Chapter 5
International Contracts

International Contracts

- *Lex Mercatoria*
- International Sales Contracts
- Contracts of Distribution
- Contracts of Carriage
- Conflict Resolution

Lex Mercatoria

- *Lex Mercatoria* is the sum total of all the international agreements, international conventions, and other international trade customs that complement the domestic laws of any given country, and to which all international trade transactions are subject.

- It is difficult to comprehensively grasp *Lex Mercatoria* because it can include agreements from many different areas, such as the United Nations, World Trade Organization, multinational conventions, free trade agreements, and any number of bi-lateral agreements.

The United Nations Complex in Vienna, Austria
Source: Radu Bercan

Convention for the International Sale of Goods

- The United Nations' Convention for the International Sale of Goods (CISG) was adopted in 1980 as a way to oversee international contracts.
- The CISG allows parties from different countries to enter into contracts with reasonable assurance that the provisions of the contract will be enforced.
- More than 98 countries have ratified this agreement. Trade between these countries represents 80 percent of all word trade.

Contract Formation under CISG

- Offer

  Initial step in the formation of the contract when one party contacts another and offers to sell or purchase something.

- Acceptance

  If the second party accepts all the terms of the offer, the contract is formed.

- Rejection

  If the second party does not accept ***all*** the terms of the original offer, it is a rejection of the initial offer.

- Counter-offer

  If the second party reject the first offer, it may make a counter-offer with new terms.

Uniform Commercial Code

- The Uniform Commercial Code (UCC) is the commercial law of the United States. This is the law that is used to form contracts in domestic transactions.
- The UCC and the United Nations' Convention for the International Sale of Goods (CISG) differ in several respects.
- For several reasons, including the fact that its provisions are different from the UCC, the United States has only partially ratified the CISG.

CISG vs. UCC

CISG

- A positive response asking for change is considered a rejection.
- A contract is not been accepted until both parties agree to all terms. An offer is open until a certain date and cannot be withdrawn until said date.
- The buyer is allowed to unilaterally apply a price reduction to the amount in the contract for nonconforming or damaged goods.

UCC

- A positive response asking for change is considered an acceptance.
- Offer can be withdrawn at any time.
- The buyer cannot change the terms of the contract unless the seller performs a fundamental breach.

Contract of Distribution

- The contract between an exporter and its representatives abroad is called a distribution contract. It is a contract between the exporter and an agent or a distributor.

- There is no uniform international agreement mandating how these relationships should work. However, the parties often agree to abide by the model contracts of the International Chamber of Commerce.

Contract Law and Labor Law

- An important point to note when entering into a contract with a foreign distributor or agent is whether this relationship will be considered a “contract between equals” or a “contract between unequal partners” by the courts of the country in which the agent or distributor is located.

- In the first case, the contract will fall under contract law. Under the second, it will fall under labor law.

- The way this relationship is viewed could have a significant impact on the way courts will resolve a dispute. Under contract law, the courts will settle disputes by following the terms of the contract. Under labor law, the courts will protect the agent.

Home Government Restrictions

- Some governments make special efforts to ensure agents or distributors working in their countries are protected from deals that are not fair or equitable, and generally place all distribution contracts under labor law. Others use contract law in all cases, but most treat agent under labor law, and distributors under contract law.

- Some countries may require the agent or distributor to be a national of the home country and/or register with the government.

- Some countries also do not allow distributors, or agents, at all. The company must have a sales subsidiary.

Termination of a Contract

A contract can be terminated under two scenarios:

- Just cause

  One of the parties to the contract did not perform what it was expected to do under the terms of the contract.

- Convenience

  One of the parties to the contract wants to end the contract for reasons other than non-performance. Most often, it is the exporter/principal who wants to end the contract.

Termination for Just Cause

- Termination for “just cause” is triggered when either of the parties is not honoring the terms of the contract.
- It is generally quite easy to end a contract this way.
- However, if the contract had been renewed under similar circumstances in the past (inadequate performance), there is a possibility that a court will consider that the contract is evergreen, which means that there was an expectation it would never be cancelled.
- It is therefore important for either party to notify the other than the contract is renewed despite the non-performance, and to include a warning that future non-performance will result in termination.

Termination for Convenience

- A contract is terminated for "convenience" when it is for any reason other than just cause. It can be initiated by any of the parties (but it is normally the exporter that seeks to terminate the agreement in such a way).

- This is typically a painful way to end a contract, as the opposite party feels slighted.

- n most instances, the opposite party should be given some form of compensation by the party seeking the termination, despite the terms of the contract that may call for no compensation. Otherwise, it is possible that courts will side with the slighted party, and impose significant compensation under the terms prescribed by labor law.

Elements of a Contract of Distribution

Choice of Law	Choice of Venue	*Force Majeure*	Contract Language
Good Faith	Scope of Appointment	Territory	Corporate Accounts
Term of Appointment	Arbitration Clause	Mediation Clause	Profitability or Commission
A number of other clauses			

Elements of a Contract of Distribution

- **Choice of Law**

  This clause specifies which country's laws will be used in the case of a dispute between the exporter and the agent or distributor.

- **Choice of Venue (Choice of Forum)**

  This clause specifies the location of the court that will be used to render a judgment in the case of a dispute. It is generally in the country whose laws are specified in the "Choice of Law" clause.

Elements of a Contract of Distribution

- ***Force Majeure***

  A French expression meaning roughly "overwhelming power." This is a clause releasing all parties from their obligations due to events outside of their control.

- **Contract Language**

  The contract is signed by parties who speak different languages. This clause specifies the official language of the contract. If a copy of the contract exists in the other language, it is considered a translation.

Elements of a Contract of Distribution

- **Good Faith**

  A contract is entered into under "good faith" and assumes that neither of the parties has an ulterior motive. This clause states that both parties entered the agreement in good faith: neither party will attempt to distort the terms of the agreement.

- **Scope of Appointment**

  This clause defines the functions that the representative will perform; it is the clause that spells out whether it will be an agency or a distributorship agreement.

Elements of a Contract of Distribution

- **Territory**

  This clause defines the geographical limits within which the agent or distributor is authorized to sell. It can be a region, a country, or a group of countries.

- **Corporate Accounts**

  This clause specifies which customers will remain corporate clients, customers to which the exporter will continue to sell directly, and to which agents or distributors are not allowed to sell.

Elements of a Contract of Distribution

- **Term of Appointment**

  This clause defines the period for which representative will be appointed. This must be a specific time period and is generally renewable, as long as the agent or distributor performs adequately.

- **Profitability or Commission**

  This clause spells out the amount of commission that the agent will earn or the price at which the distributor is expected to sell the product.

  Some countries do not allow the exporter to dictate the prices or profitability of a distributor.

Elements of a Contract of Distribution

- **Arbitration**

  This clause identified the process of arbitration. Arbitrators are empowered by the parties involved in a contract dispute to reach a decision on the facts of a dispute. Their decisions are binding.

- **Mediation**

  This clause identifies the process by which the parties to a contract can attempt to settle a dispute, generally involving a third independent party, a mediator, who can suggest a compromise solution.

Elements of a Contract of Distribution

- **Facilities and Activities**

  A clause that spells out what specific facilities an agent or a distributor will maintain (buildings, store, inventory) , and what specific activities each (exporter and agent or distributor) is authorized and expected to perform.

- **Competing Lines**

  This clause outlines which competing products the agent or the distributor is allowed to represent or sell.

Elements of a Contract of Distribution

- **Confidentiality**

  A clause that binds all parties to promise not to reveal what is learned about the other's business practices for the duration of the business relationship and often after the relationship is terminated.

- **Ownership of Customers' List**

  This clause outlines who owns the customers' list, which is considered an asset. Generally, the exporter is aware of the customers' list of an agent, but does not know who the distributor's customers are.

Elements of a Contract of Distribution

- **Trademarks, patents, and copyrights**

  In the event that an agent or distributor creates intellectual property, this clause determines the ownership of that intellectual property.

Contracts of Carriage

- Pre-Carriage and On-Carriage
- International Carriage by Ocean
- International Carriage by Air
- International Carriage by Road
- Liability Conventions

Pre-Carriage and On-Carriage

- Transportation in the exporting country (before international transport) is called pre-carriage, and transportation in the importing country (after international transport) is called on-carriage.

- These are domestic contracts, undertaken under the regulations of the country in which the transport takes place

- Domestic carriers are either public carriers, contract carriers, or private carriers.

Types of Carriers (U.S.)

The United States recognizes three types of carriers:

- Common carriers perform transportation services for any company, publish their rates, and must accept cargo from anyone. They can restrict the types of cargo they take and the locations to and from which they ship.
- Contract carriers perform transportation services under contract for one or more companies. They do not publish their rates and do not accept cargo from anyone else.
- Private carriers are owned by the company for which the provide transportation.

Regulations and liability vary in function of the type of carrier.

Types of Carriers (outside U.S.)

In Commonwealth or civil-law countries, there are generally two types of carriers:

- Public carriers perform transportation services for any customer, publish their rates, and must accept cargo from anyone. They can restrict the types of cargo they take and the locations to and from which they ship. They are held to very strict liability requirements.
- Private carriers are companies that provide transportation for one or more customers. They are exempt from the requirements of public carriers, but must meet very stringent requirements to be classified as private carriers.

Regulations and liability vary in function of the type of carrier and country.

International Contracts of Carriage

The shipper has three obligations:

- deliver the goods at a time specified by the carrier
- pack the goods appropriately for their voyage
- inform the carrier of the nature of the goods, specifically if they are dangerous or sensitive to any of the risks linked to the mode of transportation.

International Contracts of Carriage

The carrier has three obligations:

- transport the goods to their destination with “due dispatch” (that is, in a reasonable amount of time) by following the agreed upon itinerary
- inspect the goods while they are loaded
- ensure that they are loaded correctly in function of their nature

In some cases, because of bad weather or for other unforeseen reasons, the carrier is unable to fulfill the contract as intended. It must deviate from the route that had been planned or must discharge the goods in a different port or airport. These events cause the contract to be frustrated.

Contracts of Carriage by Ocean (I)

There are two types of contracts of carriage by ocean:

- A charterparty

  A contract for the entire capacity of the ship, or almost all of it, used to transport commodities, such as dry bulk (grain, coal, fertilizer), wet bulk (oil), or some breakbulk (timber, paper, automobiles).

  Charterparties are complex and have different contractual clauses depending on the number of trips, the duration of the contract, and the commodities transported.

Contracts of Carriage by Ocean (II)

- A bill of lading

  A contract for a portion of the carrying capacity of a ship, usually for containers or breakbulk cargo (cargo too large to be containerized).

  The country in which the carrier operates (not that of the shipper or recipient of the goods) dictates the terms of the contract of carriage, and especially the responsibility of the carrier if the cargo is damaged while it is transported.

  In the case of containerized goods, the shipper must provide the carrier with a Verified Gross Mass certificate that lists the actual weight of the container.

Contracts of Carriage by Air

There is only one contract of carriage by air, called an air waybill. The terms of the contract are standardized worldwide and are governed by a single international convention, which is the 1929 Warsaw Convention, that was updated several times, most recently by the Montreal Protocol of 1971.

Contracts of Carriage by Road

It is difficult to generalize about international contracts of carriage by road. They can be regulated by bilateral agreements and conventions as well as by international treaties.

Contracts for the carriage of goods from the United States to Canada are subject to U.S. domestic transportation law if there are written in the U.S., and to Canadian domestic law if written in Canada.

In the European Union and neighboring countries, the Convention on the Contract for the International Carriage of Goods by Road (CMR) dictates the terms of the contract.

Contracts of Carriage by Rail

As with international contracts of carriage by road, international rail carriage can be regulated by bilateral agreements and conventions as well as by international treaties.

In the European Union, North Africa, and parts of Asia, the Convention Concerning International Carriage by Rail (COTIF) dictates the terms of the contract.

Ocean Liability Conventions

- Hague Rules

  A 1924 convention that limits carriers' liability to $500 per package. This is the convention followed by the United States and U.S. carriers.

  It also allows carriers to invoke seventeen defenses to avoid liability.

- Hague-Visby Rules

  A 1968 liability convention that limits carriers' liability to SDR 667 per package or SDR 2 per kilogram, whichever is higher. This is the convention followed by most countries.

Ocean Liability Conventions

- Hamburg Rules

  A 1978 convention that limits carriers' liability to SDR 835 per package or SDR 2.50 per kilogram, whichever is higher. It also eliminates most of the "defenses" a carrier could use to discharge itself of liability. This convention has been ratified by few countries, none of which are large trading countries.

- Rotterdam Rules

  A new liability convention (2009) that limits carriers' liability to SDR 875 per package or SDR 4 per kilogram, eliminates most of the "defenses," and that is likely to become the most commonly adopted convention by 2020.

Conflict Resolution

In the event of a dispute between two parties to a contract, whether contract of sale, contract of distribution, or contract of carriage, three options are available:

- Litigation
- Arbitration
- Mediation

Litigation

Litigation involves using courts to resolve a dispute between the parties to a contract.

There is no international court to hear a dispute between parties to an international contract; the International Court of Justice is only for disputes between governments and for disputes between a government and a company.

An international dispute must be resolved in the court selected by the international contract (Choice of Law and Choice of Forum clauses) in one country and then enforced in the other country.

Litigation

Litigation is costly and time consuming:

- It involves two sets of legal procedures; first in the country in which the dispute is heard, and then in the other country, in which the judgment must be enforced.
- It involves hiring legal representatives who can work in a foreign country.
- It involves following all the rules of evidence, all the procedural rules, and all of the legal standards that exist in two countries.

For these reasons, litigation is often the solution of last resort, after mediation and arbitration have not worked.

The International Court of Justice in The Hague, the Netherlands
Source: Ankor Light

The Tribunal of Commerce in Paris, France.
Source: Peter Haas

Arbitration (I)

Arbitration is a form of dispute resolution in which a panel of arbitrators is asked to reach a decision on the facts of the dispute. The decision of the arbitration panel is binding on the parties to the contract.

Many arbitration panels are made up of three arbitrators: one selected by each of the party, and one selected by another party, such as the International Chamber of Commerce.

Arbitration is perceived as fair, even-handed and independent.

It is much quicker and more efficient than litigation through the courts, by using a more flexible process to accept evidence, for example.

Arbitration (II)

Arbitration has other advantages as well:

- It is more “creative”

  Arbitrators can find solutions to the dispute that a court would not be allowed to use.

- It is very efficient

  Arbitrators are professionals who know the industry and are able to quickly understand a situation.

- It is private

  Unlike court proceedings, arbitration decisions are not open to the public, and the facts of the dispute are not made public.

The Arbitration Building in Lipetsk, Russia.
Source: Sergey Lavrentev

Mediation

Mediation is a process by which an independent mediator will attempt to find a middle ground between the parties who are having a dispute.

Mediation is less formal that court proceedings or arbitration, and its recommendations are not binding on the contract parties.

Mediation is more practical for small disputes following a misunderstanding, or when parties are interested in keeping a business relationship.

Mediators tend to be trade professionals with a wealth of experience in solving such disputes and who can quickly determine a solution acceptable to both parties.