ABA Section of International Law
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Newsletter of the
INTERNATIONAL COMMERCIAL TRANSACTIONS, FRANCHISING AND DISTRIBUTION COMMITTEE

Summer 2013

Editor's Note

Welcome to the re-launch of the Newsletter of the International Commercial Transactions, Franchising and Distribution Committee. Since this is the first issue in several years, we wanted it to serve as a vehicle to re-introduce the variety of issues that fall within the Committee's charge. So, rather than focusing articles on a particular area of Committee business (as we will do in the future), we cast a wide net for submissions. Committee members were asked to submit articles of any length and on any topic, the only requirement being that the article relate to the business of this Committee – commercial transactions, franchising or distribution. Thanks to Committee members from around the world, we're able to include articles highlighting legal issues in Argentina, Israel, Saudi Arabia, the Dominican Republic and the US.

Future issues of the Newsletter will focus on specific topics of interest to our members:

Fall 2013 (September): *Franchising & Distribution*
Winter 2014 (January): *Focus on the CISG*
Spring 2014 (April): *Commercial Transactions*

We hope this issue provides valuable legal insight and practice tips, but we also hope that it generates excitement around participation in future editions. Special thanks to our contributors for this re-launch. We welcome your suggestions, your ideas and, above all, your participation so that, together, we can make these newsletters a vibrant forum for addressing important topics and showcasing the expertise of our members.

Michael Daigle, Guest Editor

In This Issue

COMMITTEE NEWS

Greetings:

The Committee has been active in the first half of 2013 and, with the re-launch of the quarterly Newsletter and participation in upcoming programs, the second half of the year promises to present many opportunities for members to actively engage in the Committee's activities.

Recap of Activities to Date

In April, we sponsored or co-sponsored 3 programs at the Section's Spring Meeting in Washington, DC.

Committee Co-Chair, Michael Daigle, was the guest writer for the May newsletter of the Distribution Commission of the AIJA. The inclusion of Michael's piece ("*Franchising in America – Tips for Representing Franchisors Entering the US Market*") in that newsletter was the first in what hopefully will be many co-operative activities between AIJA's Distribution Commission and our Committee.

At the Quebec Bar Association's Annual Congress held in Montreal from May 30-June 1, our Committee cooperated with the QBA to present six hours of programming. Patrick Goudreau, one of our Vice Chairs, assembled panelists from the Committee who presented four programs - two on the CISG and two on franchising. Thanks to Patrick and all of the panelists who delivered these well-received programs.

Upcoming Activities

- **2013 Fall Meeting** in London – We will sponsor or co-sponsor at least 4 of the programs at this meeting (October 15-19).
- **2014 Spring Meeting** in New York City - Program ideas are being solicited now for this meeting. The method for submitting programs has changed. Each Committee is being asked to propose up to five programs for consideration. Rather than submitting programs individually through the online form, programs must be submitted through the Committee. Please submit program ideas to one of your Committee Co-Chairs. Decisions on which programs will be submitted by the Committee must be made by July 31, so please submit your ideas as soon as possible.
- **2013 Leadership Retreat** – The Section's Leadership Retreat will be held August 7-9 in Sausalito, California. This meeting is open to all Section leaders as well as persons interested in assuming leadership roles in the Section. For meeting and registration information, visit: http://www.americanbar.org/content/dam/aba/uncategorized/international_law/aba_leadershipretreat_2013.authcheckdam.pdf
- **Committee Leadership Roles** – We continue to look for volunteers to serve in leadership roles on our Committee. Currently, openings are available for Programs, Projects, Membership and Communications & Website. If interested in assisting in these or any other areas, please contact one of the Committee Co-Chairs.
- **Year in Review** – Please watch for the call for submissions for the Committee's contribution to the Year in Review edition of the Section's International Lawyer publication. Our Committee has had strong contributions in the past, and we hope to continue being a significant contributor to this important publication.
- **Fall Newsletter** – The Fall edition of the Committee's quarterly Newsletter will be published in early September with a focus on international franchising and distribution. The deadline for submission of articles will be August 15. More information to follow.

Our combined mission is to make this Committee one of the most active, providing the highest quality materials, and delivering the most value to its members. We hope you'll help us get there and that you'll join us in these and other activities that will be made available through the Section and this Committee.

Caryl Ben Basat
William Johnson
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TERMINATING AN AGENCY AGREEMENT WITH AN ISRAELI SALES AGENT: WHEN THE CONTRACT MAY NOT COME FIRST

By Jeremy Benjamin and Shirley Dloomy

In any commercial agency relationship involving an Israeli party, the primary source of the parties' rights and obligations is their written agreement. But if the agency contract is for an indefinite period of time, the parties' right to determine the prior notice period required for terminating the agency contract has just been curbed. Sales agency agreements involving an Israeli Agent are now subject to The Agency Contract Law (Commercial Agent and Principal), 5772-2012 (the "**Law**"), whose main impact is to give Agents more extensive rights than they would otherwise enjoy upon termination of the relationship.

If your client is considering entering into a sales agency agreement or, alternatively, is contemplating terminating such an existing agreement, your client needs to be aware of the following developments and seek legal advice before making any related decisions.

Background

In Israel, as in most legal jurisdictions, controversies over termination of sales agency contracts (as well as distribution agreements) and compensation for termination are hardly unusual. Traditionally, such disputes in Israel were governed by general contract law principles and extensive case law, with Israeli courts establishing over the years various criteria to assess the specific circumstances of each case before them. For better or worse, the courts had the last word, often leaving the parties "guessing in the dark" what constitutes sound prior notice and reasonable termination pay in lieu thereof. But that's no longer the case.

Prompted by the growing view that the Principal-Sales Agent relationship is distinct from other commercial arrangements, and that the Agent is often the "weaker" party and usually enjoys few rights vis-à-vis the Principal, the Israeli parliament passed the Law in early 2012. Inspired by the EU Directive on the subject,[1] the Law entered into effect on April 27, 2012 and seeks to provide the parties greater protection (though mainly to the Agent), clarity and legal certainty. But does it actually provide greater clarity and certainty?

Highlights of the Law

According to the Law, the prior notice period that each party is required to provide before terminating a sales agency agreement of undefined term may not be less than:

- 2 weeks during the first six months of the agency agreement, with the prior notice period increasing incrementally the longer the contract has been in effect, culminating in a maximum of:
- 6 months during the sixth and subsequent years of the agency agreement.

If the parties decide on a longer prior notice period than the period stipulated in the Law, the prior notice required from the Principal may not be shorter than the prior notice required from the Agent to terminate the contract.

The Law further provides that in the event one of the parties terminates the contract, the Principal may demand that the Agent immediately cease acting on the Principal's behalf, provided the Agent is compensated for such immediate termination of its engagement (referred to as "Prior Notice Pay"), based on the Agent's previous average monthly profit and as set forth in the Law. While the Law affords the courts discretion to modify the Prior Notice Pay under special circumstances related to changes in the general market or the market sector in which the Agent worked, it surprisingly does not explicitly exempt the Principal from payment of such compensation when the Principal has terminated the agreement for cause without providing the aforesaid prior notice.

Upon termination of the agency contract by either party, the Agent is likewise entitled to compensation that reflects the Principal's transactions with new customers or any significant increase in the scope of the Principal's business with existing customers (referred to as "Market Share Compensation"), provided that:

1) The agency contract was in force for at least one year;
2) During the period of the contract, the Agent was instrumental in obtaining sales for the Principal with new customers or in increasing sales with existing customers;
3) The aforesaid transactions yield revenues to the Principal after the termination of the agency contract.

[1] European Union Council Directive 86/653/EEC of 18 December 1986 on the coordination of the laws of the Member States relating to self-employed commercial agents.

The Law affords the courts discretion to reduce the Market Share Compensation or deny any such compensation when they deem it appropriate. But unlike the Prior Notice Pay provision, which leaves the Principal's obligation for payment of compensation upon termination for cause unclear, the Law expressly exempts the Principal from paying the Market Share Compensation where the agency contract is terminated for cause due to the Agent's breach.

The provisions of the Law described above are not a default regime subject to the parties' right to opt out by contract; rather, they are mandatory and the Law explicitly states that it cannot be derogated from, except to the benefit of the Agent.

What the Law Leaves Unclear

For all its intended merits, the Law has its share of oversights as well.

For instance, the Law does not distinguish between an Agent that has been granted explicit contractual exclusivity, an Agent that has acted de facto as a sole agent, and an Agent who was clearly non-exclusive – a distinction made in case law that has impacted the courts' determinations of the rights of Agents to compensation upon termination of their agency agreements.

The Law also fails to address cross border relationships. Foremost in this regard is the question of whether the courts will use the anti-derogation provision in the Law as the basis to refuse to enforce choice of law clauses in agreements with foreign Principals that either stipulate the foreign law of the jurisdiction of the Principals or the foreign law of a "neutral" jurisdiction.

Equally unclear is whether the Law will apply to agency agreements in which an Israeli Agent is contracted to work abroad or, alternatively, a foreign Agent is contracted to work in Israel. Which will prevail – the Law, the terms of the agency contract regarding governing law, or the law of the foreign state in which the Israeli Agent is contracted to work or which serves as the domicile of the foreign Agent?

Likewise, the language of the Law implies, though not unequivocally, that the Market Share Compensation provision will also apply to termination of a fixed-term contract that was in effect for at least one year before being terminated prior to expiration of its fixed term.

As noted above, the Law is ambiguous about the Principal's obligation to compensate the Agent pursuant to the Prior Notice Pay provision when it has terminated the agreement, for cause, without providing prior notice.

Additionally, the wording of the Law and explanatory notes that accompanied its draft indicate that a distributor does not fall under the definition of "Commercial Agent" and hence it appears that the Law was not intended to provide statutory protection to distributors. One District Court case has recently held that the Law indeed does not apply to a distributorship relationship (C.C. (Tel Aviv) 1902/08 Danshar Ltd. v. Banketbakerij Merba B.V., et al.). Whether the courts will opt to afford distributors a similar or greater level of protection as Agents are granted under the Law, notwithstanding what may or may not be written in the relevant distribution agreement, remains to be seen.

But perhaps the most glaring omission of the Law is that it fails to denote whether it applies to existing contracts or only to contracts entered into after the Law came into effect. While the legislative comments suggest that only prospective contracts will be subject to the Law, Israeli courts may very well opt to apply the principles underlying the mandatory provisions set forth in the Law to disputes that arose after the Law entered into force regarding existing contracts. This fundamental issue alone will undoubtedly keep the judiciary busy in the near future.

Despite the uncertainty as to how some provisions of the Law will be interpreted by the courts and how they will integrate these provisions with the judicial criteria previously established, the Law needs to be taken into consideration when counseling your client about prospective or even existing sales agency agreements.

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PRACTICE TIPS FOR THE INTERNATIONAL PURCHASE & SALE OF BUSINESS AIRCRAFT

By Michelle Wade and Dillon L. Strohm

If your international commercial transaction involves a business aircraft, particularly where the buyer will register the aircraft in a different country than the one in which the seller had it registered, you have a lot of work in front of you. Cross-border aircraft transactions involve many hurdles that can be difficult to identify, and even harder to get over.

In order to establish a smooth transaction for your client, we recommend avoiding some common pitfalls, some of which include:

Original Documents – Wrong Place, Wrong Time.

Documents such as the certificate of airworthiness and certificate of registration must be on the aircraft anytime it is flown. Some aviation registries require original documents, such as the certificate of airworthiness and certificate of registration, be relinquished to that aircraft registry at closing in order for the registry to de-register the aircraft. The combination of these two requirements can affect the timing of flying the aircraft to the closing location and therefore these issues should be analyzed prior to finalizing and signing a purchase agreement. A buyer will also want to confirm that the aircraft description which will be on the de-registration notice provided by the aircraft registry in the seller's country of registration (Seller's Registry) exactly matches or is acceptable to the aircraft description to be utilized by the aircraft registry selected by the buyer (Buyer's Registry).

The Flip.

Beware of a seller buying the aircraft from someone only to instantly "flip" it to the buyer. This can initially be difficult to identify. A flip can create tax problems because your anticipated transfer tax exemption may no longer apply and now a jurisdiction might look to tax the transfer twice – double the title transfers, double the tax. A flip may also cause the Seller's Registry to issue a de-registration notice in the name of the seller and not to the buyer. If inconsistent documentation arrives at the Buyer's Registry it is likely that no registration will occur. If these issues are not identified and addressed in advance, you could be left with a grounded aircraft that is not registered anywhere, and worse, without a clear legal owner or insurable interest.

Trying To Run Solo.

International commercial transactions require a team approach. A tax advisor may recommend that the transaction close while the aircraft is in a location which is favorable for taxes; but, after consultation with your technical advisor or pilot, you discover such location has few available aircraft parking spots, no hangar space and no facility able to make any technical changes required to obtain a certificate of airworthiness from Buyer's Registry, making the location unacceptable for closing. Do you know how to perform a lien search in India? Local counsel can be crucial to a smooth transaction. Customs brokers, maintenance advisors, export/import specialists – all play critical roles and should be involved.

Last Minute Lending.

Lenders want a lot of documents signed by the buyer/borrower and they want all of the signatures in various locations in advance of closing. Due diligence requirements are extensive – especially for business aircraft transactions which may involve a buyer located in country 1, an aircraft to be registered by the buyer in country 2 (after it is de-registered from country 3), a lender based in country 4 and the aircraft to be in country 5 at the time of title transfer. If you have waited too long to obtain the loan documents for buyer's financing, a buyer may be forced to acquiesce to a lender's demands, however unreasonable they seem, because the buyer will have lost its bargaining power if it signed a purchase agreement that requires the buyer to close on the purchase by a certain date or be in default. Or you may have to pay cash.

Trying To Sprint Through a Marathon.

International commercial transactions take time, much more so than single-country transactions. Consider the difficulty you've had in setting a conference call between the New York and L.A. office to negotiate a contract. Now consider that same difficulty with a twelve-hour time zone difference, and throw in language and cultural differences, customs issues, export controls, international treaties, advisors on three continents, two governmental transportation regulatory schemes, and avoiding ambush by holidays in multiple countries. Do yourself and your client a favor, and set a realistic pace if you want to finish the marathon instead of collapsing at mile five.

Tax Tunnel-Vision.

As U.S. based transaction attorneys, we focus on U.S. tax implications of a transaction, for obvious reasons. But unlike other assets, aircraft are mobile. Merely landing in another country can subject the aircraft to taxation. This may come in the form of value added tax (VAT), customs fees and duties, or other charges. Because VAT is not a familiar concept to many U.S. attorneys, we often do not understand the scope and extent to which VAT may apply to and impact a transaction. Local counsel can help determine whether any taxes may be due in various jurisdictions. Transfer taxes such as state and local sales and use tax also need to be reviewed if they could impact the transaction. The U.S. has 1031 tax-deferred exchanges which allow a taxpayer to defer paying tax on any gain when an aircraft is sold, and this tax deferral strategy is commonly used in aircraft transactions. Many other countries do not have any tax deferral options similar to a 1031 tax-deferred exchange so they will not understand why you need to assign the purchase agreement and why you need something called a "qualified intermediary".

The number of business aircraft involved in international commercial transactions is increasing, which is inherent with a mobile asset capable of globetrotting. A little bit of common sense, careful planning, and acknowledgment of the value of outside advisors can help you guide your client to a turbulence-free transaction.

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RECENT REQUIREMENT FOR REGISTERED COMMERCIAL AGENTS/DISTRIBUTORS IN SAUDI ARABIA

By Howard L. Stovall

For many years, Saudi Arabian government ministries and public sector entities have been required to purchase products only from local commercial agents and distributors who are properly registered under the Commercial Agency Regulations. In practice, that requirement was not always strictly observed, including by government-owned companies such as Saudi Aramco. More recently, Saudi Aramco appears to be taking steps to abide by that requirement to do business only with registered Saudi Arabian commercial agents and distributors. There are some significant implications for foreign companies who now seek to register their commercial agency/distributorship agreements.

Background

Saudi Arabian commercial agencies are governed by Royal Decree M/11 (1962) as amended (the "Commercial Agency Regulations"). The Commercial Agency Regulations apply both to commercial agency and distributorship arrangements. Therefore, in this article, use of the term "commercial agent" generally also includes "distributor".

The Commercial Agency Regulations contain a number of qualification requirements applicable to commercial agents. For example, the Commercial Agency Regulations state that only Saudi Arabian nationals or companies organized under Saudi Arabian law and wholly-owned and managed by Saudi Arabian nationals may act as local commercial agents. The Commercial Agency Regulations also require a commercial agent to submit its commercial agency agreement for registration at the Ministry of Commerce and Industry (the "Ministry"), within three months of the agreement's commencement date.

Registration Requirement

According to the Commercial Agency Regulations, the parties' agreement must be submitted to the Ministry in Arabic or, if drafted in a foreign language, then accompanied by an authorized Arabic translation. The commercial agent bears both the responsibility for registering the parties' agreement as well as the penalties for failing to register.

Given the scrutiny sometimes applied by the Ministry to commercial agency agreements during the registration process, some foreign companies have been unwilling to amend the terms and conditions of their own standard commercial agency agreement, even if this might prevent registration. (Another reason why Saudi commercial agency agreements are sometimes not registered: in cases where the commercial agency agreement is extremely technical or lengthy, the required Arabic translation can be very difficult and expensive.)

Because the Saudi Arabian Customs Department has not customarily required that imported goods be cleared by a registered commercial agent, commercial agents have generally been able to operate in Saudi Arabia without registering their agreements with the Ministry. Assuming the Saudi Arabian commercial agent is otherwise qualified to perform commercial agency in the Kingdom (e.g., Saudi nationality, commercial registration to do business, purposes which include commercial agency activities), Saudi Arabian government authorities have rarely (if ever) sought to prosecute a qualified commercial agent for failure to register its commercial agency agreement.

Moreover, registration is not a prerequisite to the validity and enforceability of a commercial agency agreement in Saudi Arabia. Saudi Arabian courts have recognized and enforced the terms of commercial agency agreements despite the lack of registration. (Unlike some other commercial agency laws in the Middle East, the Commercial Agency Regulations do not contain any provision stating that 'no claims shall be heard on unregistered agreements'.)

From the foreign manufacturer's perspective, the most serious disadvantage of such an unregistered arrangement might be the commercial agent's inability to sell products to some Saudi Arabian government ministries and public sector entities. Over thirty years ago, the Saudi Ministry of Finance issued a circular instructing government departments not to enter into any contracts for the procurement of foreign manufactured goods unless the local supplier showed a certificate of registration under the Commercial Agency Regulations. However, not all Saudi Arabian government and public sector purchasers strictly observed that circular. Moreover, in some instances, Saudi government purchasers – including Saudi Aramco – would be willing to accept a letter from the foreign manufacturer, simply confirming that the Saudi commercial agent was authorized to act on its behalf for a particular tender.

Thus, in many instances in the past, Saudi Arabian commercial agents have been able to successfully market foreign products to Saudi Arabian government ministries and entities without being registered under the Commercial Agency Regulations. However, that practice now appears to be changing – at least in procurement by Saudi Aramco.

Saudi Aramco's Recent Policy

Beginning at least one year ago, the Supplier Registration Unit of Saudi Aramco began sending notices to local businesses listed within Saudi Aramco's records as commercial agents for foreign suppliers. That notice stated in part:

> *Please be advised that as of the date of this letter, Saudi Aramco will only accept (new) and maintain (existing) agency linkages between local and foreign suppliers when a local supplier provides a certified copy of the valid Commercial Agency Registration Certificate issued by Ministry of Commerce and Industry (MOCI). Maintaining a valid Commercial Agency Certificate is mandatory to maintain the agency linkage in Saudi Aramco system.*

The notice from Saudi Aramco goes on to state that suppliers who fail to provide the necessary documentation will have their existing agency linkages removed from Saudi Aramco's records until such time as the necessary documents are received. The implication is that Saudi Aramco will no longer procure goods through a Saudi Arabian commercial agent if the latter cannot provide a certificate from the Ministry, reflecting registration of a commercial agency agreement for the relevant products.

Some Implications

The Saudi Ministry of Commerce developed a model Contract of Agency or Distributorship in the mid-1980s, a form which was more or less required for registration with the Ministry for a few years. Over the past two decades or more, however, the Ministry has been willing to register commercial agency agreements that vary significantly from that model contract – provided that at least certain provisions (e.g., compliance with Saudi Arabian Standards Organization specifications, and a commitment to provide spare parts) are included in the agreement submitted for registration.

In light of Saudi Aramco's recent insistence on dealing only with registered commercial agents, some local commercial agents have begun presenting the Ministry's model contract to their foreign suppliers, suggesting that the model contract is required for registration with the Ministry. In fact, registration does not require use of the Ministry's model contract.

For example, the Ministry's model contains contractual provisions granting a commercial agent the right to claim compensation upon the foreign principal's termination or non-renewal of the commercial agency agreement – although neither Saudi Arabian law nor Ministry policy requires such provisions. Saudi Arabian law would offer significantly less protections to a commercial agent in the event of termination or non-renewal absent such contractual provisions. Therefore, if a foreign manufacturer does decide to make some effort to register its commercial agency agreement in response to Saudi Aramco's request, these types of contractual provisions found in the Ministry's model contract should be avoided to the greatest extent possible.

One of the biggest potential 'down-sides' to registration of a commercial agency agreement with the Ministry might occur if the foreign manufacturer subsequently decides to terminate its relationship with the Saudi Arabian commercial agent. The Ministry has discretion to refuse registration of a replacement commercial agency until all disputes with the prior commercial agent are resolved. In this context, the Ministry established a special Committee for the Settlement of Commercial Agencies Disputes, and many terminated (or non-renewed) commercial agents have filed complaints before this special committee, effectively blocking the registration of replacement commercial agents for lengthy periods of time. We do not know what Saudi Aramco's position would be in such circumstances, for example, if it would insist on dealing only with the currently registered commercial agent. In the past, some replacement commercial agents have obtained temporary registrations from the Ministry, pending resolution of the prior commercial agent's dispute, if such temporary registration is in the public interest -- for example, if the principal's products are crucial to the Saudi Arabian market.

Given the Ministry's relatively recent policy permitting the registration of multiple non-exclusive agreements, a foreign manufacturer might consider developing a non-exclusive commercial agency for registration with the

Ministry. A registered non-exclusive commercial agent would presumably have some difficulty subsequently blocking the registration of another non-exclusive commercial agent at a later time, e.g., in the event the foreign manufacturer decides to terminate the existing registered commercial agency.

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DOING BUSINESS IN SAUDI ARABIA: FINANCING INTERNATIONAL COMMERCIAL TRANSACTIONS

By Wassem M. Amin, Esq.

If a company is exporting goods to Saudi Arabia, the Middle East, or anywhere else for that matter, a key consideration is how to collect payment from the importer or buyer. A risk assessment of the underlying transaction and the buyer is necessary to determine what option to choose. For the exporter, on the risk spectrum, the least risky is to request that the importer pay up front prior to shipment. However, unless there is an established history between the parties involved, it is highly unlikely for the buyer to do so. On the other end of the spectrum is the option to sell on an open account - which involves simply shipping the goods to the foreign buyer along with an invoice. Again, this method of payment is ill-advised, because the U.S. company may end up not getting paid and, instead, quickly finding out how difficult it is to collect debts in foreign jurisdictions.

Use of Letters of Credit

An alternative to both these options is the use of a Letter of Credit ("LC"). Frequently used in international transactions, an LC is a document issued by a bank in which the bank agrees to pay money upon the presentation of specified documents. The transactional costs in obtaining LCs are miniscule compared to the risk of loss that comes with nonpayment. The most basic LC transactional structure is one where the buyer-importer opens an LC with an agreed-upon bank (the issuing bank) in favor of the seller-exporter (the beneficiary). The Letter of Credit is then transmitted to the seller's bank (usually, the advising bank) which releases the funds to the seller upon the seller's presentation of a bill of lading or any other agreed-upon documents. In the event the issuing bank's credit rating is low, a third bank, a confirming bank, can act as a surety for payment.

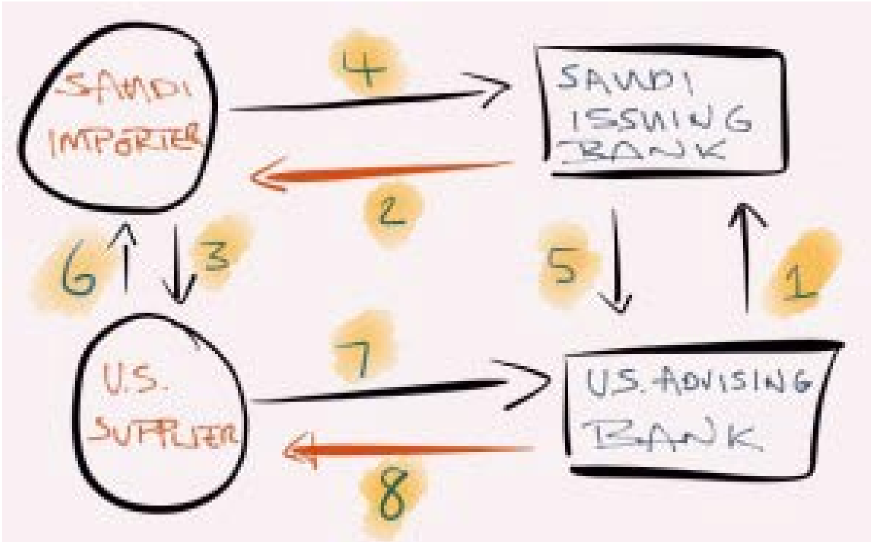
Terms for Letters of Credit are strictly defined in an internationally-agreed upon nomenclature. In addition, a uniform set of rules is used to govern the interpretation of terms as well as the rights and obligations of each party involved. Today, these payment instruments are used in complex financing transactions which may involve multiple banks, parties and stipulations. There are two main types of LCs: a standby LC and a performance LC. The standby LC is used to guarantee payment in the event of default or non-performance by a party; while a performance LC is used to guarantee payment for performance (usually the shipment or receipt of goods).

An Example

In some transactions, a combination of both types is used to ensure compliance by the buyer and the seller. Consider, for example, a transaction involving a U.S. manufacturer of custom-designed casework and a Saudi Arabian subcontractor who contracts for the supply and installation of laboratories in connection with the construction of a new hospital complex in the Kingdom's Eastern Province. The total value of the contract exceeds several million dollars. Due to the highly technical and specialized nature of these goods, the challenge is to design a financing mechanism that protected the interests of both the buyer and the seller. The U.S. manufacturer would be hesitant to begin fabrication and manufacturing without an advance payment. On the other hand, the Saudi subcontractor would not want to bear the risk of losing the down payment in the event of the manufacturer's default. In addition, there would still be the need to secure payment for the remainder of the project. A possible solution:

- First, to provide security for the down payment, the U.S. manufacturer would be asked to issue a standby letter of credit through its U.S. issuing bank to the subcontractor's bank in Saudi Arabia. The bank in Saudi Arabia would in turn issue a guarantee against default only for the advance payment amount. The standby letter of credit would be triggered in the event of the U.S. manufacturer's non-performance.
- Second, to ensure that the U.S. manufacturer would be paid, the subcontractor would issue a (performance) letter of credit for the remaining amount through a Saudi Arabian issuing bank to the manufacturer's bank in the United States. The terms of the LC would stipulate payment to the manufacturer against presentation of Bill of Lading documents, which allow staggered payment for each phase of the project. This structure allows minimal risk exposure for all parties involved.

The following sketch illustrates the steps that would be performed by each party, numbered in the order they would be performed.



1. U.S. supplier instructs its advising bank to issue a standby letter of credit to the importer's bank in Saudi Arabia;
2. Saudi bank, using the standby letter of credit of collateral, issues a bank guarantee to the importer for the advance payment;
3. Saudi importer wires the advance payment to the U.S. supplier's account;
4. Saudi importer instructs its bank to issue a performance letter of credit for the outstanding amount;
5. Saudi bank issues the letter of credit to the supplier's U.S. bank;
6. U.S. supplier ships goods to Saudi importer;
7. U.S. supplier presents bill of lading to its bank for payment against the letter of credit;
8. If documents presented conform to the letter of credit requirements, U.S. supplier's bank releases funds, pro-rata, according to the bill of lading.

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INCREASING ARGENTINE FOREIGN EXCHANGE CONTROLS AFFECTING TRADE, FINANCING AND TOURISM

By Carlos E. Alfaro

During 2012 the Central Bank of the Argentine Republic ("BCRA") began imposing exchange controls to protect the value of the Argentine currency and the foreign currency reserves of the BCRA. Those controls have been strengthened in 2013 both by the BCRA and the Federal Administration of Public Revenue (*Administración Federal de Ingresos Públicos*; hereinafter "AFIP") to prevent the fall of foreign exchange reserves. Access to the official exchange market, so-called Single Free Foreign Exchange Market (*Mercado Único y Libre de Cambios*; hereinafter "MULC"), in order to either make direct or portfolio investments abroad or keep foreign currency in Argentina for saving purposes is not permitted.

In addition, foreign exchange transactions have been generally subject to increasing *de facto* restrictions, preventing foreign exchange transactions that would otherwise be authorized pursuant to the regulations that are formally in force.

In light of the current foreign exchange formal and *de facto* restrictions, access to the MULC is limited to transactions comprising mainly as follows:

Travel and Tourism

Purchase of foreign currency to pay travel and tourism expenses is regulated through a Foreign Currency Transactions Consultation Program (*Programa de Consulta de Operaciones Cambiarias*; hereinafter "COC") which requires the validation of the amount of foreign currency the Argentine residents wish to purchase to pay "travel and tourism expenses". The COC keeps record of all the exchange transactions conducted for any reason.

Imports

Authorizations of import have been subject to discretional approval from governmental agencies. The process includes filing with the AFIP an Early Sworn Statement for Imports (*Declaración Jurada Anticipada de Importaciones*; hereinafter "DJAI"), under which governmental authorization is required to be able to pay for the import of goods. Import of services is subject to a similar restriction: in this case the party wishing to conduct an import must file with the AFIP an Early Sworn Statement for Services (*Declaración Jurada Anticipada de Servicios*; hereinafter "DJAS"), under which governmental authorization is required to pay for the import of services.

The filing of DJAIs and/or DJASs must be submitted to the AFIP before the issuance of any document used for executing an international sale transaction, and must include detailed information on the imported good (for example description of the good, tariff classification code, value, currency, quantity, condition, country of origin or country of shipment) or contracted service (for example date of the agreement, place of performance of the service, term of the agreement, data of the service provider, price of the services or payment conditions). If there is no written agreement, the information should be obtained from the invoice or equivalent document issued by the goods' or services' providers. The AFIP is entitled to request an electronic copy of the agreement or any other document it may consider relevant. Objections should be raised within 72 hours following the filing of the statement. This term can be extended up to 10 calendar days or even more since the Secretariat of Domestic Trade has been vested with a special term of 15 business days to object to authorization. If objections are raised, the importers can still appeal to the agency that has raised the objections.

As a matter of fact, in several cases the Secretariat of Domestic Trade has been raising objections without providing any explanation, and has required from the importer of goods or services additional information, such as price lists, business plans, and commitments from the company to balance the amount of its exports and imports. Those requests constitute more of a *de facto* requirement than a legal one, and are part of the government's so-called import substitution plan.

Once the relevant DJAI or DJAS is authorized, the approval is included in a special database that must be consulted by Argentine Customs before clearing customs and by the banks or financial institutions before selling foreign exchange currency to wire funds abroad in consideration of imports or services.

Financial Debts

Argentine borrowers that receive loans or any other financial indebtedness from foreign lenders are required to bring into Argentina the funds received and trade them in at the MULC for Argentine pesos within 30 days. Moreover, a financial loan with non-resident parties (including inter-company loans) should have a minimum tenor of 365 days as from the date the loan proceeds are transferred into Argentina. Finally, at the time the borrower transfers the proceeds of the loan into Argentina, unless for a few exceptional cases, a compulsory non-transferable US dollar-denominated deposit must ordinarily be made in an Argentine bank for at least 30% of the amount of such loan proceeds. This mandatory deposit will not earn interest, will have a minimum term of 365 days, and cannot be used as collateral for any transaction. Subject to compliance with certain regulatory requirements, the following transactions are exempt from constituting mandatory deposit before referred: (i) foreign loans to finance Argentine imports and exports (foreign trade financing); (ii) loans to the Argentine residents and local entities (excluding banks and other financial entities) with an average duration of at least two years (calculating principal and interests payments) to the extent funds are used exclusively for investments in non-financial assets; (iii) loans granted by multilateral and sovereign credit agencies; (iv) financing obtained to repay foreign financial debts, when the proceeds of the loan entering into Argentina are used simultaneously to repay such foreign debt; (v) financing obtained for investments in long-term foreign assets, when the proceeds of the loan entering into Argentina are used simultaneously for such investment; and (vi) financing obtained for initial public offering of debt securities in local stock markets.

In any case, prior governmental authorization is required for the acquisition of foreign currency at the MULC and wire transfer for the payment of principal and interest pertaining to cross-border financial debts.

Exports

Under the rules in force, Argentine exporters and service providers have the obligation to transfer to Argentina foreign currency proceeds of such transactions with non-Argentine residents, or funds disbursed abroad and to sell them in the MULC. Through these obligations, the government is trying to ensure the supply of foreign currency in the foreign exchange market.

The time-frame for selling at the MULC foreign currency obtained from the collection of exports of goods has lately been reduced, according to each tariff position. Except for a few very limited exceptions not reaching a certain threshold value, exports to related companies require that the amount of the export be sold at the MULC within 30 calendar days as from the transaction regardless of the tariff position. The funds collected from the export of services must be traded on the MULC within 15 business days counted as from the date of their collection in Argentina or abroad.

Also, according to recent regulations, oil, gas and mining exporters which had formerly received partial or total exceptions are obliged to repatriate all of their export proceeds.

Repatriation of Investments and Dividends

Even though according to the formal regulations non-Argentine residents are allowed to buy foreign currency in order to repatriate their investments or dividends from Argentine source subject to the prior compliance of a number of requirements, as of this date none of those transactions is feasible. Since the government is intending to curtail the demand of foreign currency and the fall of international reserves, as of lately, in general terms, no authorizations are being granted for repatriation of investments and dividends.

The exchange rate applicable within the MULC is the result of a free flotation of the supply and the demand of foreign currency with BCRA intervention by selling and purchasing foreign currency on its own account. As a result of the restrictions above mentioned a parallel currency market has developed that is tolerated by government, where the cost of purchasing US Dollars with Pesos is 90% per cent higher than the cost of a similar transaction at the MULC.

Likewise, to circumvent the current restrictions to transfer currency from Argentina to foreign countries a mechanism has been used by which the party intending to make a cross-border transfer, purchase in Argentina securities that are listed both in Argentina and abroad, and then, after a mandatory waiting period of not less than 3 business days, instruct the intervening stock-broker to have the *Caja de Valores* (Argentine Central Depository) transfer the securities to a foreign central depository, (Euroclear, DTC), to finally end-up selling the relevant securities abroad (the above complex transaction generally referred to in Argentina as "Contado con Liquidación"). A reverse transaction may be used to transfer foreign currency to Argentina, and thus avoid selling such foreign currency at the artificially low price applicable within the MULC.

Even though Contado con Liquidación transactions are generally held by experts as *prima facie* not forbidden, they have never been regarded with sympathy by the BCRA. However, as of this date, due to the coupled effect of certain technicalities of the Argentine Foreign Exchange Criminal Regime (as defined below) and the current scenario of Argentine politics, it is not prudent to make an assertion that Contado con Liquidación transactions will not be held in the future as an infringement to said legal framework.

The penalty system for the infringements to the Criminal Foreign Exchange Regime is set forth in Law No. 19,359 (as per Decree 480/95), as supplemented by regulations of the BCRA. Article 1° of Law No. 19,359, punishes with penalties the following actions:*"…a) Every exchange negotiation carried out without the intervention of an entity authorized to do such operations; "…b) Operate in exchange transactions without the corresponding authorization;...e) Every act or omission that infringe the regulations about the exchange regime…"*. Article 2°, sets forth the applicable penalties for the infringements established in Article 1°, by determining that they are punished with: *"…a) Fines of up to 10 times the amount of the operation, the first time; …b) Prison from one to four years in case of first recidivism or a fine of 3 to 10 times the amount of the operation under infringement;…c) Prison from one to eight years in case of second recidivism and the maximum of the fine fixed in the subparagraphs mentioned above; …d) through g) other penalties"*.

A further strengthening of the above restrictions should be expected in the short term. Pressure to devaluate is mounting. But the government is intending to maintain the *status quo* at least until the upcoming mid-term elections in next October.

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LEGAL FRAMEWORK OF AGENCY AGREEMENTS BETWEEN U.S. FIRMS AND DOMINICAN AGENTS

By Merielin Almonte

Once the Free Trade Agreement signed by the United States and other Central American Nations on 05 August 2004 and ratified by the Dominican National Congress via resolution number 357-05, dated 09 September 2005 (hereafter "DR-CAFTA" for Dominican Republic and Central America Free Trade Agreement, or "Treaty") came into effect, a new legal schema applies to agency contracts between Dominican licensees and United States licensors.

This new legal schema radically transforms the regulatory framework of the licensor-licensee relationship foreseen by Law No. 173 on Importer Agents of Merchandise and Products, dated 06 April 1966 and its modifications, which had governed said relationship until DR-CAFTA came into effect, on 01 March 2007, and b) Law No. 424-06 for the implementation of said treaty, promulgated on 20 November 2006, modified by Law No. 493-06 of 22 December 2006.

Purpose of Law 173

From its beginnings, Law 173 had the purpose of granting judicial security to the Dominican licensee *vis-à-vis* the possibility that once the image, marks, products and services of the foreign licensor were positioned in the local market, then it would decide to unilaterally terminate the contract and exploit the distribution of its products and services in national territory on its own or by means of third parties to the detriment of the Dominican licensee and ignoring their acquired rights.

This system of legal protection for the Dominican licensee was based fundamentally on: first, the obligation of the foreign licensor to indemnify the Dominican licensee, following the compensation formulas enshrined in article 3 of Law 173, applicable in the case of unilateral termination of the contract or refusal to renew it, in both cases without just cause; and secondly, the inapplicability of the clause that "conventionally" limited the period of the life of license contracts, assimilating them into "contracts for an indefinite period" (Art. 2 Law 173). Such mechanisms and other aspects of the Law in question were invested further with the nature of a public order provision (Art. 8 Law 173), which imposed on Dominican judges the obligation of applying Law 173, even if the Dominican licensee had waived their benefits in the contract.

With the implementation and entry into effect of DR-CAFTA, in the specific case of United States licensors, the public order nature of Law 173 has been overturned, converting it to a rule of partial and supplemental application, if the contracting parties (licensor-licensee) should so expressly agree in the contract.

DR-CAFTA utilizes the term "covered contracts" (hereafter "DR/USA agency contract") to refer to "a license contract … to which a provider of merchandise and services from the United States or any company controlled by said provider forms part."[1] According to the regulation, the general principle is that the Dominican Republic will not apply Law 173 to any DR/USA agency contract which has been signed after the date DR-CAFTA entered into effect, except for an express agreement by the contracting parties to abide by the schema of said law [2]. Even, in the event that Law 173 should apply by express decision of the contracting parties, the indemnification schema it contains which, along with its public order nature, constitutes the essence of same, will be excluded.

The overturning of the public order nature of Law 173 with respect to DR/USA agency contracts, is not based on a sole or specific provision of the new regulation, but rather is derived from the whole set of provisions making it up: a) DR-CAFTA, in Chapter 11 on Trans-Border Service Transactions, attachment 11.13 on Specific Commitments, section B: Dominican Republic, paragraphs 1-5, and b) Law 424-06 on the implementation of said treaty, in articles 67-71.

Effect of Treaty

In this new scenario, Law 173 is not yet applicable to DR/USA license contracts signed subsequent to the date of entry into effect of DR-CAFTA (March 01, 2007), except when the contracting parties expressly stipulate in the contract that they wish to submit to the schema of Law 173. According to the provisions of attachment 11.13 section B paragraph 1 items (a) – (g) of the Treaty, backed by article 68 and paragraph de Law 424-06, such contracts will be subject to the following provisions:

- The principles of the Civil Code of the Dominican Republic will be applicable. That is, they will be subject to the provisions of Title III of the Civil Code, entitled "On contracts and conventional obligations in general", which will have a supplemental nature to govern the aspects related to the interpretation, scope and nature of the obligations assumed by the parties, when they have not been explicitly defined in the contract.

- The contractual bond between licensor-licensee is treated as an ordinary contractual relationship, based on the principle of the will of the parties (Art. 1134 of the Civil Code). Its legal governance and, consequently, its treatment by the jurisdictional agencies, is shorn of the public order nature imposed by Law 173. This implies that the terms and conditions under which the parties should decide to establish their relationship are under their full liberty and discretion. If any conflict should arise, which must be resolved by a jurisdictional agency, the conventions agreed to in the agency contract prevail and are imposed upon said agencies, with the capacity of them to intervene in the contractual relationship of the parties being limited.

- The licensor and the licensee can freely agree to a term of specific effectiveness for their contractual relationship, upon the expiration of which they are at liberty to not renew the agency contract. When the term of expiration agreed to should be reached, either of them should refuse to renew the contract, the termination under these circumstances is considered to be based on just cause. Therefore, the party executing the unilateral termination in these circumstances (arrival of term) will not, in principle, compromise their civil liability solely by the act of termination or their refusal to renew the contract. Even in those cases in which the contract does not have a specific period of effectiveness, termination based on "just cause" is imputed when either of the parties should serve the other with a "termination notice" six months of advance notice. Obviously, this does not exclude the possibility of suing for judicial compensation against the party exercising the termination when there are causes for generating contractual civil liability, according to the general principles governing same.

- Although the new regulation of DR-CAFTA and Law 424-06 enshrine the possibility of the parties to be able to put an end to their contractual relationship, whether by stipulation of a specific term of effectiveness, or via an notice of termination served six months in advance, this "will not prevent the parties from demanding an indemnification, when it is in order, in the form, the manner and the amount agreed to in the contract." [3] From this provision of the Treaty it is inferred that the parties can agree in the contract to some formula for indemnity compensation (penalty clause) applicable in the event that the termination should produce a violation of that provided for in the contract. However, this has two limiting factors, namely "…a provider of merchandise or services is not required to pay damages and indemnities for terminating a contract due to just cause or for allowing for said contract to expire without renewal for a just cause." [4]

- In the event that the termination of a DR /USA agency contract signed subsequent to DR-CAFTA should occur, the following provisions will be applicable: "(i) if the contract contains a provision regarding an indemnification, including non-indemnification, this aspect of the contractual relationship will be governed by that which may have been agreed to in the agency contract; (ii) if the covered contract should not have said provision, any indemnification will be based on the real economic damages and not on a statutory compensation formula (as foreseen by article 3 of Law 173); (iii) the licensor will honor pending guarantees; and (iv) the licensor will compensate the distributor for the value of any inventory which the distributor cannot sell by reason of the termination or the decision to not renew the contract. The value of the inventory will include any customs duty, surcharge, transportation expenses, internal movement costs and the costs of for taking the carrying the inventory paid by the distributor." [5]

- The parties have the faculty of recurring to a procedure of binding arbitration to resolve the disputes that may arise between them. They further have the liberty of choosing, at their entire discretion, and to establish in the contract the mechanisms and forums they wish to turn to in the case of conflicts. This opens the possibility that the parties may attribute competence to foreign agencies to resolve disputes that may occur among them.

- Regarding the rights of exclusivity which the United States licensor may confer upon their Dominican licensee, the Treaty establishes that "it shall be interpreted that a contract establishes exclusivity of a distribution only to the degree in which the terms of the contract explicitly declare that the distributor has the rights of exclusivity to distribute a product or service."[6]

The provisions indicated above constitute the law currently applicable to agency contracts which are formalized by United States licensors and Dominican licensees. However, since they are not of a public order nature, the parties can renounce the benefit of same in the document sustaining the contractual relationship.

Notes:

[1] Paragraph 5 of section B of attachment 11.13 of DR-CAFTA
[2] Paragraph 1 of section B of attachment 11.13 of DR-CAFTA and Art. 68 Law 424-06
[3] Infine part of paragraph 1 of section B of attachment 11.13 of DR-CAFTA
[4] Paragraph 3 of section B of attachment 11.13 of DR-CAFTA
[5] Section B paragraph 1 literal e) of attachment11.13 of DR-CAFTA
[6] Ídem

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