ATTORNEYS' FEES AS PART OF RECOVERABLE DAMAGES

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In a decision by the U.S. District Court for the Northern District of Illinois in *Zapata Hermanos Sucessores S.A.* v. *Hearthside Baking Co., Inc.*[1] the court discusses, among other things, whether the winning party may have those attorneys' fees, which were necessarily incurred in seeking relief from the court, reimbursed as part of the damages. The question is answered in the affirmative. The decision deserves the greatest attention.

The plaintiff produced cookie tins that it sold to the defendant for a period of approximately six years. The tins had a special motif, specified by the buyer, printed on them and were used by the buyer as packaging for its products. The defendant paid sluggishly and finally refused payment based on untenable factual and legal assertions.[2] The court upheld the jury's verdict,[3] which essentially ordered the defendant buyer to pay the

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[1] Due to complicated procedural rules, which cannot be dealt with in detail here, different decisions were rendered in the same case. The material legal question, which is to be discussed here, was according to the mutual consent of the parties, decided not by the jury but by the judge. The decisions can be found at http://cisgw3.law.pace.edu/cases/010829ul.html; 155 F. Supp.2d 969 (N.D. Ill. 2001); 2001 WL 1000927 (N.D. Ill. 2001); 2001 WL 936112 (N.D. Ill. 2001); 2001, WL 830973 (N.D. Ill. 2001); 2000 WL 1809988 (N.D. Ill. 2000). The author of this case comment also had access to parts of the parties' briefs.

[2] The defense of the defendant-buyer was based, *inter alia*, on late or defective (partial) delivery; the reasoning of the court concerning this matter may be ignored here.

[3] In one of its decisions in which the defendant's attack on the jury's verdict was dismissed, the court defined this attack as being "of the type that attempts to fling gobs of mud towards a wall or a ceiling, hoping that as much as possible will stick," and in a further ruling concerning the question of interest here, the court called the evasive and misleading argumentation of the defendant "better suited to a shell game along the midway of a state fair than to a legal memorandum."

purchase price, and granted damages based on CISG Articles 74 and 78, not only in the form of interest but also as a general reimbursement for attorneys' fees both against the defendant itself and its attorneys. The claim against the attorneys was based on a special rule in the American procedural law for federal courts.[4] Of interest here is the losing party's duty to bear the costs and its support by CISG Article 74,[5] i.e., the decision to generally qualify the winning party's attorneys' fees as part of the consequential damages awarded according to CISG Article 74. This passing of costs to the losing party as damages awarded to the winning party is a transgression on the so-called "American Rule." According to this rule, each party generally bears its own costs, subject to exceptions such as in cases of unwarranted claims or defenses brought in bad faith.

In this respect, the judgment is of great importance to parties who sue or are sued in the United States under contracts subject to the CISG. Although there has not yet been a final decision on the precise amount of recoverable damages,[6] the decision gives cause for deliberations on this matter.

1. Rules concerning the reimbursement of costs for the winning party vary worldwide.[7] In most cases, a decision on the costs of the proceedings is made as part of the judgment itself as, for example, in Germany according to section 91 of the German Code of Civil Procedure (ZPO). In this context, ZPO section 91 is *lex specialis* to claims for damages for late performance in the form of costs of litigation.[8] Thus, such costs can only be

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[4] *See* 28 U.S.C. § 1927 (Defendant's attorney is liable if he "multiplies the proceedings . . . unreasonably and vexatiously."); *see also* 155 F. Supp.2d 969 (N.D. Ill. 2001); 2001 WL 1000927 (N.D. Ill. 2001). The said rule on the passing of costs is only applicable in cases decided in federal courts; the diversity of state procedural rules concerning this matter cannot be described here.

[5] In addition, the judgment was based on the "extreme bad faith" refusal to pay; here as well, the legal basis was 28 U.S.C. § 1927 and the possibility through this provision to impose the costs onto the other party if he or she "has acted in bad faith, vexatiously, wantonly, or for oppressive reasons." *See Zapata*, 155 F. Supp.2d 969 (quoting F.D. Rich Co. v. United States f/u/o Industrial Lumber Co., 417 U.S. 116, 129 (1974)).

[6] At the time this article was written only the next hearing on the extent of the loss had been concluded.

[7] *See* Gotanda, *Awarding Costs and Attorneys' Fees in International Commercial Arbitration*, 21 MICH. J. INT'L L. 1 (1999).

[8] *See* STAUDINGER/LÖWISCH § 286 No. 53. (13th ed. 1995).

claimed as damages for late performance insofar as they are not subject to ZPO section 91. These are particularly the costs for the pursuit of one's rights outside the courts. However, ZPO section 91 contains a general principle: The restriction of the reimbursement to costs necessary for the pursuit or defense of one's rights in ZPO section 91(1) is an expression of the obligee's duty to mitigate the loss, which does not allow for avoidable costs to be passed on to the other party.[9] The same is true for cases in which the CISG is to be applied. This is why in addition to the fees of its German lawyer, attorneys' fees in the plaintiff's home country must be reimbursed, if and insofar as they were necessary.[10] If a fee was agreed upon with a foreign attorney, e.g., a contingent fee, it will be necessary to thoroughly investigate, and as a plaintiff to prove, whether and why the agreed upon fee was necessary for the pursuit of the claim.[11] If it was not necessary, it cannot be claimed as part of the damages for late performance.

2. If the proceedings are governed by an (arbitral) procedural law which gives the court or tribunal the power to grant reimbursement for costs of litigation and of the pursuit of a claim according to its own discretion, these same principles should govern its deliberations; the (only) exception to this rule is a diverging agreement by the parties.[12] The *necessary* costs are therefore to be awarded; avoidable costs are to be borne by each party respectively. The same applies where costs are

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[9] *See* BAUMBACH/LAUTERBACH/ALBERS/HARTMANN, ZPO-KOMMENTAR § 91 No. 29 (Munich, 60th ed. 2002); BGB (German Civil Code) §§ 249 et seq., esp. § 254 are not directly applicable but are nevertheless relevant with respect to their basic ideas. *See also* Schiedsgericht der Handelskammer Hamburg (Arbitral Court of the Hamburg Chamber of Commerce) June 21, 1996, NJW 1997, 613, at 615, for the supplementary application of §§ 91 et seq. ZPO in arbitration.

[10] *See* OLG Düsseldorf, January 14, 1994, *available at* http://cisgw3.law.pace.edu/cases/940114g1.html, where CISG Article 74 was drawn upon as the legal basis for the claim, but the damages claimed were denied as being against good faith because the same costs had already been claimed in the proceedings on the costs of the litigation. *See also* Schiedsgericht der Handelskammer Hamburg (Arbitral Court of the Hamburg Chamber of Commerce), *supra* note 9, at 616.

[11] *See generally* BAUMBACH/LAUTERBACH/ALBERS/HARTMANN, *supra* note 9, at No. 224.

[12] *See* Schiedsgericht der Handelskammer Hamburg, *supra* note 9, at 615 (where an agreement between the parties was established by supplementary interpretation of the arbitration agreement, while the interpretation was orientated to § 91 ZPO).

claimed as part of the damages and not in the context of separate proceedings on the costs of the litigation.

3. a) If legal costs are claimed as damages under the CISG,[13] the claim has to be based on CISG Article 74. A first limit is set by the second sentence of CISG Article 74, i.e., the so-called foreseeability rule. However, that costs would necessarily be incurred in the pursuit of one's rights, in particular the costs of attorneys' fees, is certainly foreseeable at the time of conclusion of the contract and thus a part of the risk undertaken. Nevertheless, certain costs might fail this requirement, e.g., if at the time of the conclusion of the contract, contingent fees were to be considered unusual in the countries in which the parties are domiciled or, if different, where the arbitration has its seat. Should a party wish to retain the possibility of engaging attorneys on a contingent fee basis, perhaps even in addition to attorneys working on the basis of an official regulation for fees, it would have to inform the other party of this possible increased risk of costs at the time of the conclusion of the contract.[14]

b) An additional limit is the duty to mitigate the loss laid down in CISG Article 77. It restricts the efforts made by the aggrieved party confronted with a breach of contract to what is necessary. Of course, the particular difficulties of a transnational pursuit of a claim have to be taken into account. They might, for example, often require the engagement of several attorneys – in the country where the party has its place of business and in the country of the court having jurisdiction. Special expenses and efforts such as expert opinions, the payment of which will have to be made according to corresponding stipulations, will often also be unavoidable. However, a breach of contract does not give the aggrieved party a blank check as to agreements on attorneys' fees in the preparation and execution

[13] Unlike under the German Civil Code (BGB), where a delay in performance for which the obligee is responsible is necessary, under the CISG loss is recoverable from the moment when performance becomes due.

[14] For this general principle of the foreseeability rule, see SCHLECHTRIEM & STOLL, KOMMTAR ZUM EINHEITLICHEN UN-KAUFRECHT - CISG Art. 74 No. 4 (Munich, 3d ed. 2000); Peter Schlechtriem, Internationales UN-Kaufrecht, Tübingen 169 et seq., No. 302 (1996).

of the pursuit of its legal claims. In view of the general principles mentioned above underlying ZPO section 91, one should be allowed to use this provision and its interpretation developed by academics and the courts as orientation in the interpretation of CISG Article 77 in cases concerning legal costs.