LEGAL CONCERNS IN EXPORTING TO LATIN AMERICA

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A common perception of companies who are hesitant to try their hand at exporting is that the inherent risks, including legal concerns, outweigh the potential rewards. Quite often this is true, especially with regards to exports to Latin America. The lowering of barriers to trade and investment over the years in many Latin American countries has reduced many of the legal risks of doing business in the region and created new opportunities for U.S. exporters and investors. For example, the recent political and economic liberalization which is taking place in certain Latin American countries such as Mexico has reduced the risks and created opportunities for U.S. exports to these countries. But even with these noteworthy changes, there nevertheless remain important legal concerns in exporting to those countries in Latin America which are in the forefront of political and economic liberalization, not to mention those which are lagging behind. This article will identify these legal concerns, and will recommend ways in which the U.S. exporter can effectively deal with them.

Civil Law System

One major legal concern in general which U.S. exporters need to keep in mind when doing business with Latin America is that the countries of Latin America have an entirely different legal system than that in the U.S. Under the Common law system in the U.S. (except in Louisiana, which utilizes the Civil law system) law, including statutes and codes, is primarily developed and interpreted by the judiciary; a court's application of a given law to a certain fact situation generally provides a binding precedent for future applications of the same law to similar fact situations. Additionally, when a novel fact situation arises which is not covered by any statutes or prior case law, common law judges will usually fashion rules to apply to that fact situation, rules which then became legal precedent. While it is true that in many instances, Common law courts do not always follow precedent, the predominant feature of the Common law system continues to be *stare decisis*- even if a court does not follow precedent, it must least *consider* it.

In Latin America, however, under the Civil law system, previous decisions by courts which apply a given law to a certain fact situation do not as a matter of law form a precedent for future applications of the same law to a similar fact situation. Rather, the Code (or statute) itself is supreme in all instances to any previous judicial interpretation of the Code. Civil law judges do not operate under the rule of *stare decisis*. If the code is silent, civil law judges will turn only to local custom or general principles of law to determine the law to apply to a certain factual circumstance. Therefore, while not prohibited from examining prior decisions, they also are not required to consider, or much less to follow prior decisions. Furthermore, in many instances, it will be an administrative official or governmental agency, rather than a court, who determines the application of the Code to a particular fact situation. While a Civil law court may indeed examine prior decisions, the precedential value of those decisions in most instances will only provide one *factor* in the court's overall determination of the application of a Code provision. Perhaps the difference between these two legal systems is best summarized by stating that in a Common law system prior decisions are *binding*, while in a Civil system they are merely *permissive*.

To give a practical example of what this can mean for the U.S. exporter, say you and your Latin American importer contractually agree that all purchase orders from Latin America will be transmitted using EDI. During one transmission a poor line connection results in incorrect data being transmitted which, in turn, leads to a late delivery of goods. EDI transfers are a relatively new development, and are not covered extensively or at all by statutes in either the U.S. or Latin America. In the absence of such statutes, U.S. courts would either turn to previous court decisions with the same or similar factual patterns, or would develop new rules of law. On the other hand, without a specific statute to apply, Latin American courts would only rarely, if ever, turn to previous decisions. Rather, a civil law court would examine local custom or general principles of law, matters which might not have any relevance whatsoever to EDI transfers involving transmission errors, and would be very hesitant to develop any new rules of law to apply to a novel fact situation.

What all of this means for the exporter is that if a particular trade transaction is governed by the Civil law, previous ways in which the law was applied to the same or similar transaction may not provide any basis for an exporter to make any judgments about the likely legal treatment of the transaction in the Latin American country. A concrete example would be where a Latin American agent has filed a lawsuit in the agent's home country against a U.S. exporter for an alleged unpaid commission. Regardless of how a previous court may have interpreted the provision of the relevant Code which governs agent commissions, the exporter could not be sure that the judge in the present case would even consider the previous decision. The practical result is that legal predictability for the U.S. exporter may be far less certain in much of Latin America than it is in the U.S. The relevancy of this to the U.S. exporter is that since Latin American courts do not as a general rule turn to previous cases to determine the law to apply, the accumulated occurrences of previous exporter–importer contractual disputes in the courts of a Latin American country are not usually available to provide any guidance to the exporter as to how a particular dispute might be resolved. It is also one reason why, as shall be seen later, it is vital to negotiate a choice of law clause if at all possible.

Economic Nationalism

Along with the above, in general the U.S. exporter also needs to be aware of the continuing impact of economic nationalism on law in Latin America. While not a monolith in terms of political, economic and legal structures, Latin America nevertheless has great similarities from country to country as regards these structures. One of the most prevalent has been, and continues to be economic nationalism. Even though much of Latin America today is beginning to make tentative, and in some cases, strong moves towards free markets and internationalization of their economies, the legal structures in most Latin American countries which govern commerce and trade remain strongly influenced by economic nationalism.

One of the most prevalent ways in which economic nationalism will continue to strongly influence economic law in Latin America is in the form of covert and overt discrimination against foreign business interests. This discrimination, for example, might include limits on foreign royalty payments and profit expatriation, or required minimum agent commissions, just to name a few.

This discrimination quite frequently is not actual overt discrimination, meaning that foreign firms are treated differently than local firms, but rather consists of laws and regulations which have a discriminatory *effect* on foreign companies.

Legal change generally lags behind economic and technological change as the mechanics required to change law are far more complex and convoluted than that which is to develop new technology or products. Only as economic and technological forces, primarily influenced by global competitive factors, threaten to leave an nationalistic economy far behind (as has happened in the last few years in Mexico), will economic nationalism no longer have the present impact it has upon international commercial and trade law in most of Latin America.

The following can be helpful when dealing with issues of economic nationalism:

» When negotiating agreements with parties in Latin, America, always remember that as an exporter you are a foreigner and that the legal system will probably treat you as one.

» Additionally, always employ local counsel in the importer's country. They can not only provide you with contacts, they can also improve your local image and bargaining position.

» Joint ventures can be another solution to get around this problem of being perceived as a foreign business interest.

International Sale of Goods Contracts

Choice of Law

Perhaps the most fundamental legal concern for exporters is the law which governs their international sale of goods contracts. Fortunately, most countries accept the principle, called party autonomy, that the parties to a contract are free to contractually choose the law which will govern their contract. The conditions usually imposed is that the law chosen must bear a reasonable relationship to the underlying transaction, and that the choice of law itself must not violate the public policy of the countries of which the contract's parties are citizens.

The use of choice of law clauses in export contracts with Latin American importers, however, can be a problem due to the fact that most Latin American countries historically have not recognized party autonomy. In particular, this lack of recognition is relevant when it comes to enforcing a U.S. judgment in the importer's country or litigating the dispute entirely in the importer's country itself. If the parties have chosen the law of a country other than that of the Latin American importer's country, a court in a Latin American country may ignore the parties' choice of law and rule that the importing country's law must govern the contract. Using choice of law clauses in export sale of goods contracts with Latin American importers, however, are usually only a problem if the exporter is seeking enforcement in a Latin American country of a judgment which was obtained in the U.S. against the Latin American importer. In those instances, if the parties to a contract choose law other than that of the Latin American importer's country, and then either litigate that contract in that Latin American country or seek to enforce a U.S. judgment there, the court in that country may ignore the parties' choice of law clause, and rule that that country's law must instead govern the contract. This potential problem is less of a concern than its used to be due to the fact that many Latin American countries are now beginning to recognize the principle of party autonomy. Therefore, choice of law clauses are strongly recommended for U.S. exporters to in their international sale of goods contracts with Latin American importers

UCC vs. CISG

The law preferred by most U.S. exporters to govern their international sale of goods contracts in the Uniform Commercial Code, Article 2, Sale of Goods, which has been adopted in all states except Louisiana. The UCC is widely praised for its consistency and practicality in governing sale of goods contracts. However, many countries, including a number in Latin America, feel uncomfortable with the UCC, in part because it is has common law requirements (such as consideration). Therefore, for several years the U.N. worked on a Convention which would in theory provide a uniform law for international sale of goods contracts, much like the UCC has done in the States. The U.N. Convention on Contracts for the International Sale of Goods (CISG) is the result.

The CISG Convention, however, is not the panacea which many of its promoters claim. The biggest problem is that even if every single international sale of goods contract were governed by the CISG, the effect on exporters and importers still would not be uniform because there does not exist an international court which can uniformly interpret the CISG. The CISG, as with any other source of law governing an international contract, will still be interpreted by a domestic court. In many instances, if not most instances, it is the interpretation of a law which is the most critical concern.

The U.S. is currently a party to the CISG, and upon ratification stated that the CISG will govern a contract for the international sale of goods whenever the contract is between a U.S. exporter and a foreign importer from a country who also is a party to the CISG, unless the parties to the contract choose some other law to govern the contract. What this means to the U.S. exporter is that in the above situation, the CISG will automatically govern your contract if it does not have a choice of law provision. In other words, the CISG automatically applies to a U.S. exporter's sales contract if there is no choice of law clause and the importer is from a CISG-member country. Many U.S. exporters, therefore, are unwittingly entering into contracts without knowing that the CISG is governing their contract. While this is not necessarily a bad thing in that the many CISG provisions are very similar to those of the UCC, it is critically important to know before entering into any international contract what law is going to govern the contract.

One important difference is that unlike the UCC, which requires all sales contracts over $500 to be in writing in order to be enforceable, the CISG has no writing requirement. U.S. exporters, used to considering a deal done only when it is in writing, may end up entering into an enforceable sales contracts merely by making or accepting offers over the telephone. The CISG also requires that any acceptance of an offer must "mirror" the terms of the offer. Under the UCC, a party's response to an offer that adds additional terms does not constitute a rejection of the offer if the additional terms add only minor changes. A U.S. exporter, unaware that the CISG is governing its offer to an Argentinean importer, might consider the additional terms in the importer's faxed response to its offer to be so minor that it considers the response to be an acceptance, and then begins the process of delivery only to later discover that the Argentinean's response was not an acceptance but rather a rejection and a counteroffer. While other differences exist as well, until a body of law interpreting the CISG is developed, it will remain uncertain as to the extent of the differences between the UCC and the CISG.

Keep the following points in mind when negotiating your contracts:

» In choosing which law you propose to the other party to govern your international sale of goods contract, it is best if you can get the other party to agree to choosing the UCC since it is the law with which you will be most familiar.

» Also important to remember in this regard is that most judges in the U.S., particularly in state courts, are unfamiliar with the CISG, and may not know how to interpret it. This will also be true in most foreign countries.

» If the other party is intractable in refusing to agree to the UCC as the governing law, then propose the CISG, which is your second best alternative. Even if the other party's government has not signed the CISG, you may still choose it to govern.

Latin American Agency & Distributorship Law

Most exporters market their goods in foreign countries through agency or distributorship arrangements. There are several important legal concerns for exporters in the use of these relationships in exporting to Latin America.

Agency Relationships

Agency law in Latin America differs widely in many aspects from agency law in the U.S. Other than agency relationships arising in an employer/employee context, agency law in the U.S. falls solely under the province of commercial law. Parties to an agency agreement in the U.S. have complete freedom of contract, provided that the scope of the agency agreement itself is not illegal in terms of its subject matter. The vast majority of states do not even have statutes covering agency relationships as they do for partnerships and corporations. In most Latin American countries, on the other hand, agency law falls under the general area of labor law as well as under commercial law, and the parties freedom to contract is often highly regulated. Furthermore, if a local agent contracts with a foreign exporter, the local law of that country will generally govern the contract as to such matters as agent commissions, termination, and the like (Bolivia, for example, requires that Bolivian law govern the agreement if enforcement of the agreement will be sought in Bolivia).

The most important concerns regarding agency law in Latin America are the scope and powers of the agent, agent compensation, and termination of the agency relationship. Many Latin American countries divide agents into commission and non-commission agents. Virtually all Latin countries do not allow agents to act for non-disclosed principals. In this regard, the agency arrangement must be placed on the local country's *commercial registry,* which is a device unknown in the States. Some Latin countries restrict the use exclusive agencies. Many Latin countries also have minimum or maximum commission rates which can be paid to commission agents.

Finally, perhaps the area of agency law most troublesome for U.S. exporters is the standard requirement that notice be given in order to be able to legally terminate an agency relationship. U.S. companies are used to being legally able to terminate agency relationships at will with little or no notice. However, most Latin American countries require a minimum notice period of at least thirty days (Brazil, for example, requires a payment to an agent of one-third of all commissions earned over the last three months if the required thirty day notice of termination is not given). This requirement for obvious reasons can hamper the effective use of agents for marketing of goods in Latin America. The profitable use of Latin American agents is certainly not impossible by any means; the U.S. exporter, however, must carefully draft its agency agreements to avoid running afoul of the local laws which may indeed make the use of an agent an unprofitable exercise.

Distributorship Relationships

Distributorships are often considered by developing countries, including those in Latin America, to be an attractive alternative to agency arrangement. This is true in part because distributors are typically seen as possessing greater bargaining power than agents since they take title to goods. It is very important when using a distributorship relationship in Latin America to make it clear in the agreement that title will pass to the distributor. Many Latin American countries use the term "distributor" to mean "agent", as do many exporters themselves. Woe to the exporter who discovers upon the theft or destruction of goods in a foreign country that its supposed foreign distributor is really an agent, thereby leaving the exporter holding the proverbial bag.

In general parties have greater freedom of contract in distributorship relationships in Latin America than they do in agency arrangements. One area, however, which is very critical in distributorship as it is in agencies is termination. Many Latin countries will provide local distributors with special protection from early termination when the distributor is required by its agreement with a foreign exporter to make substantial investments in facilities or marketing. Termination can also cause a problem for the exporter if the distributor is left with a substantial inventory of the exporter's goods upon termination. This may allow the distributor to become a competitor to the exporter in that country. This problem can be avoided by requiring the distributor to resell any leftover inventory back to the exporter upon termination.

Also important to distributorship are such concerns as exclusive arrangements and price resale maintenance. The latter is often illegal, which may give the exporter very little control, if any, over the price the distributor is reselling the goods it purchased from the exporter.

Agency vs. Distributorship

No hard and fast rule legally speaking applies when choosing between the use of an agency or distributorship arrangement in marketing of goods in Latin America. It is recommended that the U.S. exporter first decide from a business standpoint which option is more attractive, and then analyze the legal issues arising from the use of either relationship.

This issue of termination of agency and distributorship relationships can be dealt with by the following method:

» A U.S. exporter can provide itself with the option of termination at will in agency or distributorship agreements by stating in the contract certain conditions that will result immediate termination. This is usually recognized and enforced in Latin American countries.

Organizational Structures

U.S. exporters who wish to develop a direct presence in Latin America can choose between roughly the same organizational structures that are available in the U.S. -- partnerships or stock companies (corporations or limited liability companies). In Latin America, however, many of these forms differ significantly in scope and detail.

Latin American countries offer a form of limited partnership similar to that in the U.S. called Sociedad de Responsabilidad Limitada (*S. de R.L.*). This option limits the liability of investors for partnership obligations to the amount of their investment and allows them to avoid the requirements of corporate structures. As in the U.S., a general partner with unlimited liability must be a partner of the *S. de R.L.* Foreign investors are advised to locate a local partner to fulfill this role. Latin American countries also have a general partnership structure in which all partners have unlimited liability. Unlike the U.S., Latin American countries additionally permit partnerships that include a silent partner, a Sociedad an Comandita (*S. en C.*).

The civil law equivalent of the U.S. corporation in Latin America is a stock company called Sociedad Anonymous (*S.A.*) or Sociedad de Capital e Industria. Latin American countries also allow a type of stock company, the Sociedad Anonymous Responsabilidad Limitada (*S.A.R.L.*) -- often called limited liability companies -- that resembles U.S. limited partnerships insofar as shareholders can be held liable for company obligations up to the amount of their investment, but which nevertheless must have a corporate charter. These limited liability companies, however, are not the equivalent to U.S. limited liability companies. The biggest difference in general between U.S. corporations and Latin American stock companies is that under the civil law these stock companies receive their life not from a state-granted charter, but rather from a contractual arrangement between two or more persons. This means that, unlike in the U.S., single stockholder stock companies cannot exist in Latin America because one cannot presumably contract with one's self. Since this restriction applies to both individual and corporate stockholders, U.S. corporate exporters interested in forming stock companies must find at least one other person someone to serve as a co-shareholder, which can be either an individual or a business entity.

Intellectual Property Law

U.S. companies doing business In Latin America must also take steps to protect their intellectual property rights. While the U.S. is a party to the Pan Am Convention, that Convention only guarantees that persons which own intellectual property rights in a foreign country will receive the same protection as domestic owners of such rights. The fundamental rule is that in order to obtain intellectual property right protection in a country, you must obtain the protection under that country's rules. The U.S. has yet to enter into any treaty which states that the ownership of a patent, trademark, or copyright in the U.S. automatically entitles a party to the same right in another country.

An exporter, therefore, who holds a U.S. trademark does not necessarily have the right to exclusive use -- or any use at all -- of that trademark in Latin America. To obtain protection, a trademark must he registered with every national governmental. Trademark registration requirements in Latin America are quite often completely different from U.S. requirements. If an exporter is tardy in registering his mark, he may find that a local competitor has already obtained the right to use his mark in that country. Fortunately, with the recent U.S. accession to the Madrid Protocol, it is now easier for U.S. trademark holders to obtain trademark protection in foreign countries by applying for protection directly with the World Intellectual Property Organization. In regards to patent law, the law in virtually all countries in Latin America holds that the first-to-apply usually receives the patent, which recently also has become the law in the United States. The main point is that mere possession of a U.S. patent, trademark, or copyright means nothing in the country to which you export.

The following are some ways you can enhance your intellectual property protection:

» Require your agents and distributors in their agency and distributorship contracts to obtain protection of your intellectual property in their territory.

» Your agency and distributorship contracts should also state that your agent's and distributor's failure to obtain protection of your intellectual property makes you eligible for damages.

Dispute Resolution

International commercial arbitration has been the method of choice for dispute resolution between exporters and importers throughout most of the world. Arbitration, however, is often not used in Latin America because many Latin American countries traditionally have not enforced arbitral awards obtained outside that country. Some Latin American countries, however, have bound themselves by a treaty, the New York Convention, to recognize foreign arbitral awards. Such countries include Argentina, Chile, Columbia, Costa Rica, Ecuador, Guatemala, and Mexico (the U.S. is also a party). Several Latin American countries have also signed the Panama Convention which states that unless contractually otherwise agreed, arbitration between member countries will be conducted under the rules of the Inter-American Arbitration Commission.

In order for arbitration to be binding, your export contract must include an arbitration clause. When drafting such a clause, the most important considerations are the rules to be used and the site of arbitration. It is recommended that exporters to Latin America use the rules of the Inter-American Commercial Arbitration Commission, and site arbitration in a neutral third-country in Latin America. Other considerations include the number of arbitrators and the method for choosing them. It is best to contractually agree to three arbitrators, with each party choosing one, and the two nominees choosing the third.

Countries that do enforce foreign arbitral awards will generally enforce them when the arbitration rules are followed, the arbitrators show no bias, and the awards do not contravene local public policy. Even though not all Latin American countries recognize foreign arbitral awards, U.S. exporters to Latin America should make arbitration clauses standard in their contracts and, when a dispute arises, let the specific circumstances determine whether you will resort to arbitration.

As is the case with international commercial arbitration, the most crucial issue in international commercial litigation is the enforceability of a foreign judgment. As has been learned by many firms from sad experience, unenforceable judgments are not worth the paper they are written on. The reasons that foreign courts do not enforce a judgment include defective service of process, or failure to recognize a choice of law or forum clause. The prospects of the slow, tortuous ordeal of litigating in Latin American courts must he weighed against the likelihood that a judgment obtained in a U.S. court will be enforced. Enforcement of U.S. judgments in Latin American courts is not impossible, but you should identify obstacles to enforcement in advance and prepare yourself accordingly.

Keep in mind these basic points before embarking upon international commercial arbitration or litigation:

- Arbitration is not necessarily faster or cheaper than litigation. Its main advantages are that evidence rules are less stringent and that arbitrators are -- or should be -- experts in the factual areas of the dispute.

- Litigate in the country in which the importer's assets are located.

- Whenever possible, obtain some up-front security or surety against non-performance by the other party.

Conclusion

In general, always remember that the true value of a contract is not necessarily its enforceability, but rather its capacity for making all parties feel they must abide by its terms. When you negotiate those kinds of contracts, and know what legal concerns to watch out for and guard against, then you will greatly enhance your prospects for success and well positioned to break into Latin America's most tempting markets.