements, FAO submitted that this would not be legally justified under the circumstances. Granuco had not played any role in respect of the Purchase Orders N^{os} 86517/90126 and 86638 especially when considering closely critical moments in the life of these Purchase Orders [i.e. (i) their negotiation and conclusion; (ii) their execution or non-execution and (iii) their termination].

33. FAO denied having ever accepted, explicitly or implicitly, the purported assignment of the Purchase Orders to Granuco, and further denied that it was "*estopped from raising jurisdictional objections (...) because it never took positive steps to imply its recognition*". FAO claimed to have viewed its relationship with Granuco as entirely separate from its relationship with ARD, and stressed the fact that it had always used separate channels of communication. In addition, FAO clarified that the issue of jurisdiction raised at the First Procedural Meeting had been referred to in a generic way.

B. <u>On the termination of Purchase Order N^{o} 98363</u>

(a) <u>Delays in delivery</u>

34. Granuco insisted that the cancellation of the Purchase Orders by FAO was "*groundless and irrelevant*", arguing that the delay in delivery had resulted from FAO's own actions "*in that it* [had] *requested the delay in delivery;* [had] *provided contradictory instructions for delivery; and* [had] *otherwise accepted or acquiesced in any delay in delivery*". According to Granuco, FAO's letter of 25 September 2002 addressed to Granuco referring to the need to wait for the availability of import permits was, in fact, a request to delay the delivery of the goods, on which Granuco relied upon.

35. FAO argued that the cancellation of the Purchase Order was justified by the fact that Granuco was accountable for its "*non-performance, late performance, and defective performance*", and stressed the fact that Granuco had fully accepted the General Terms and Conditions when replying to invitations to bid, and had agreed to all conditions of the Purchase Order. FAO had received from Granuco so many "*misrepresentations and ambiguous declarations*" with regard to the delivery dates, that it could no longer "*reasonably rely on future performance*". FAO stressed that it had acted diligently by

sending notices and reminders to perform. Regarding the letter of 25 September 2002, FAO stated that "*a communication stressing that it was important to ensure that the import permits were available (...) could not be seen, in any possible manner, as acquiescence in delays, or as a request not to produce or not to deliver.*"

(b) Force Majeure

36. Granuco invoked *force majeure* for the first time at the hearing of December 2008. Granuco claimed that the EU Decision forced it to move its factory from Spain to Brazil, creating significant administrative hurdles in order to get the business organized. Granuco insisted that due to this event, it had been released from its obligations, and referred to the General Terms and Conditions in support of its argument.

37. FAO argued that the conditions of *force majeure* were not met. The EU Decision had made it difficult, but not absolutely impossible to deliver the goods, a necessary element for such a defence. FAO also pointed out that the EU Decision occurred in December 2000 and Granuco had been capable of delivering goods after that date. Lastly, FAO underlined that Granuco had needed to demonstrate *force majeure* throughout a period of two years from the date of the event.

(c) Allegations of corruption

(i) Allegations of extortion by FAO's officials

38. Granuco made extensive submissions that the "*real reason behind*" FAO's cancellation of the Purchase Orders was that FAO officials wanted to extort money from Granuco's Manager, and Granuco's Manager had "*refused to accede to illegitimate requests for payments*". According to Granuco, FAO officials retaliated by cancelling the Purchase Orders and by deciding that the November Shipment was not in conformity to the required contractual specifications. In support, Granuco mentioned that FAO "*ha*[d] *been subject to investigation for fraud corruption and mismanagement in the operations connected with the United Nations Oil-for-Food Programme*". Granuco insisted that FAO had been investigated for fraud and corruption by the Independent Inquiry Commission (IIC). As such, it stated that the cancellations were null and void, and that it was entitled to indemnification for the damages it had suffered as a consequence.

39. FAO denied the allegations, and pointed to the fact that Granuco submitted such allegations at a very late stage of the proceedings, which was not in conformity with the basic requirement of good faith, and that by its actions had "*intended to cause embarrassment*" to FAO. Therefore, it requested for the Tribunal to declare that the allegations were inadmissible.

40. Regarding the allegation of extortion by FAO officials, FAO argued that extensive investigations had been carried out by the FAO Office of the Inspector-General, which had concluded that the allegations were baseless, given that five individual inspection reports had found the November Shipment not to conform with the required contractual specifications, and that the cancellation of the Purchase Orders was a corporate decision which needed to be made by an official at a higher level of administration and in liaison with the authorities of the country. FAO explained that the IIC was set up in April 2004 with the purpose of "*carry*[ing] *out investigations into all United Nations officials and*

personnel, the Coalition Provisional Authority of Iraq and all other Member States, including their national regulatory authorities", adding that no evidence of any fraudulent behaviour on the part of FAO or its officials had been found.

(ii) Alleged misrepresentation of FAO's responsibility with respect to Granuco's claims

41. Granuco referred to a letter of 24 February 2006 addressed to the Inspector-General, requesting payment for the supposed abusive cancellation of the Purchase Orders, and requested the Inspector-General to "*study* [Granuco's] *complaint and to answer* [its] *queries*". However, Granuco indicated that the Inspector-General had responded that due to the termination of the Oil-for-Food Programme *"the responsibility for any remaining activity* [was to] *be transferred to the Government of Iraq*". Thus, Granuco alleged that the Inspector General's response was written "*in order to mislead* [Granuco] *by exonerating* [FAO] *illegally from any responsibility, to direct* [Granuco] *mischievously to seek remedy from the Government of Iraq as the lawful successor of the Oil-For-Food Programme and its related funds."* Granuco also alleged that the information provided was false given that the funds had never been transferred to the United Nations, and that FAO had remained the "*sole and unique legal entity responsible to repair damages"*.

42. FAO clarified that during that period of time it had the obligation of returning all residual funds to the Government of Iraq through the United Nations, and that all responsibilities for matters related to the Oil-for-Food Programme were to be shifted to the Government of Iraq. FAO explained that negotiations had been underway with the United Nations regarding the possibility for the United Nations to provide to FAO the benefit of a "*hold-harmless clause*" which would have "*indemnif*[ied] [FAO] *from any action which could be brought against it*". FAO stated that in the end the United Nations had not accepted such a clause, but it had been in that context that the Inspector-General had responded to the Claimant's letter and it was similarly in that context that a letter of the Inspector-General to Granuco had to be considered.

C. <u>On the delay in the payment of invoices 001/03 and 002/03 under Purchase Order N° 98363</u>

43. Granuco argued that the late payment of invoices 001/03 and 002/03 under Purchase Order N° 98363 for the November Shipment had been wrongful, rejecting FAO's argument that it had refused to pay because the shipment did not comply with certain contractual specifications and, instead, pointed to the corruption on the part of FAO officials.

44. Moreover, Granuco rejected the analyses of the November Shipment, arguing that the surveillance company, NSSC, was incompetent and that it allowed FAO to manipulate the test results in order to pressure Granuco into paying "*kickbacks*" to FAO officials; that the results were scientifically impossible and incomplete; and, that some of the results could only have been carried out through microbiological testing rather than microscopic testing. Granuco also mentioned that the November Shipment had been produced in the same plant and consisted of the same raw materials as the goods supplied by ARD (Unifert), however that FAO had precisely refused to pay Granuco.

45. In reply, FAO reiterated that the delay in the payment of the invoices for the November Shipment was due to goods not meeting the required contractual specifications set out under Purchase Order N° 98363, which had been accepted in its entirety by Granuco when agreeing to the Purchase Order.

46. As to the inspection carried out by NSSC, FAO explained that the first test results indicated that the goods did not conform to the required contractual specifications, and that other samples of the goods had been inspected on four different occasions, all of which resulted in similar findings. FAO indicated that it had initially refused to pay for the November shipment; however, given the miscommunication which led to the delivery of a portion of the goods, it had decided to pay for it, with reservation as to its technical position. FAO also stressed that the payments had been delayed as a result of the five tests requested by both Granuco and FAO, and that the General Terms and Conditions did not stipulate the duration of such testing. FAO replied with regard to Granuco's assertion that NSSC was "*not up to required standards*" and that its findings were baseless and unfair. FAO argued that NSSC was a reputable company, an "*old company established in Rotterdam in 1918 with activities worldwide"* which had "*performed its services in a diligent manner"*. The findings of NSSC were confirmed by several other external laboratories.

RELIEF SOUGHT FROM THE TRIBUNAL

47. Granuco asked the Tribunal to refute FAO's plea on the lack of jurisdiction in relation to Purchase Orders N^{os} 86571/90126 and 86638, and to assert its jurisdiction in respect of these Purchase Orders. Moreover, Granuco asked the Tribunal to order FAO to pay to it the amount of US$ 4, 434,107.88 with accrued interests as of 1 January 2003 for the cancellation of Purchase Orders N^{os} 98363, 86517/90126 and 86638 and compensation for the charges and expenses due to the cancellation, plus the amount of €112,637.26, and the amount of US$ 3,000,000 for wreck of image and reputation as well as loss of profit, with their accrued interests until full and final payment. Granuco also asked that the Tribunal rule that all fees, costs and expense be borne exclusively by FAO.

48. FAO asked the Tribunal to declare that it did not have jurisdiction with regard to Purchase Orders N^{os} 86517/90126 and 86638 and to declare them unfounded on the substance. FAO aksed the Tribunal to conclude that all the claims raised in connection with Purchase Order N° 98363 were unfounded on the merits given Granuco's failure to perform the Purchase Order, and that any delayed payment of the goods had been entirely attributable to the goods not being in conformity with the required contractual specifications.

RULINGS OF THE TRIBUNAL ON THE CLAIMS

A. <u>On the Tribunal's jurisdiction regarding Purchase Orders N^{os} 86517/90126 and 86638</u>

49. Under the General Terms and Conditions ARD (Unifert) could not assign or make any other disposition of the Contract, without the prior written consent of FAO, any unauthorised assignment would be void, and would entitle FAO to cancel the Contract without liability. Purchase Orders N^{os} 86517/90126 and 86638 had been concluded on 28 September and 2 October 2000, and then cancelled on 5 February 2003. ARD (Unifert)

immediately accepted the cancellation. In addition, Granuco waited until 19 May 2003, more than three months after the cancellation, to inform FAO of the purported assignment of the Purchase Orders. The Tribunal pointed out that Granuco had not provided any evidence showing that FAO was informed of such an event prior to 19 May 2003.

50. The Tribunal also found that Granuco had failed to demonstrate that FAO had, in fact, provided its *prior written consent* to the purported assignment, an essential component to a valid assignment. The Tribunal considered that the Inspector General's letter constituted an administrative response which did "*not validate what* [was] *otherwise an invalid assignment under Purchase Orders 86517/90126 and 86638*."

51. The Tribunal rejected Granuco's argument that, at the First Procedural Meeting, FAO had accepted the jurisdiction of the Tribunal over all the claims. The Tribunal noted that FAO's jurisdictional objections were raised in a timely manner in its letter of 5 May 2008, and that the Statement of Defence, raising an objection to the jurisdiction of the Tribunal in respect of a number of claims, was in accordance with the UNCITRAL rules. Furthermore, the Tribunal was not persuaded by Granuco's argument that the arrangement between Granuco and ARD (Unifert) was in any manner a valid *assignment.* It appeared to be a letter from ARD (Unifert) to Granuco, setting out delivery instructions for a consignment, which Granuco would make entirely on behalf of ARD (Unifert). This purely internal arrangement clearly showed that Granuco S.A.L. "*did not replace ARD as* [FAO's] *partner under the Contract*." **Therefore, the Tribunal agreed with FAO's characterization that the agreement between ARD and Granuco was simply "*a commercial dealing between a trader and one of its suppliers*", and that no valid *assignment* had taken place between ARD (Unifert) and Granuco under Purchase Orders N^{os} 86517/90126 and 86638. The Tribunal concluded that it had no jurisdiction in respect of claims related to these Purchase Orders.**

B. Termination of Purchase Order N^{o} 98363

(a) Delay in delivery

52. The Tribunal was satisfied that although FAO had accepted initial delays in delivery, it had not accepted subsequent delays given its numerous notices and reminders to perform. Communications between 2 August 2002 and 7 July 2003, demonstrated that FAO "*considered* [Granuco] *to be overdue in its obligation to deliver and that* [it had] *expected* [Granuco] *to make the delivery as soon as possible*". **The Tribunal found that that Granuco had been "*in a constant state of default from the date it received written notice by* [FAO] *on 11 March 2002*."

53. Moreover, the Tribunal did not accept the arguments made by Granuco that the "*validity period of the extended approvals of the Sanctions Committee constituted a new date for the delivery of the goods under the Purchase Order*" nor did it accept that it would be somewhat "*reasonable for* [Granuco] *to believe that it had until the expiry of the Sanctions Committee approvals to complete Purchase Order 98363"* given that FAO had to seek the extensions of the Sanctions Committee's approvals simply because Granuco had not delivered the goods.

54. The Tribunal observed that the issuance of an import permit was necessary for goods to be imported into Iraq, however, added that they "*had no bearing on the*

contractual terms of the Purchase Orders, including the delivered date", details of which Granuco had been fully aware. The Tribunal did not accept that FAO's letter of 25 September 2002 "*vindicated* [Granuco's] *chronic failure to deliver in the months prior thereto*", given that the letter was a notification to Granuco to deliver as well as not to deliver, unless it had an import permit. The Tribunal indicated that Granuco had received an import permit on 14 October 2002 and that its "*obligation to make full delivery of Purchase Order 98363 was revived at that time*."

(b) Force majeure

55. The Tribunal recognized that the EU Decision of 4 December 2000 was an "*unforeseen cause beyond the control of and without the fault or negligence of*" Granuco. The Tribunal also noted that Granuco submitted its bid on 25 October 2000; the EU Decision was only later issued on 4 December 2000. Purchase Order N° 98363 was dated 25 May 2001 and it was not until 28 June 2002 that Granuco advised FAO of its difficulties, without ever expressly invoking *force majeure*. The Tribunal considered that the "*delay in notifying* [FAO] *of the effect of the EU Decision on* [Granuco's] *ability to perform the Contract was not reasonable, especially in light of the fact that delivery was originally supposed to have been made within a three-month period*."

56. The Tribunal rejected Granuco's argument that it was unable to perform its obligations under Purchase Order N° 98363 as a consequence of the EU Decision, given its letter of 28 June 2002 which informed FAO of its success in establishing a new plant, regardless of the EU Decision and administrative difficulties. Additionally, the Tribunal noted that the contractual provisions allowed for termination of the contract in the event of *force majeure,* and that, in such a case FAO "(*should) pay to the Contractor* [...] *a sum* [...] *for those reasonable costs incurred by the Contractor prior to the date of termination for completed work*". However, the Tribunal concluded in clear terms that force majeure, including its elements of unpredicatility and inherent impossibility to perform, were not established.

(c) On the allegations of corruption

(i) Allegations of extortion by FAO's officials

57. The Tribunal found that Granuco did not provide evidence of any corrupt practice on the part of any of the officials of FAO. The Tribunal noted that the IIC's Report on the Manipulation of the Oil-For-Food Programme of 27 October 2005 as well as its Report on the Management of the Oil-For-Food Programme of 7 September 2005 did not provide evidence of instances of fraud or corruption on the part of FAO and did not support Granuco's allegations. The Tribunal indicated that Granuco did not submit any conclusive evidence that Purchase Order N° 98363 had been cancelled, or that invoices 01/003 and 02/003 had not been paid, due to corrupt practices.

58. On the contrary, the Tribunal found that FAO's argument that the cancellations were due to fundamental non-performance and delays in delivery, as well as that the invoices had not been paid due to the lack of conformity with the required contractual specifications, had been fully documented.

(ii) ***Alleged misrepresentation of FAO's responsibility with respect to Granuco's claims***

59. The Tribunal did not find that Granuco had submitted evidence proving that the Inspector-General's letter had been sent to it "*in bad faith, with the intention to mislead*". The Tribunal accepted FAO's explanation that the letter had been "*sent during a period of transition, during which certain outcome was anticipated, although it never eventuated*", and observed that FAO had participated fully in the proceedings, which "*would belie* [Granuco's] *implicit allegations that* [FAO] *was attempting to shirk responsibility for the claims raised by* [Granuco] *in connection with the Oil-for-Food Programme*."

(d) On the delay in the payment of invoices 001/03 and 002/03 under Purchase Order N° 98363

60. The Tribunal observed that Granuco accepted the contract without reservation during the tender process, particularly that NSSC would be the company in charge of carrying out the inspections of the goods, and that payment would depend on the receipt of a satisfactory inspection report from the superintending agency. The Tribunal noted that Granuco had failed again to provide satisfactory evidence of its allegations that FAO's refusal to pay the invoices, and the unfavourable test results were due to corruption. In fact, the Tribunal noted that the shipment was not in accordance with the required specifications of FAO, that the delay in payment was due to the process of verification by several laboratories of the poultry feed and that FAO was entitled to refuse payment.

61. However, the Tribunal noted FAO's decision to waive its objections to the November Shipment, notwithsanding its rights as a result of the unfavourable test results. FAO decided to pay the invoices which caused Granuco to incur charges and expenses (including storage) which it was not for it to bear. As a result the Tribunal determined that Granuco *"should be compensated for this loss to the extent that it is justified*." Therefore, the Tribunal ordered FAO to pay Granuco damages of €45,054.90, representing 40% of the charges and expenses incurred by Granuco as a result of the late payment of invoices 01/003 and 02/003, along with simple interest at the rate of 8% per annum on this amount as of 11 August 2003 until the date of full payment.

62. In conclusion,the Arbitration Tribunal ruled as follows:

62.1. The Granuco/ARD Agreement was not a valid assignment under the Contract, and consequently, the Tribunal did not have jurisdiction to determine the claims raised by Granuco under Purchase Orders N^{os} 86517/90126 and 86638 in these proceedings;

62.2. Granuco failed to perform Purchase Order N^{o} 98363, which entitled FAO to cancel Purchase Order N^{o} 98363;

62.3. Granuco's claims for damages due to the cancellation of the Purchase Orders in the amount of US$ 4,434,107.88, and its claims for damages suffered as a result of

harm done to Granuco's image and reputation, as well as loss of profit in the amount of US$ 3,000,000.00, were denied;

62.4 FAO was ordered to pay Granuco damages of €45,054.90, representing 40% of the charges and expenses incurred by Granuco as a result of the late payment of invoices 01/003 and 02/003, along with simple interest at the rate of 8% per annum on this amount as of 11 August 2003 until the date of full payment;

62.5. Granuco's claim for an award of its legal fees, expenses, and other costs of arbitration, was denied; and

62.5 The costs of arbitration of the proceedings were fixed at €135,000.00 (shared equally between both parties).

SUGGESTED ACTION BY THE COMMITTEE

63. The CCLM is invited to review the present document, as well as the arbitration award of 30 April 2009, and make such comments thereon as appropriate.