



PRELIMINARY ROUND PROPOSITION 1

# GAME OF DRONES

2ND ALLEN & OVERY - NLU JODHPUR

INTERNATIONAL DEAL

NEGOTIATION COMPETITION

16 - 18 FEBRUARY, 2024

## BACKGROUND OF PARTIES

### State Defence Procurement Agency (“SDPA”)

Veridia, a developing country in South Asia, established the State Defence Procurement Agency, known as SDPA, in 1985 amidst a climate of growing regional tensions. Its inception marked the beginning of Veridia’s ambitious journey to modernise and strengthen its military capabilities.

In the early 2000s, with the world witnessing rapid technological advancements, SDPA spearheaded the import of digital technologies from Western countries and their integration with Veridia’s military hardware, setting Veridia apart in the regional defence landscape. Such technological advancements led to the emergence of new challenges such as cybersecurity threats. SDPA responded by diversifying into cybersecurity and intelligence-gathering technologies, ensuring that Veridia stayed ahead in the artificial intelligence arms race in South Asia.

However, recent developments have necessitated a significant shift in SDPA’s approach. In particular, domestic advancements in artificial intelligence and the arms industry (which were in part due to technology transfer provisions in SDPA’s defence contracts) have enabled Veridia to develop its own indigenous defence industry. This, coupled with the Government’s “Make

in Veridia” policy, has resulted in SDPA primarily procuring from within the country.

The SDPA is led by Director General Edward Masterson, a decorated military veteran known for his strategic foresight. Under his leadership, SDPA has not only enhanced Veridia’s defence capabilities but has also played a key role in fostering strong global alliances by participating in joint military exercises and defence technology collaborations.

The agency’s motto, “*Vigilance and Strength*,” reflects its commitment to maintaining a robust and ready defence force for Veridia. This commitment is evident in SDPA’s numerous contracts over the years. From acquiring state-of-the-art fighter jets to investing in cyber defence systems, SDPA’s procurement decisions have continually adapted to the evolving landscape of modern warfare. The SDPA prides itself in being ahead of the curve and ensuring that Veridia has access to technology and equipment not available to other countries in South Asia.

Despite its status as a developing country, Veridia allocates a significant portion of its national budget to defence. There is support from the public for such hefty expenditure on defence due to long-standing regional unrest and geopolitical tensions and because the public has a favourable opinion of SDPA.



## Horus Defence Systems (“HDS”)

Horus Defence Systems, or HDS, was founded in 1997 by visionary engineer, Dr. Helena Strauss, and former military officer, Col. Jacob Reynolds, and is headquartered in Nartrick, Heralia, a European country. Dr. Strauss and Col. Reynolds envisioned a company that could revolutionize defence technology with innovation at its core. HDS began as a small start-up, focusing on avionics and precision-guided munitions. Its journey is marked by successful contracts, innovative breakthroughs, and a strong ethical stance on the use of their technology.

One of HDS’s early breakthroughs came in 2009 with a contract to develop unmanned aerial vehicles (“UAVs”) for a European country. These UAVs, lauded for their precision and reliability, played a crucial role in various intelligence and reconnaissance missions. This contract put HDS on the map as a key player in drone technology.

HDS is vocal about its stance on the ethical use of its technology. The company has a policy against the use of its weaponry in situations that could lead to war crimes or a violation of international humanitarian law. This commitment to ethical practices is deeply ingrained in the company’s philosophy.

HDS’s latest development, the HawkEye drone series, stands at the vanguard of aerial surveillance, integrating cutting-edge

technology to deliver unparalleled performance in reconnaissance and intelligence gathering. The drones are equipped with state-of-the-art sensors, including a high-resolution, gyro-stabilized electro-optical camera capable of capturing 4K footage, and an infrared imaging system for night operations. At the heart of the HawkEye is a sophisticated AI-powered processing unit that enables real-time data analysis and threat identification with minimal human oversight. The drones utilize lightweight, composite materials for their airframe, reducing their radar signature while enhancing flight endurance and agility. Additionally, the HawkEye drones feature encrypted communication links for secure transmission of data. With the ability to operate in swarms and collaborate through a mesh network, the HawkEye drones offer a comprehensive package for modern military and strategic application.

While HDS has a large customer base in Europe and the North America, it has struggled to achieve any breakthrough in the Asian market due to its premium pricing. HDS hopes that the HawkEye drone series will provide it with an opportunity to establish itself in the Asian market.

## GENERAL INFORMATION

In 2022, the SDPA embarked on a significant expansion of its aerial reconnaissance capabilities by contracting with HDS for 45 state-of-the-art HawkEye drones. The drones, boasting advanced surveillance technologies capable of real-time data analysis and endurance for high-altitude long-duration missions, represented a major leap forward in Veridia's military capabilities.

The deal, struck at a substantial cost of \$350 million, laid out a four-phase delivery and payment schedule culminating in February 2024.

There was some public uproar in Veridia surrounding this deal on the basis that it apparently contravened the "Make in Veridia" policy. However, these concerns were assuaged by HDS's promise to transfer some of its technology and know-how and the involvement of domestic manufacturers in the assembly process.

Moreover, following the completion of the deal, Veridia stands to be the only country in South Asia with access to such advanced UAVs, further cementing its position as a leader in defence in the region. SDPA agreed to a 15% increase in the purchase price for the drones in order to have an exclusive supply of the drones in South Asia (although it was not fully satisfied with the duration of such exclusivity). Veridia has planned joint military operations with its key regional allies

in May 2024 at which it plans to demonstrate the capabilities of the UAVs.

In the case of HDS, the contract for the HawkEye drones was seen as the beginning of a long-term relationship with Veridia and as an entry point into the Asian market. The company recognises the potential for future contracts that could arise from the successful fulfilment of this deal.

The Parties signed the contract in April 2022 and the drone delivery began in September 2022. Until the beginning of November 2023, deliveries progressed on time. However, on 20 November 2023, HDS notified Veridia that it would be unable to deliver the remaining Phase IV drones and carry out the technology transfer in accordance with the contractual delivery schedule. In response, SDPA withheld payment for the Phase III drones (which have been delivered as scheduled).

HDS, which has several global contracts, pointed to supply chain disruptions as the reason for the delay. It asserts that the root cause of the disruptions is a conflict between Estoria, a key supplier of raw materials for defence technologies, and its neighbour, Meridinia. HDS procures essential microchips for the HawkEye drones' navigation systems from Estoria. The conflict between Estoria and Merdinia has

halted these exports, creating a critical shortage.

HDS is also facing liquidity issues, which are exacerbating its procurement difficulties.

These developments come at a time when there was already some friction between the Parties arising from alleged variations in the avionics of the drones delivered in Phase III in comparison to the agreed specifications set out in the contract. The contract provided that any alterations or modifications to the technical specifications required prior written approval from SDPA. Any failure to comply with the specifications gives SDPA a unilateral right to terminate the contract. HDS has asserted that the variations are actually ‘technical upgrades’ that will enhance the performance of the drones. SDPA, however, remains unconvinced. SDPA, with the assistance of HDS, has already completed the necessary technical training to the intended operations of the UAVs based on the contractually agreed specifications. HDS has provided 120 hours of training.

The public image of both SDPA and HDS is now under scrutiny. SDPA risks losing face both in Veridia and with its regional allies in case the contract with HDS is not completed. HDS is grappling with global media attention — a misstep in Veridia could ripple out of control, jeopardizing HDS’s reputation for reliability and punctual delivery as well as its foray into the Asian market.

The Parties have met twice in order to find an amicable and mutually acceptable resolution to their dispute. However, no resolution has been achieved. At their last meeting, both Parties threatened to formally exercise their respective termination rights and avail of the other legal remedies available to them.

## ANNEXURE-I

### *Defence Contract Agreement (relevant extracts)*

#### **Object of the Agreement**

The object of this Agreement encompasses the procurement, delivery, and local assembly of forty-five (45) HawkEye aerial reconnaissance drones, herein detailed in the attached technical appendix (**Appendix A**) of this Agreement (the “**Drones**”).

The Parties acknowledge that the Drones are intended solely for defensive and surveillance purposes.

#### **Clause 1: Sale and Purchase**

SDPA agrees to buy and HDS agrees to sell 45 Drones in accordance with the terms set out below.

#### **Clause 2: Delivery**

HDS shall comply with the following delivery schedule for the Drones:

|                  | <b>Delivery date</b> | <b>Quantity</b> |
|------------------|----------------------|-----------------|
| <b>Phase I</b>   | 1 September 2022     | 7               |
| <b>Phase II</b>  | 1 April 2023         | 14              |
| <b>Phase III</b> | 1 November 2023      | 14              |
| <b>Phase IV</b>  | 1 February 2024      | 10              |

The assembly of the Phase IV Drones will take place in Veridia, at a location to be specified by SDPA.

#### **Clause 3: Purchase Price**

The total purchase price for the Drones shall be USD 350 million. SDPA shall pay USD 50 million within 30 days of signing this Agreement. SDPA shall pay the remaining USD 300 million in a phased manner in accordance with the table set out below. Payment shall be made for each phase within 30 days of receipt of the Drones for that phase.

|                  | <b>Delivery Date</b> | <b>Payment due (USD)</b> |
|------------------|----------------------|--------------------------|
| <b>Phase I</b>   | 1 September 2022     | 50 million               |
| <b>Phase II</b>  | 1 April 2023         | 75 million               |
| <b>Phase III</b> | 1 November 2023      | 75 million               |

|                 |                 |             |
|-----------------|-----------------|-------------|
| <b>Phase IV</b> | 1 February 2024 | 100 million |
|-----------------|-----------------|-------------|

#### **Clause 4: Technology Transfer and Training**

HDS shall transfer the Information and provide the Rights to SDPA. Such transfer shall commence from the completion of Phase II and shall be completed by 1 April 2024.

HDS shall provide all necessary Know-How and Training to operate, maintain and repair the Drones. HDS's obligation to provide such Training is limited to 150 hours. HDS shall also arrange for local assembly of the Phase IV Drones in Veridia and transfer all Know-How as required for such assembly.

#### **Clause 5: Specifications and Modifications**

All Drones shall strictly conform to the specifications set forth in Appendix A (the "Specifications"). Any proposed alteration or modification to any Specification shall be notified to SDPA at least three months before the relevant Delivery Date and will require the prior written consent of SDPA:

Provided that consent for: (i) minor alterations or modifications; or (ii) upgrades shall not be unreasonably withheld.

#### **Clause 7: Force Majeure**

Subject to this Clause 7, HDS shall not be liable or responsible for its failure or delay in fulfilling or performing its obligations under this Agreement when and to the extent such failure or delay is caused by the following force majeure events: (a) acts of God; (b) flood, fire, earthquake, pandemics; (c) war, invasion, hostilities, terrorist threats or acts, riots or other civil unrest; (d) government order, law or actions; (e) embargoes or blockades in effect after the date of this Agreement; and (f) national or regional emergency.

In case of HDS's delay in fulfilling its obligations under Clause 2 due to force majeure, the Purchase Price shall be discounted as follows:

|                  | <b>Delivery Date</b> | <b>Discount for Each Month of Delay</b> |
|------------------|----------------------|---|
| <b>Phase I</b>   | 1 September 2022     | 0.2%                                    |
| <b>Phase II</b>  | 1 April 2023         | 0.2%                                    |
| <b>Phase III</b> | 1 November 2023      | 0.5%                                    |
| <b>Phase IV</b>  | 1 February 2024      | 1%                                      |

[...]

### **Clause 8: Termination rights**

8.1: Subject to Clause 7, SDPA shall have the right to terminate this Agreement in case:

- (a) HDS fails to comply with Clause 5; and
- (b) HDS fails to deliver the Drones in accordance with the Clause 2.

8.2: Exercise of such termination right is subject to SDPA notifying HDS of its default and providing HDS with a two-month period to cure such default.

8.3. HDS shall have the right to terminate this Agreement in case:

- (a) SDPA fails to comply with its payment obligations under Clause 3; and
- (b) circumstances listed in Clause 7 make fulfilment of its obligations under this Agreement impossible for a duration exceeding ten months.

8.4: Exercise of the termination right in Clause 8.3 (a) is subject to HDS notifying SDPA of its default and providing SDPA with a two-month period to cure such default.

[...]

### **Clause 9: Exclusivity**

HDS shall not enter into any agreement with any other Asian country listed in Appendix B for the supply of Drones (or equipment substantially similar to the Drones) until 1 February 2024.

[...]

### **Clause 15: Governing Law and Jurisdiction**

The law governing this Agreement and any non-contractual obligations arising out of or in connection with it shall be English law.

The Parties agree that the English courts shall have exclusive jurisdiction to determine any dispute arising out of or relating to this Agreement.

[...]



## ANNEXURE-II

*E-mail dated 7 November 2023 from SDPA to HDS on Avionic System Variations*

**Subject: Immediate Attention Required: Discovery of Unreported Avionic System Variations in HawkEye Drones**

Dear Dr. Emily Zhang,

I trust this email finds you well.

We are writing to formally address a critical issue that has recently come to our attention. It has been brought to our notice that there are certain unreported variations in the avionic systems of the fourteen HawkEye drones delivered to the SDPA by HDS as part of Phase III of the Defence Agreement.

As per the Defence Agreement, any variations or modifications to the specifications of the HawkEye drones are to be communicated to, and approved by, SDPA in writing. The discovery of these variations without prior notification and approval contravenes our agreement.

The lack of communication in this matter is not only a deviation from our contract but also raises serious concerns about the integrity of the drones' operational capabilities and, by extension, Veridia's national security.

Given the sensitive nature of our defence operations and the potential ramifications of these unreported changes, we seek an immediate and comprehensive explanation for this oversight. It is imperative that we understand the nature of these variations, the rationale behind their uncommunicated implementation, and the impact they may have on the drones' performance and our ongoing operations.

We expect HDS to provide a detailed report on the deviations from the original specifications, along with an action plan to rectify the breach of contract to the satisfaction of SDPA.

We await your prompt response to discuss the next steps.

Kind regards,

**Jacob Nethergrand**

**Director, State Defence Procurement Agency (SDPA)**

This problem is drafted by Ms. Rachana Rashmi Rammohan (Senior Member, Alternative Dispute Resolution Committee) in collaboration with Mr. Arun Mal (Senior Associate, Allen & Overy, London) and Ms. Aashna Agarwal (Associate, Allen & Overy, London). This problem is drafted purely for academic purposes and for use as a mock problem in the 2<sup>nd</sup> Allen & Overy – NLU Jodhpur International Deal Negotiation Competition 2024. The narrative adopted by the authors of the problem is purely personal and is not attributable to the organization. Resemblance to any person or organization is purely coincidental.