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INTERNATIONAL COUNTERTRADE

Draft Legal Guide on International Countertrade Transactions

Report of the Secretary-General

Addendum

XIV. CHOICE OF LAW

Contents

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[Editorial note: The present draft chapter is a revision of draft chapter XIV, "Choice of law", published as document A/CN.9/WG.IV/WP.51/Add.5. The note in square brackets at the beginning of each paragraph indicates either the number under which the paragraph appeared in document A/CN.9/WG.IV/WP.51/Add.5 or that the paragraph is new. The revisions of paragraphs that appeared in document A/CN.9/WG.IV/WP.51/Add.5 are underlined.]

A. General remarks

1. [3] This chapter focuses on the choice by the parties to the countertrade transaction of the law applicable to the countertrade agreement, the supply contracts in the two directions, and the contract by which a party committed to fulfil a countertrade commitment engages a third party to fulfil that commitment. The chapter considers also the question whether the countertrade agreement and the contracts forming part of the transaction should be made subject to a single national law or to different national laws (section C). This chapter does not discuss the law applicable to other related arrangements in which a person who is not a party to the countertrade transaction is involved. Such other arrangements may include a guarantee supporting fulfilment of a countertrade commitment, an agreement between countertrade parties and their banks concerning linked payment arrangements, and an interbank agreement between banks involved in carrying out payment arrangements. Certain aspects of the law applicable to such arrangements are discussed in chapter XII, "Security for performance", paragraphs [3], [5] and [13], and chapter IX, "Payment", paragraphs [4], [7], [16], [18], [19], [24] and [37].

2. [1] Under the rules of private international law of many national laws, the parties are permitted by agreement to choose the applicable law, though under some of those laws there are certain restrictions on that choice (rules of private international law are in some legal systems referred to as "conflict of laws" or "choice of law" rules). If the parties do not choose the applicable law, the applicable law is determined by the application of rules of private international law.

3. [2] It should be noted that by choosing the applicable law the parties are not making a choice as to jurisdiction for settlement of any disputes. Issues relating to jurisdiction are discussed in chapter XV, "Settlement of disputes".

4. [4] Whatever be the law applicable to the countertrade agreement or the supply contracts, particular aspects of the countertrade transaction may be affected by mandatory legal rules of an administrative or other public nature in force in the countries of the parties or in the country where their obligations are to be performed. Those mandatory legal rules may regulate certain matters in the public interest, for example, international transfers of funds, the types of goods that may be traded in countertrade transactions, and restrictive business practices (see below, section D).

5. [5] In addition, the extent to which the parties may designate particular issues to be governed by the chosen law may be limited. For example, regardless of the choice by the parties, the law of the State where

goods are situated may govern the transfer of ownership of those goods, and the law of the State in which the bank holding funds is located may govern disposition of the funds. The question of which State's procedural law is to govern arbitral or judicial proceedings for the settlement of disputes arising in connection with the countertrade transaction is discussed in chapter XV, "Settlement of disputes".

6. [6] A sales contract forming part of the countertrade transaction may be subject to the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). According to its article 1, the Convention applies to contracts of sale of goods between parties whose places of business are in different States: (a) when the States are Contracting States, or (b) when the rules of private international law lead to the application of the law of a Contracting State. It should be noted that, even if the law of a State that is a party to the Convention is the applicable law, there is a divergence of opinion as to whether the Convention would apply to a countertrade agreement containing a commitment to conclude a supply contract in the future. However, uncertainty appears not to exist in the laws of some States as to the applicability of the Convention to a countertrade agreement that contains all the essential elements of the supply contract yet to be actually concluded. This is because, in those States (as noted in chapter IV, paragraph 40), a party refusing to honour such a commitment may be deemed to have consented to the actual contract of sale.

7. [7] For a discussion of contract drafting in the light of the applicable law, see chapter V, "General remarks on drafting", paragraph 6.

B. Choice of applicable law

8. [8] It is desirable for the parties to choose expressly the applicable law to govern the countertrade agreement and the supply contracts. Such an identification of the applicable law is useful because it enables the parties to gear the actions they take to fulfil their contractual obligations, or the actions taken pursuant to their contractual rights, to the requirements found in the applicable law. If the parties do not choose the applicable law, the result provided by rules of private international law may not be satisfactory to the parties. For example, absent a contrary choice by the parties, sales contracts in a counter-purchase or offset transaction are likely to be, according to the rules of private international law, subject to the law of the seller. If in such a transaction the countertrade agreement is not subject, by the rules of private international law, to the same law as the sales contract to be concluded pursuant to that countertrade agreement, contractual terms common to both the countertrade agreement and the supply contract may not be given the same meaning (see below, paragraph 25).

9. [9] An express choice of the law applicable to the countertrade agreement and the supply contracts is advisable also to avoid uncertainty as to what law applies. Uncertainty in the absence of a choice of law may arise from two factors.

10. [10] First, the applicable law is determined by the application of rules of private international law of a national law. When a dispute arises concerning the countertrade agreement or a supply contract that is to be settled in judicial proceedings, the rules of private international law

applied by the court settling the dispute will determine the applicable law. A court will apply the rules of private international law of its own country. If there is no exclusive jurisdiction clause agreed upon by the parties (see chapter XV, "Settlement of disputes", paragraph [41]), the courts of several countries may be competent to decide the dispute (e.g., the countries in which the parties to the dispute have their places of business or the country in which the obligation in question is to be performed). There may therefore be several possible systems of private international law that could determine the law applicable to the countertrade agreement or the supply contract. When disputes are to be settled in arbitral proceedings, the arbitral tribunal will determine what law is applicable, unless the parties have chosen the applicable law. In some cases, the arbitral tribunal will determine the applicable law according to the private international law rules that the tribunal considers appropriate; in other cases, the arbitral tribunal will directly determine the applicable law that the tribunal considers appropriate for the case, without express reference to the rules of private international law. It may be difficult to predict on which criteria or rules the arbitral tribunal will rely in determining the applicable law.

11. [11] The second factor producing uncertainty as to the applicable law is that, even if it is known which system of private international law will determine the applicable law to govern the countertrade agreement and the supply contracts, the criteria and concepts used in that system may be too general or vague to enable the parties to predict with reasonable certainty which law will be determined to be applicable. This difficulty is compounded in the case of countertrade agreements because of possible uncertainty as to the legal nature of the countertrade agreement and the consequent uncertainty as to which rule of private international law should determine the applicable law.

12. [12] [paragraph 13 as it appeared in A/CN.9/WG.IV/WP.51/Add.5 has been incorporated in the present paragraph] The extent to which the parties are allowed to choose the applicable law will be determined by the rules of private international law being applied. Under some systems of private international law, the autonomy of the parties is limited and they are permitted to choose only a national law that has some connection with the contract, such as the law of the country of one of the parties or of the place of performance. Such a limitation is sometimes referred to as the "nexus" rule. Under other systems of private international law, the parties are permitted to choose the applicable law to govern the countertrade agreement and the supply contracts without those restrictions. Since a court that is to settle a dispute will apply the rules of private international law in force in its country, the parties should agree upon a choice of law that would be upheld by the rules of private international law in the countries whose courts might be competent to settle their disputes. If the parties are considering an exclusive jurisdiction clause, they should pay particular attention to whether courts in the contemplated jurisdiction would uphold their choice of law. If a dispute is settled in arbitral proceedings, the law chosen by the parties will normally be applied by the arbitral tribunal. In order to avoid the application of a nexus rule, parties sometimes expressly stipulate in the choice-of-law clause that that rule should not apply. It should be noted that such a stipulation may have no effect inasmuch as the nexus rule is likely to be considered mandatory. The likelihood that such a stipulation would be upheld appears to be greater in arbitration proceedings.

13. [14] When choosing the law to govern the countertrade agreement or the supply contracts, it is in general advisable for the parties to choose the law of a particular country. The rules of private international law of a country where legal proceedings may be instituted in the future may not recognize the validity of a choice of general principles of law or of principles common to several countries (e.g., of the countries of both parties). Even if such a choice would be valid, it may be difficult to identify principles of law that could resolve disputes of the type arising in connection with a countertrade agreement or a supply contract. Nevertheless, such a choice might be feasible in certain circumstances.

14. [new paragraph] When an international convention relevant to the countertrade transaction is in force in a State, it is widely accepted that the choice of the law of that State will include that international convention. Such a choice of a convention through the choice of the national law is expressly recognized in article 1(b) of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). Article 1(b) provides that the Convention applies to contracts of sale between parties whose places of business are in different States when the rules of private international law lead to the application of the law of a Contracting State.

15. [new paragraph] In some States it is recognized that parties can agree that their transaction should not be governed by a national law but by an international convention or by other rules of law such as an international legal text not having the force of an international treaty or a set of legal principles dealing with international trade. Other States, however, require the applicability of a national law, so that any international convention or other rules chosen by the parties will apply in so far as they do not contravene the mandatory provisions of the applicable national law.

16. [15] In many national laws a choice-of-law clause is interpreted as not to include the application of the rules of private international law of the chosen national law even if the clause does not expressly so provide. However, if that interpretation is not certain, the parties may wish to indicate in the clause that the substantive legal rules of the national law they have chosen are to apply. Otherwise, the choice of the national law may be interpreted as including the private international law rules of that national law and those rules might provide that the substantive rules of another national law are to apply.

17. [16] The parties may wish to choose as the applicable law the law of the country of one of the contracting parties. Alternatively, they may prefer to choose the law of a third country which is known to both parties and which deals in an appropriate manner with the legal issues arising from the countertrade agreement or from the supply contract. If the countertrade agreement or a supply contract provides for the jurisdiction of the courts of a particular country to settle disputes between the parties, the parties may wish to choose the law of that country as the applicable law. This could expedite judicial proceedings and make them less expensive, since a court will normally have less difficulty in ascertaining and applying its own law than the law of a different country.

18. [17] In the case of countries that have two or more territorial units in which different laws are applicable (as in some federal States), it is advisable to specify which one of those laws is to be applicable in order to avoid uncertainty.

19. [18] The parties may also wish to take the following factors into consideration in choosing the applicable law: (a) the parties' knowledge of, or possibility of gaining knowledge of, the law; (b) the capability of the law to settle in an appropriate manner the legal issues arising from the contractual relationship between the parties (for example, the parties may wish that their countertrade commitment to enter into future contracts would be given effect under the chosen law); (c) the extent to which the law contains mandatory rules that would prevent the parties from settling by agreement questions that arise in their contractual relationship.

20. [19] Changes legislated in the law chosen by the parties to govern the countertrade agreement and the supply contract may or may not affect contracts in existence at the time those changes are made. If the parties wish that only the legal rules in force at the time the countertrade agreement or supply contracts are entered into are to apply, it is advisable that they expressly so provide. However, parties should be aware that such a restriction will not be effective if the application of the changes in the legislation to existing contracts is mandatory.

21. [20] Different approaches are possible with respect to the drafting of a choice-of-law clause. One approach may be merely to provide that the countertrade agreement or the contract is to be governed by the chosen law. This approach may be sufficient if it is clear that the body chosen to settle disputes between the parties will apply the chosen law to all the issues that the parties desire to be regulated by it. A second approach may be to provide that the chosen law is to govern the countertrade agreement or contract in question, and also to include an illustrative list of the issues that are to be governed by that law (e.g., formation of contract, or breach, termination, or invalidity of the countertrade agreement or contract). This approach may be useful if the parties consider it desirable to ensure that the issues contained in the illustrative list in particular will be governed by the chosen law.

22. [21] Under the private international law of some countries a choice-of-law clause may be considered to be an agreement separate from the rest of the contract between the parties. Under those laws, the choice-of-law clause may remain valid even if the rest of the contract is invalid, unless the grounds for invalidity also extend to the choice-of-law clause. Where the contract is invalid but the choice-of-law clause remains valid, the formation, the lack of validity, and consequences of the invalidity of the contract will be governed by the chosen law.

23. [22] Under most systems of private international law the chosen law may govern the prescription of rights, while under some systems rules relating to prescription (limitation of actions) are of a procedural character and cannot be chosen by the parties in their contract; in those cases the procedural rules of the place where the legal proceedings are brought will apply. The Convention on the Limitation Period in the International Sale of Goods (New York, 1974) as amended by the Protocol of 1980 provides in its article 3 that, unless the Convention provides otherwise, the Convention applies irrespective of the law which would otherwise be applicable by virtue of the rules of private international law. As discussed above in paragraph 6, it may be uncertain whether countertrade agreements committing the parties to the future conclusion of a sales contract fall within the scope of application of the United Nations Convention on Contracts for the International Sale of

Goods. Similarly, it may be uncertain whether such countertrade agreements fall within the scope of application of the Convention on the Limitation Period in the International Sale of Goods.

24. [23] The parties may include in the countertrade agreement a choice-of-law clause that will designate the applicable law not only for the countertrade agreement but also for the future supply contracts to be concluded pursuant to the countertrade agreement. In this way the parties may settle in the countertrade agreement an issue that they would otherwise address in each supply contract.

C. Choosing the same or different national laws to govern countertrade agreement and supply contracts [title changed]

25. [24] In making an express choice of the applicable law, the parties may wish to consider whether the countertrade agreement and any future supply contracts to be concluded in one direction or in both directions pursuant to that countertrade agreement should be made subject to a single national law or to different national laws. The application of a single national law may be desirable when the countertrade agreement stipulates terms of the future supply contracts and the parties wish to ensure that the legal meaning of terms stipulated in the countertrade agreement would remain the same when those terms are subsequently incorporated in a supply contract. Consistency of legal meaning may be desirable in particular with regard to terms concerning payment mechanisms (see chapter IX, "Payment", paragraph [16]), quality of the goods, and terms of delivery.

26. [25] If the parties have structured their obligations in such a way that their obligations arising from the supply contracts in the two directions are interrelated to a high degree, they may find it appropriate to subject all their mutual rights and obligations to a single national law. The obligations of the parties are closely interrelated, in particular, in barter transactions (see chapter III, "Contracting approach", paragraphs 3 to 8) and in direct offset transactions (see chapter II, "Scope and terminology of Legal Guide", paragraph 17). The application of more than one national law to such transactions may lead to inconsistency between obligations of the parties.

27. [26] In the case of counter-purchase, buy-back and indirect offset transactions, the obligations of the parties arising, on the one hand, under the supply contract in one direction (export contract) and, on the other hand, under the countertrade agreement and the supply contract in the other direction (counter-export contract) are usually not interrelated to the same degree as the obligations are interrelated in barter or direct offset transactions. In these cases, no generally valid advice can be given as to whether it would be preferable for the parties to subject their obligations to one national law or to different national laws. In some of these cases, the parties may wish to subject all their obligations to one law. They may wish to do so since it may be simpler to administer the countertrade transaction and to obtain the necessary legal advice with a view to a single national law rather than to have to take into account more than one national law. There may, however, be situations in which the parties decide to subject the export contract to one law and the counter-export contract to another law. The parties might choose different laws when, on the one hand, there are special

reasons for making one of the contracts subject to the law of a particular State and, on the other hand, the parties do not wish to subject the entire transaction to that law. Such special reasons concerning one of the contracts may be, for example, mandatory rules of a State of a party requiring certain types of contracts to be subject to the laws of that State, trade practice according to which one of the contracts is traditionally made subject to a particular national law, or the conclusion of the contracts by different sets of parties. If the parties decide to subject the supply of goods in the two directions to different national laws, the parties may wish to consider, as noted above in paragraph 25, to subject the countertrade agreement and the supply contract to be concluded pursuant to it to the same law.

28. [27] When the party originally committed to purchase engages a third party to fulfil that commitment, the party originally committed and the third party may wish to subject the contract by which the third party is engaged to the law governing the countertrade agreement. Such a choice would help to ensure that terms found both in the countertrade agreement and the contract engaging the third party would be given the same meaning. (The need for coordination between the contract engaging a third party and the countertrade agreement is discussed in chapter VIII, "Participation of third parties", paragraphs [22] to [25]. Certain other aspects of the law applicable to participation by third parties are mentioned in paragraphs [7], [9], [13] and [16] of chapter VIII.)

29. [28] When the countertrade agreement is incorporated in an export contract (see chapter III, "Contracting approach", paragraph 17), a choice-of-law clause in the export contract would, absent a contrary provision, cover the clauses making up the countertrade agreement.

D. Mandatory legal rules of public nature

30. [29] In addition to the applicable law, mandatory rules of an administrative or other public nature in force in the countries of the parties and in other countries (e.g., the country of a third-party purchaser or of a third-party supplier or the country in which the proceeds of the supply in one direction are being held) may affect certain aspects of the countertrade transaction. These mandatory rules may be addressed to residents or citizens of the State that issued the rules, or to certain business activities being carried out or having an effect in the territory of the State. They may be enforced primarily by administrative officials. Their purpose is to ensure compliance with the economic, social, financial or foreign policy of the State. The parties should take these mandatory rules into account in drafting the countertrade agreement and the supply contracts. (Mandatory governmental regulations are also discussed in chapter II, "Scope and terminology of legal guide", paragraphs 9 and 10.)

31. [30] Such rules may be of a general nature, applicable to various types of commercial transactions, or they may be specific to countertrade. Rules of a general nature often relate to safety requirements, environmental protection, health and labour conditions, consumer protection, employment of local personnel, restrictive business practices (see chapter X, "Restrictions on resale of countertrade goods", paragraph 3), customs duties, taxes, and restrictions on exports, imports, transfer of technology and payment of foreign exchange.

32. [31] Mandatory rules specific to countertrade may provide, for example, that: (a) specified types of countertrade transactions require governmental approval; (b) importing of certain types of goods may be carried out only within the framework of specified forms of countertrade; (c) only certain types of goods are permitted to be offered in a countertrade transaction (see chapter VI, "Type, quality and quantity of goods", paragraphs 3 and 40); (d) goods purchased in fulfilment of a countertrade commitment must meet origin requirements (see chapter VI, paragraph 4, and chapter IV, "Countertrade commitment", paragraph 26); (e) evidence accounts are permitted to be used only under specified conditions (see chapter IV, "Countertrade commitment", paragraph 69); (f) the purchase of certain types of goods is to be credited toward the fulfilment of the countertrade commitment at specified rates (see chapter IV, "Countertrade commitment", paragraphs 31 to 34); (g) prior governmental authorization is required for linked payment arrangements restricting foreign currency payments into the country (see chapter IX, "Payment", paragraphs [5] and [18]); (h) specified financial institutions must be used for payment (see chapter IX, paragraphs [24] and [37]).

33. [32] The parties may wish to address in the countertrade agreement the possibility that fulfilment of the countertrade commitment would be impeded by the promulgation or modification of a mandatory rule after the conclusion of the countertrade agreement. Such clauses are discussed in chapter XIII, "Failure to complete countertrade transaction", section D.