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I. Introduction

In recent years, the use of countertrade transactions has increased dramatically. At first, this kind of trade was closely associated with East-West trade; however, it is now becoming more and more popular in North-South and East-South relations.[1] At the root of this recent surge in countertrade activities are shifts in international economic conditions. The rapid increase in the cost of key imports has left importing nations with significantly diminished supplies of hard currency. In addition, less developed countries, partly because of the worldwide recession and decreasing prices of primary commodities, have had to contend with declining exports and increasing protectionism in the markets to which they export.[2] These trends have often resulted in serious balance of payment deficiencies.

Increasingly, more countries in the world need their limited supply of foreign currency to service their international debts and to purchase essential imports. As a result, barter and countertrade arrangements between industrialized Western countries and less-developed and eastern-European countries are becoming more widespread.[3] Parties imposing countertrade requirements are usually

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1. Rajski, *Some Legal Aspects of International Compensation Trade* 35 INT'L & COMP. L.Q. 128, 129 (1986) [hereinafter Rajski]. *See also* Walsh, *Countertrade: Not Just for East-West Anymore*, 17 J. WORLD TRADE L. 3 (1983) [hereinafter Walsh]; Fontaine, *Aspects Juridiques des Contrats de Compensation*; 2 DROIT ET PRATIQUE DU COMMERCE INTERNATIONAL (DPCI) 179, 181 (1981) [hereinafter Fontaine].

2. International Monetary Fund, *1983 Annual Report on Exchange Arrangements and Exchange Restrictions* 44 at 5 (1983). After an export growth in the late seventies, export growth after 1980 was almost static or even declined. Zarin, *Countertrade and the Law*, 18 GEO. WASH. J. INT'L L. & ECON. 235-38 (1984) [hereinafter Zarin] *citing* Estimates of Business Trend Analysts Inc., *The World of Countertrade, and Analysis of the Current Environment and Prospects for Future Growth* 13, 31 (1983).

3. Welt, *Countertrade as a Competitive Tool*, MGMT. REV. 53, 54 (1986) [hereinafter Welt]; Zarin, *supra* note 2 at 238; Grabow, *Negotiating and Drafting Contracts in International Barter and Countertrade Transactions* 9 N.C.J. INT'L. L. & COM. REG. 255 (1984)

sovereign nations[4] purchasing products and technology in the international marketplace. Parties that encounter these requirements are generally private companies. Normally, such companies would prefer conventional forms of trade, but they accept the risk and the inconvenience of countertrade in order to complete the sale of their products to their buyers in the Third World or in eastern-European countries.[5] Countertrade, of course, means a major departure from conventional forms of commercial dealing. Countertrade violates many of the major principles of our free market system as a coercive, anticompetitive practice.[6] Whether countertrade in a specific case violates those principles laid down in the General Agreement on Tariffs and Trade (GATT) is a question that is not always simple to answer, for a potential problem exists. That question, however, extends beyond the scope of this article.[7]

Countertrade also raises a series of far-reaching legal issues regarding antitrust, import relief and unfair trade practices. These issues have received ample attention, especially in the American legal environment.[8] This article will limit itself to a short overview of the legal problems one can encounter upon entering into a countertrade and a counterpurchase agreement. This article first addresses the three main forms of countertrade and then considers the private law implications of countertrade and counterpurchase agreements.

II. Forms of Countertrade Arrangements

A. *Barter*

Pure barter[9] is probably the world's most ancient form of commerce. Barter is generally defined as a transaction that provides for a direct exchange of goods or services of equal value between two parties without any cash changing hands.[10] In pure barter transactions, the parties always trade directly with each other; consequently,

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[hereinafter Grabow].

4. *See* Welt, *supra* note 3, at 54 where he states that in 1986 there were more than 91 countries practicing some degree of countertrade among which more than 81 countries had actual pro-countertrade government policies. For a number of examples, *see* Walsh, *supra* note 1, at 6-8.

5. McVey, *Countertrade: Commercial Practices, Legal Issues and Policy Dilemmas*, 16 LAW POL'Y. INT'L. BUS. 1, 7 (1984) [hereinafter McVey].

6. *Id.* at 2-3; *see also infra* note 8.

7. For a full treatment of this issue *see* Zarin, *supra* note 2, at 241-47 and McVey, *supra* note 5, at 35-69.

8. *See* Zarin, *supra* note 2, at 241-83 and McVey, *supra* note 5, at 35-56.

9. Grabow, *supra* note 3, at 259. More complicated barter transactions exist: there can be three or more parties; the exchange can take place over a longer period of time; and currency can be utilized to offset variations in the values of bartered goods. McVey, *Countertrade and Barter: Alternative Trade Financing by Third World Nations*, 6 INT'L TRADE L.J. 197, 201 (1980-1981).

10. Grabow, *supra* note 3, at 259. *See also* Rajski, *supra* note 1, at 130.

each party to the transaction must desire what the other offers. Such pure barter contracts are rare in international trade.

B. Compensation Arrangements/Buy-Back

A compensation or buy back transactions may be described as a long-term arrangement which involves a party that is under an obligation to deliver equipment, licenses or know-how for the construction of an industrial installation, and is committed to rendering appropriate technical services. This party undertakes to buy, over a fixed period, products resulting from those installations, in total or in part payment.[11] Identification of the compensation goods is normally, if not always, well known in advance. Parties, therefore, can determine more precisely the quality and quantity of these goods, and may agree on the time limits for delivery. Prices also can be determined more easily. Since the risks to all parties are readily assessable, the elaborate contracts used in compensation arrangements do not encounter the same problems as the contracts used in the third main form of countertrade, namely counterpurchase.

C. Counterpurchase

Counterpurchase is the linkage of a sales transaction for the export of goods, technology, or services with reciprocal purchases of products from the purchaser's country. Counterpurchase transactions outnumber any other form of countertrade. They are particularly evident in East-West trade.[12] In an East-West counterpurchase agreement, the reciprocal purchase commitment of the Western company, stated in terms of a percentage of the original sale, is more often less than one hundred percent. The duration of the counterpurchase commitment is usually from one to three years.[13] Both parties generally pay cash for the services or products received. Payment is made in a so-called hard currency and usually by means of a letter of credit.

III. Establishing the Contract

A. Contract Negotiations

How the contract between the Western company and the Third World country is established is often important for the bargaining position. If the Third World country has initiated the negotiations, it will normally be more interested in the deal than when it is ap-

11. Rajski, *supra* note 1, at 133. *See also* Zarin, *supra* note 2, at 236 n.1.

12. Hobér, *Countertrade: Negotiating the Terms, Part 1*, INT'L FINANCIAL L. REV. 28 (Mar. 1987); *see also*, *Countertrade: Negotiating the Terms, Part 2*, INT'L FINANCIAL L. REV. 17 (Apr. 1987) [hereinafter Hobér].

13. Mishkin, *Countertrade and Barter: The Basic Legal Structure*, INT'L BUS. LAW. 11 (Jan. 1986) [hereinafter Mishkin].

proached by the Western exporter. This fact may be of importance for the contents of the subsequent counterpurchase contract. The terms and conditions of financing offered by the exporter are also very important. An attractive scheme that guarantees a low interest rate limits the incentive for the importer to negotiate a high counterpurchase requirement. In countries with a planned economy, the Western exporter should be aware that his direct partner in the negotiations (the manufacturer) is normally not the party who makes the final decision. Normally, it is the foreign trade office (FTO) of that country which has final approval of the deal.[14] Moreover, it is often the FTO which comes forward with the counterpurchase requirements.[15] Clearly, a Western company interested in exporting to a foreign country should look into that second party's past history of negotiations. The demand for a counterpurchase commitment should not come as an absolute surprise. The Western company should plan ahead to ensure that it possesses the distribution channels to market and sell the goods it receives as a (partial) quid pro quo for the goods or services it hopes to sell. The Western company should also carefully check whether there exist any valid, applicable import restrictions on the goods it wants to counterpurchase.

During the actual negotiations, the Western exporter must, if necessary, raise the issue of a possible counterpurchase requirement.[16] In any case, a Western company should defer any final price quote until agreement has been reached on all terms of the sale.

B. *Form of the Contract*

Normally, countertrade and counterpurchase contracts should consist of two separate purchase agreements with a third agreement, the protocol, linking the two together.[17] Separate contracts make it easier to obtain financing from a bank for the primary sale, and to receive export guarantees and/or export insurance. Separate agreements also make it possible to assign rights under each of the purchase contracts. An additional advantage is that, upon assignment of the contract, the conditions of the export contract will re-

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14. In countries with a planned economy, it is not the producer, but a government agency commonly referred to as a FTO, which has final approval. *See* Report Netherlands Ministry of Economic Affairs, *Report of the Study on Countertrade* 1, 83 (1984) [hereinafter Report Ministry of Economic Affairs]. For the use of FTO's *see also* Fontaine, *supra* note 1 at 184 *et seq.* For a definition of FTO's, see Grabow, *supra* note 3, at 257 n.9.

15. This is contrary to popular belief. This was established in the survey conducted which led to the Report Ministry of Economic Affairs *supra* note 14, at 84.

16. If the FTO does not raise the issue, the Western Exporter should do so, because the countertrade requirement "risk" should be calculated in the price quote. *See*, Report Ministry of Economic Affairs, *supra* note 14, at 83-84.

17. *See* Mishkin, *supra* note 13, at 8; McVey, *supra* note 9, at 206; Grabow, *supra* note 3, at 261.

main secret.[18] This three-part division of the contract makes applicable to the two purchase agreements the normal obligations, liabilities and rights of the purchaser and seller under the law. In some if not most countries, however, this would be true even if the countertrade agreements had to be considered a pure barter transaction.[19] The relation between the two sales/purchase contracts is then explicitly laid down in the protocol. If there is no protocol, or no explicit clause with regard to the relation of the contracts in the protocol, the relation is not clear and will be considered under the applicable law or in the light of good business practices.[20]

The DPCI working group[21] expressed the view that if the export agreement (primary agreement) is not executed (fulfilled), the import agreement (secondary agreement) need not be fulfilled. The working group also arrived at this same result for annulment or a breach of contract under the export agreement.[22] The reasoning of the working group is that the export contract constitutes the raison d'être for the import contract.

Generally, the Western company is only induced to enter into the secondary contract because it wants to export, and not because it really wants to receive goods in return for money. This is probably the reason why Fontaine describes the export contract as the "contrat principal" (primary contract) and the import contract as the "contre-achat" or the "contrat accessoire."[23] This reasoning is of dubious validity in light of the legal relation established in the agreements. One of the two contracts is not more important. One is really the condition precedent for the other; the secondary contract being the condition for entering into the primary contract, and performance under the primary contract the condition for performance

18. It is often advantageous to keep certain contract conditions secret, e.g., the price.

19. R.J.V.F. Bertrams, *Internationale Ruilhandel*, N.J.B. 1389, 1392 (1985) [hereinafter Bertrams]. Bertrams cites the Netherlands (1582 B.W.), Germany (Article 515 B.G.B.) and France (Article 1707 C.C.). England is an exception to the rule. Under the definition provided in Sale of Goods Act, § 61 (1977) barter is not a sale. *See* Ellington, *Compensation Contracts and Set-off in English Law* DPCI 225, 228 (1981), "English Courts seek to avoid the conclusion that a transaction is indeed barter and will often construe the facts as, say, reciprocal sales." *Id.* at 228.

20. *See* Fontaine, *supra* note 1, at 189-91 for a discussion of this subject with emphasis on French and German law. Fontaine comes to the conclusion that under French and German law there is a good case to support the view that if the primary agreement is not fulfilled, the secondary agreement does not have to be fulfilled. Under French law there is no case law in either direction. German case law after a decision of the Bundesgerichtshof of July 12, 1972 (as published in Wertpapiermitteilungen, 1972, 1351) points in the direction indicated by Fontaine. For a discussion on the potential problems under Netherlands law, *see* Bertrams, *supra* note 19, at 1393.

21. The Fontaine article, *supra* note 1, is the result of the research of a working group of attorneys, law professors and in-house counsels from civil and common law countries.

22. Fontaine, *supra* note 1, at 190.

23. *Id.* at 184, where Fontaine for the first time uses the word "contrat principal." In his summary of the Report in DPCI 161, 166 (1982) he mentions the "contrat de contre-achat" and the "contrat accessoire."

under the secondary contract. Each party has its own specific interest. All these problems can and should be avoided by inserting the link in the protocol or in the secondary agreement. The choice of law clause for the linkage can also be of crucial importance.

If it is desirable that the two agreements remain completely isolated and independent of each other,[24] the protocol should recite the independent nature of each agreement, and specify that the failure of performance by one party in one contract will not defeat the rights of the parties under the other agreement. As noted above, in a countertrade transaction, the secondary (import) agreement is often entered into by the Western company for the exclusive purpose of obtaining the first contract. Western countries in this position may wish to provide for a link of the contracts in the protocol, by expressly stating that the cancellation of the primary contract will result in cancellation of the import contract, or even classification of that contract as null and void. Such a clause contains some inherent vagueness, and can lead to undesired results if the first contract is partly fulfilled. It, therefore, seems advisable to insert the clause only if necessary, or to place it in the secondary contract. If the secondary agreement is dependent on the primary agreement, in the authors' view, both the entire protocol and the "whereas clause"[25] can be deleted.[26] If a contract drafter deems these general clauses necessary,[27] he must take care when including them, to avoid provisions that would cause the two contracts to merge into a single instrument.

C. *The Export-Contract as Primary Contract*

The export or primary contract is the standard agreement for the transnational sale of goods and services. If either the protocol or the secondary contract provides for a link, insofar as cancellation of the primary contract means cancellation of the secondary agreement, it is necessary for the Third World or eastern-European countries to pay special attention to the reasons for termination or cancellation of

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24. Taking into account the different legal systems, it seems wise to decide what will happen if the primary contract is not fulfilled, e.g., separate contracts make it easier to obtain financing from a bank for the primary sale, to receive export guarantees and to assign the rights under each of the contracts. *See supra* text accompanying notes 17-18.

25. In the "whereas" of "preambular" clauses of the contracts, parties often describe what happened during the negotiations. These introductory clauses (also called recitals) are placed before Article 1 of the contract. They tend to state things like: "because the FTO demanded a counterpurchase and we were willing to accept this, we entered into the contract." These clauses can easily make the two contracts conditional on each other, especially under a civil law regime.

26. The "whereas clause" could lead to confusion while the Protocol is normally used to provide a link between the two contracts. If this link is already laid down in one or both purchase contracts, the Protocol becomes superfluous.

27. *E.g.*, Because in the legal system that governs the contract such clauses are normal or even required, or because the contract parties for one reason or the other insist on such clauses.

the contract. In certain circumstances, it can be very attractive for the Western exporter to invoke the force majeure clause.[28] The Third World country should therefore always seek to limit the scope of the force majeure clause or its results.[29]

Since a shortage of hard currency is often the primary reason for the importer to negotiate a counterpurchase, the importer should secure payment of the counterpurchase goods. If the importer does not secure this payment, it will end up having spent its valuable hard currency without receiving it back under the secondary agreement. Payment can be effected by documented credits or stand-by letters of credit. Parties can also demand bank guarantees. Since it is often difficult for a Third World country to obtain a bank guarantee from a first class international bank, parties typically negotiate payment into an escrow account and link the counterpurchase ratio with the amount initially paid, increased by the accrued interest. On the basis of the security of the escrow account, the bank can then issue a bank guarantee. The guarantee will be phrased in such a way that it will be proportionally reduced as counterpurchases are made by the Western exporter when he presents the agreed documents to the bank.[30] The bank guarantee will often state that it expires on the last day of the time period specified for the performance under the counterpurchase contract.[31]

D. The Counterpurchase Contract, the Import Contract as Secondary Contract

The secondary contract is of utmost importance in countertrade agreements. This contract reflects the "involuntary" nature of the sales agreement. This contract often requires tougher negotiations and presents more difficult drafting problems.[32] It is important to keep in mind that the counterpurchase agreement merely constitutes an undertaking to purchase goods at some time in the future. The actual purchase of goods from the importer is often covered by a

28. Normally, it is the Third World country that is very eager to conclude the contract. The Western exporter often concludes the contract, because it is the only way to extend his market. If the Western exporter finds another buyer or discovers that he can not sell or market the counterpurchase goods, e.g., for logistic reasons or because of the price level, he may seek a way out of the contract.

29. *E.g.*, It should be stated on the face of the primary contract whether application of the force majeure clause dissolves or merely suspends the agreement.

30. For different ways to secure payment *see* Bertrams *supra*, note 19 at 1396; Hober (Apr. 1987), *supra* note 12, at 18. The Third World country can, in lieu of the securities mentioned in the text, also negotiate a penalty clause, secured by a bank guarantee. If the Western exporter does not fulfill its obligations, it forfeits a penalty which in theory, of course, can be for the same amount as the counterpurchase obligation of the Western Exporter. *See infra* § E8.

31. For a general discussion on penalty clauses, *see infra* § III E8.

32. The primary contract is a standard sales contract. In the secondary contract, the special countertrade clauses come into play.

fulfillment agreement, which again represents a standard international contract for the sale of goods. The main clauses of such a contract are discussed below.

E. Contractual Provisions

1. Cancellation Clause.—The cancellation clause is optional. When included, it usually states that cancellation of the primary agreement will lead to automatic termination of the secondary agreement. Usually, it is better to phrase the cancellation clause in such a way that the exporter (i.e. the Western Company) has the option to cancel.[33] Most Third World countries will fiercely oppose this clause because it means that they may be unable to receive a return of hard currency. As importer, the Third World countries typically prefer a clause that provides for renegotiation. If parties desire a complete independence of the contracts, they cannot use the cancellation clause. However, the same effect can be reached by a careful drafting of the choice of law clause since some legal systems will consider both contracts related, even if there is no formal link whatsoever.[34] Thus, even when the courts decide that no link has been created on the face of the contracts, the applicable law may create a relationship between them.

"From a practical point of view the most important relationship is that of set-off."[35] In set-off, "a party claiming failure of performance by the other party under one agreement may be entitled to withhold amounts due to the other party under a separate and unrelated agreement."[36] In order to minimize unpleasant surprises caused by set-off, the relevant provisions of the applicable law should be scrutinized in detail.

2. Time Period for Performance.—The counterpurchase agreement should specify the time limit in which the Western country is required to fulfill its obligation. The Third World or Eastern-Bloc country will try to limit the performance period because it wants its hard currency back as soon as possible. The Western company seeks as much time as possible before performance is due. The

33. For a Western Company, an automatic cancellation can be beneficial, but also detrimental. It is beneficial in most cases because the counterpurchase agreement was involuntary in the first place. However, it can be detrimental if the rights under the contract are assigned or when the Western Company has a genuine interest in the goods or products.

34. *See supra* text accompanying notes 17-27.

35. Hobér (Mar. 1987), *supra* note 12, at 30.

36. *Id. See also Black's Law Dictionary* 1230 (5th ed. 1979), *quoting Edmonds v. Stratton* 457 S.W.2d 228, 232 (Mo. Ct. App. 1970): "A counter-claim demand which defendant holds against plaintiff, arising out of a transaction extrinsic of plaintiff's cause of action. Remedy employed by defendant to discharge or reduce plaintiff's demand by an opposite one arising from a transaction, which is extrinsic to plaintiff's cause of action."

longer the period, the more time the exporter has to organize the marketing of the products or find a third party who buys all the goods at one time. Absent a clause negating the effect, a longer period will bring extra revenues out of interest.[37] In many cases, the Third World country will agree on a relatively long period because it can not produce sufficient counterpurchase goods in a short period of time. The length of the period is usually one to three years.[38]

3. *Range of Counterpurchase Products.*—The Western export company will want to choose from as wide a range of products as possible. The other party typically wants to limit the list of available products to products it can not sell directly on the market.[39] If the importer in the primary country is a specific government agency, it will try to include on the list of counterpurchase products the products it manufactures or grows itself.[40] In such cases, a Western exporter should always try to negotiate a linkage with other government agencies. And, the Western company should try to obtain as extensive a list of products as possible. The Western company can thereby prevent the situation in which it later discovers that the products on the list are no longer produced, a true hazard in countries with a planned economy. Permission to establish linkage is often hard to obtain. Therefore, to entice the importing country's authorities into agreeing to linkage, linkage fees are sometimes used.[41]

4. *Quantity of the Countertrade Products.*—The quantity of countertrade products is normally expressed in a so-called compensation ratio.[42] This ratio gives the percentage of the value of the Western company's sale that is the subject of countertrade. This percentage is sometimes 100% or close to 100%, but is more often between 10 and 30 percent.[43] For developing countries, this ratio is often low, because the export contract is for goods or services recognized and

37. In the meantime, the Western exporters can accrue interest on the purchase price received from the Third World importer. *See infra*, text accompanying notes 28-31 and Mishkin, *supra* note 13, at 11.

38. *See* Grabow, *supra* note 3, at 265; *see also* Mishkin, *supra* note 13, at 11; McVey, *supra* note 9, at 202 n.18.

39. *See* Report Ministry of Economic Affairs *supra* note 14, at 73, where it is stated that the list of counterpurchase goods published by the Indonesian government at that time (1984) contained 33 products, but excluded oil. *See also* Grabow, *supra* note 3, at 263.

40. *See* Grabow, *supra* note 3, at 263. FTO's are generally granted exclusive authority to handle both import and export transactions for a specified area of products. *Id.* at 258 n.9. In such circumstances, it is obvious that the FTO for heavy industries will pay for a large machine with products generated by such machine or with products produced by the branch members.

41. *See* Hobér (Mar. 1987), *supra* note 12, at 31.

42. *See* Grabow, *supra* note 3, at 262 and Rajski, *supra* note 1, at 133.

43. *See* Report Ministry of Economic Affairs, *supra* note 14, at 59, where it is stated that the study based on returned questionnaires revealed an average counterpurchase ratio of 25% for East-West trade. *See also*, Grabow, *supra* note 3, at 262.

financed by the exporter's government as a development aid project.[44] A so-called soft loan usually pays for about 80 percent of the necessary goods or services.[45] The willingness to negotiate a percentage differs from country to country. If the goods to be purchased are of an essential nature or highly advanced and hard to obtain on the market, the compensation ratio decreases and can even approach zero. Some countries, by statute, require a counterpurchase of 100%.[46]

5. *Price.*—Like any sales contract, the counterpurchase contract will state the price of the goods. Commonly, the goods must be purchased over a period of one or more years. Normally, the products to be purchased by the Western company are not specified in the contract. However, the contract does often contain a pricing formula. The pricing formula will usually refer to the normal market price of the goods at the time of purchase.[47]

A Western company should seek a most-favored customer clause. This clause shields the company from loss in the event that, over the life of the contract, its own market should be flooded by lower priced products from the same country. The Western exporter who succeeds in bargaining for a long time period must protect himself from such fluctuations in the market. It is often wise to insert a clause which provides for periodical adjustment of the price.

6. *Quality of the Goods.*—The counterpurchase goods are often of an inferior quality, and consequently low in demand. The importer will try to sell to the Western company goods it will not normally be able to sell on the market.[48] To protect the purchaser, the contract should set forth detailed specifications for acceptable

44. *E.g.*, Gabon needs a new road to connect the airport to the city. The French government is willing to pay for 80% of the cost of the total project as long as French contractors will receive the contract. The French contractors then only have to receive 20% of the actual price from the Gabon government. An imposed counterpurchase duty is then easier to bear. The profit on the project possibly exceeds 20% and very probably the sale of the counterpurchase goods will bring in at least some money.

45. This is an international bank term, also used by the International Monetary Fund and the World Bank. A soft-loan is a loan on conditions more lenient than one would be able to acquire in the market.

46. In Indonesia, government investments exceeding the amount of USD 1 million require a compensation of 100%. *See* Grabow, *supra* note 3, at 262 n.21. Grabow mentions USD 750,000, but this amount, because of the exchange rate, is now closer to USD 1,000,000. Iran and China have requirements which in some cases and for some products comes close to 100%. *See* Report Ministry of Economic Affairs, *supra* note 14, at 77 (Iran) and 80 (China).

47. Terms refer to "the acceptable international price at time of purchase" or "10% below the fair market value of the goods in the first party's home country." *See* McVey, *supra* note 9, at 209, 210; Fontaine, *supra* note 1, at 195; and Hobér (Mar. 1987), *supra* note 12, at 31.

48. *See supra* note 39. Japan buys close to 100% of Indonesia's oil. *See* Report Ministry of Economic Affairs, *supra* note 14, at 72; McVey, *supra* note 5, at 10 n.23, *citing* Indonesian Guidelines. *See also* Grabow, *supra* note 3, at 263.

goods, or should at least state that the products have export quality.

In all counterpurchase contracts, the Western country should bargain for the right to appoint an independent surveyor to check the goods before shipment. This right helps to avoid serious problems that may arise if the Western country is sued for breach of contract or product liability for defects in the counterpurchase products it sells.

7. *Delivery.*—The Western company often deals with governments or government agencies who more or less control the availability of the counterpurchase products. The contract should contain a specific date of delivery or, in the case of periodic purchases, a specified time in which delivery should be made. Non-fulfillment on the delivery date, should explicitly be stipulated as a material breach of contract and should entitle the Western company to opt for termination of the contract.[49]

8. *Penalty clause.*—Due to the "involuntary" nature of the counterpurchase requirement, the Western company should seek the enactment of a penalty clause in the secondary agreement. This clause is intended to limit the potential liability for breach of contract. In the event the Western company is no longer interested in fulfilling, or can not fulfill its obligations, such a provision will enable the company to calculate its risk. If the penalty negotiated is not excessive, the penalty provision can serve as an escape clause.[50] The penalty may be lower than either the discount the Western country will have to grant the distributor of the goods, or the charge for administrative costs and the exporter's selling costs. If, for example, the counterpurchase ratio is 30% of the export transaction and the penalty is 10%, the costs would only amount to 3%.[51] Payment of the penalty then extinguishes any further obligations of the Western company. Of course, by invoking such a clause, the Western company risks its chances of establishing a long-lasting relation with the

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49. *See supra* text accompanying note 28. *See also* Grabow, *supra* note 3, at 267-68 where he states that frequent and often substantial delay in delivery is one of the greatest difficulties Western companies encounter when entering into countertrade transactions. Late delivery under most legal systems will constitute a material breach of contract. The question can, however, arise regardless of whether every late delivery is a material breach. The question "when" can be important in order to be relieved under a bank guarantee or to receive back monies in an escrow account. *See supra* text accompanying notes 30 and 31.

50. *See* Report Netherlands Ministry of Economic Affairs, *supra* note 14, at 89, where it is stated that the average penalty in contracts with eastern-European countries is between 10 and 15%. *See also* Grabow, *supra* note 3, at 268, who mentions 10-20% as the average penalty.

51. This does happen. A penalty of 10% may make it easier to sell the products available for counterpurchase to another Western exporter for an attractive price. One should not forget, however, that most countries that impose counterpurchase requirements have a hard time in producing the products. *See also* Report Ministry of Economic Affairs, *supra* note 14, at 89.

import country. Undoubtedly, any future contract between these two signatories will specify a penalty clause containing a much higher percentage. Often the importer insists on a penalty clause secured by a bank guarantee.[52] The clause should state that the penalty is to be considered as payment of liquidated damages,[53] and that the right to claim actual damages is waived by the importer. This penalty clause can benefit both parties.[54]

9. *Marketing restrictions.*—The contract should entitle the Western company to market and sell the counterpurchase goods free of any restrictions. The Western company may even negotiate an exclusive distributorship in certain markets. On the other hand, the Third World country will want to limit the marketability of the goods in order to increase the possibility of concluding countertrade deals with exporters from other countries.

10. *Assignment.*—The Western company will try to negotiate the transferability of countertrade obligations. Most Third World countries will not allow assignment (i.e. substitution of the debtor) without sufficient security that the assignee will meet the obligations of the exporter.[55] Here the bank guarantee can again play an important role. Assignment for the Western company is important, for it enables the company to transfer its counterpurchase obligation to a trade house or barter business club. Upon assignment, the Western company will be released from its counterpurchase obligation, and the assignee, normally a trading house, becomes a party to the counterpurchase agreement.

11. *Force majeure.*—A clause should be included which provides that the seller shall not be held responsible for the delay or nondelivery of the goods due to force majeure. The force majeure doctrine is different in every legal system. There are notable differences between the impossibility doctrine under American or English law (common law countries in general) and the risk attribution the-

52. A bank guarantee provides better security than an unsecured claim, which still has to be recognized in a court of law. For a practical example, *see* Hobér (Apr. 1987), *supra* note 12, at 18.

53. *See* Grabow, *supra* note 3, at 268 n.29. This seems true for common law jurisdictions, but not for civil law jurisdictions. *See* also Fontaine, *supra* note 1 at 198-99 and P. Benjamin, *Penalties, Liquidated Damages and Penal Clauses in Commercial Contracts: A Comparative Study of English and Continental Law*, INT'L. & COMP. L.Q. 600 (1960).

54. *See* Fontaine, *supra* note 1, at 198, where he states (translated from French by the authors): "The experience of the Group is that certain Western exporters never have any intention to actually fulfill their counterpurchase obligation, but in lieu thereof from the beginning have the intention to pay the penalty." *Id.* at 198 n.34. The Group found that there are also FTO's that make it as hard as possible for the Western company to fulfill its obligations in the hope that the Western company will terminate the contract by paying the penalty.

55. Who is both the assignor and original purchaser.

ory in civil law countries.[56] What is considered an act of God may also differ from country to country. Therefore, a very detailed force majeure clause is recommended. Furthermore, the clause should specify under what conditions the contract is suspended, and in what circumstances it can be terminated, and by whom. The clause must also assign the risks of subsequent government measures.

12. Dispute settlement.—Both the primary and the secondary contracts should identify the preferred forum for dispute settlement and the chosen law applicable to the contract. If the parties have failed to state a method of dispute resolution, the court of the defendant will normally obtain jurisdiction.[57] Normally, however, parties do provide for arbitration.[58] The possibilities of arbitration are widely known. In East-West countertrade, arbitration in Stockholm and Vienna under the UNCITRAL rules is popular.[59] In other countertrade transactions, arbitration by the ICC in Paris, or elsewhere under the ICC-rules, is often preferred.[60] In attempting to resolve those difficulties that might compromise the continuous performance of a contract, the parties should first state in specific and detailed fashion the circumstances in which the contract may be adapted.[61] They may then insert an ICC regulatory clause in the contract providing for intervention by a third person. Finally, the parties should define precisely the scope of the intervention by a

56. It is very hard indeed to chart the different definitions of force majeure and even more difficult to point out when they will lead to a different result. In the German Civil Code, it is stated that "[t]he debtor is relieved from his obligation to perform if the performance becomes impossible because of a circumstance, for which he is not responsible, occurring after the creation of the obligation." Burgerliches Gesetzbuch [BGB] art. 275 (W. Ger.). The comparable provision in the Dutch Code is much shorter. Burgerlijk Wetboek [BW] art. 1281 (Neth.). However, case law interprets the Dutch provision much like the German one; French law is also very similar. *Cf.* J. BENJAMIN, SALES OF GOODS 316 (2d ed. 1981) (summary of French law).

57. Some countries like the Netherlands, however, also know a so-called forum actoris. The Forum Actoris provides that, absent a clause to the contrary, the forum of the Netherlands' plaintiff is competent. *See* Article 126(1) B.W.

58. Very rarely are disputes solved in court or by arbitration. Most often, parties negotiate a commercial solution. *See* Report Ministry of Economic Affairs, *supra* note 14, at 89.

59. All eastern-European countries are a party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, 330 U.N.T.S. 38 (1959), and will therefore recognize a foreign arbitration award.

60. Designation of the institution as "the ICC" should be sufficient since there exists only one International Chamber of Commerce in the world. Parties often add "in Paris." By doing so they avoid possible confusions with other arbitration bodies, but they also induce the ICC Court of Arbitration to consider it to be their will that Paris be the place of arbitration. It is preferable that the parties, after clearly identifying the Institution to which they will refer their disputes, state in writing any agreement they may have reached on the place of arbitration. Absent an agreement, parties may wish to insert "the place of arbitration shall be fixed by the ICC Court of Arbitration." See ICC Publication No. 382, *Guide to Arbitration*, at 30 (1983).

61. The adaptation could arise from the lack of precision in the contractual provisions, or from the existence of gaps.

third person, by adopting one of the ICC standard clauses.[62]

The ICC also offers a service for parties who believe that a conciliation attempt by a neutral third person may be useful. Conciliation under the ICC-Rules for Optional Conciliation is, as indicated in the name, optional; it occurs only when the parties agree to it.[63] Arbitration remains optional, even if provisions for conciliation have been made through a clause inserted in the contract.[64]

The choice of applicable law is another important issue. Under private international law,[65] it is recognized that a contract is governed by the law of the most characteristic obligation.[66] For example, in sales contracts, the law of the most characteristic obligation is the law of the seller. This rule appears in all international conventions on international sales of goods and in the EEC[67] Execution Treaty (EEX). If no choice of law is made, the law of the seller will normally govern the contract. In the view of the DFCI working group, this means that the law of the seller in the primary contract (the Western country) governs both the primary *and* the secondary contract; this second contract is only an accessory of the primary contract.[68] The normal choice of law in countertrade agreements is the law of the seller.[69] This means that the primary and secondary

62. The two standard ICC clauses are:

> *Clause A*: In the event that the parties are unable to agree to apply all or any of the provisions of article(s) . . . of this contract, they shall apply to the Standing Committee for the Regulation of Contractual Relations of the ICC in order that a third person (or board of three persons) who shall be appointed in accordance with the Rules on the Regulation of Contractual Relations of the ICC, and who shall carry out his mission in accordance with the said Rules, may issue a recommendation.
>
> or
>
> *Clause B*: In the event . . . and who shall carry out his mission in accordance with the said Rules may on their behalf make a final decision which shall be binding on the parties and shall be deemed to be incorporated in the contract.

See ICC Publication No. 382 *supra* note 60, at 13.

63. The Conciliation Rules are part of the ICC Rules of Conciliation and Arbitration (1975), published as *Rules for the ICC Court of Arbitration* (1975), I.C.C. Publication No. 291.

64. *See* Article 5 Conciliation Rules: "Should a settlement not result, the parties shall be at liberty to refer their dispute to arbitration or to bring an action at law should they so desire, unless they are bound by an arbitration clause.

65. Often termed conflict of laws.

66. *See, e.g.*, Article 4, para. 2 EEC Convention on the Law Applicable to Contractual Obligations, Rome, June 19, 1980.

67. Convention on the Law Applicable to Contracts for the International Sale of Goods, Dec. 22, 1986, The Hague, art. 8, para. 1. The Convention derives its official date from the date it was signed by the first party, Czechoslovakia. The Convention is designated as the conflict of laws complement of the Vienna Convention of April 11, 1980 on the International Sale of Goods (Trb. 1986, 61).

68. Fontaine, *supra* note 1, at 203: "On devra donç se référer aux principes généráux du droit international privé. Dans la mesure où l'on reconnâit l'existence d'un lien avec le contrat principal, on pourra sans doute se référer à la clause de droit applicable de ce contrat."

69. As was stated, the seller performs the most characteristic obligation in a sales contract. Contrary to the DPCI Working Group, most authors and most contract drafters will consider and/or draft the primary and secondary contracts as two individual sales contracts.

contract are governed by different laws. To avoid this conflict, parties often agree on the law of the site of arbitration.[70]

IV. Conclusion

Countertrade arrangements are a factor of growing importance in international economic intercourse. They comprise a wide variety of contractual relations that range from traditional barter to very elaborate long-lasting contracts. Given the existing structure of the world's economic and financial condition and the division between rich and poor countries, countertrade and barter transactions are here to stay.

Consequently, obligation will lead to the applicability of a different legal system in each sales contract.

70. The authors, as practitioners, have found that if parties cannot agree on a choice of law, they will try to agree on a forum and a place of arbitration. Then, because of the availability of arbitrators, they are tempted to opt for application of the local law of the arbitrator(s). Since the arbitration site is normally located in a neutral country with a well-developed legal system, parties in practice will take the chance and accept applicability of English, French or Swiss law, often without knowing the contents of those legal systems.