

# The little guide to International Contracts

## *The right questions to consider before signing a contract or exporting*

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## The importance of contracts in international transactions

All too often, companies, and especially small or medium-sized businesses, find themselves defenceless when a legal action is brought against them by a trading partner based in another country.

There are many reasons for this:

1. The absence of a contract continues to be a regrettably common state of affairs. Companies, believing themselves to be protected by a long-term commercial relationship based on mutual trust, make no provision for a written statement of each party's obligations.
2. The contract may be incomplete or imprecise; in other words, one or more essential clauses relating to matters such as payment deadlines and methods, the applicable law or the court of jurisdiction may have been omitted. There may also be difficulties because the company does not have a command of the language in which the contract is written.

Whether there is no contract or an incomplete contract, the consequences can be very serious, possibly even compromising commercial relations between the parties as well as having significant financial consequences.

Quite apart from any legal burden generally associated with them, contracts are essential means of guaranteeing compliance with obligations and ensuring acceptance of them by both parties.

The drafting of contracts is also an integral element of business strategies, because the clauses inserted into a contract impose defined obligations on a trading partner on which the latter cannot renege.

Differences in approach between national legal systems must not be overlooked either. In essence there are two major historically rooted categories of legal system, each of which has given rise to different customs and ways of thinking. There is the type of system based on Roman law, which largely prevails in the countries of continental Europe, and the systems based on the English common-law tradition that exist in Britain, the United States of America and the 56 or so former British colonies that make up the Commonwealth.

There are also countries where the legal regime is based on ideas that do not correspond to our Western understanding, such as the law of societies governed by religious principles, particularly Muslim and Hindu societies, or systems influenced by ancient traditions and customs, as in China and Japan.

Before entering into a contractual relationship, it is therefore essential to have a general knowledge of the economic and cultural environment in which the other party operates and of business practices in the partner's country in order to succeed in international business (part I).

This guide then deals with the clauses that must be included when an international contract is drafted (part II).

The third part of the guide provides details of the main types of contracts used by small and medium-sized enterprises for their international transactions, namely international sales, distribution and agency contracts (part III).

## I. General framework for international contracts

### 1. Language used

Contracts must be drawn up in a language that both parties understand. English is the business language *par excellence*, and its use should be the preferred option.

### 2. Business practices

Familiarity with business practices means knowing how to speak a trading partner's business language.

**Knowledge of the rules and customs of trade in your partner's country** is essential for the proper conduct of negotiations and for the application of the contract.

**The Enterprise Europe Network can help you to identify more clearly the cultural differences that exist within Europe.**

A user's guide in French, entitled *Préparer ses rendez-vous d'affaires en Europe*, for those preparing for business meetings with partners from other European countries has been produced by the Centre Region office of Enterprise Europe and is available at:

<http://www.centre.cci.fr/mediatheque/EuropActu/GUIDE-BUSINESS-WEB.pdf>

### 3. How to deal with the various legal systems in your negotiations with foreign partners

- ✓ You should not forget that the mere act of negotiating with a foreign partner pitches together not only the negotiators but also their legal systems, which are often quite unrelated. To this end, it might be interesting to make a brief comparison between contracts in civil-law countries and those concluded in countries whose legal system is based on the English common-law tradition, particularly since the latter is tending to prevail in international transactions.
- ✓ In a **civil law system such as the French one**, rights and obligations are derived from a statute book constructed in the form of codes, which comprise general concepts that are subsequently interpreted by courts or administrative authorities. The law is presented in conceptual terms. For this reason, French contracts are synthesised and are often shorter than those in most other countries.
- ✓ **Common law is a casuistic system**, in which norms are established on a case-by-case basis. Derived directly from appeals to the Crown, the system is still largely focused on procedure. It is therefore highly technical, and landmark decisions are rare.

#### - **Negotiations:**

- ✓ **In France**, whenever negotiations are delicate, it is customary to leave grey areas, whereby what is left unsaid increases the risk in the event of litigation. In this respect, it may be said that the French are sometimes defensive in their negotiations.
- ✓ **Negotiators from English-speaking countries**, proceeding on the principle that might is right, follow the rules of war with an approach that is polite and stealthy but none the less warlike. In practice, this means that a French negotiator who decides to give up his insistence on a particular clause in the hope of a *quid pro quo* from his partner on the next clause is making a mistake,

because Anglo-American negotiators are out to make a clean sweep. This is why they are regarded as very aggressive negotiators in spite of their urbane demeanour.

- ✓ The efforts of French negotiators focus on the aim of concluding the negotiations with a contract rather than on the details of its implementation.
- ✓ While the written word always far outweighs an oral company in France, the same does not apply in England. Thus the conduct of the parties may suffice to scrap a clause that one of the parties to the contract has not been applying. One such example is the **waiver**, which is an implicit renunciation that takes effect in the event of one party not making use of the provisions that it has negotiated or accepted.

#### - **Drafting:**

- ✓ As far as drafting practices are concerned, it should be noted that, in France, a **preamble** comprises statements describing the process by which the parties arrived at the agreement. It may serve as a means of interpreting the obligations set out in the body of the contract. Its legal value may therefore be decisive in a highly interpretative judicial system.
- ✓ **Drafters of English contracts tend not to insert preambles**, and indeed the content of a preamble **is null and void**. The practice of English courts, however, is referred to as literal interpretation, which means that each word of each clause has its own significance. In order to clarify the terms used by the parties and to facilitate the administration of the contract, authors of English contracts insert a set of definitions. You must therefore take the utmost care to read these definitions, because they sometimes serve to absorb intellectual property rights under cover of services rendered if the other party is not wary.
- ✓ **Accordingly, the drafting of contracts governed by common law tends to result in lengthy and detailed contracts.**

A contract governed by common law is subject to highly sophisticated fine-tuning by means of words that intensify or diminish the binding nature of an obligation. Behaving 'reasonably' defines a form of social conduct, a requirement to employ one's 'best endeavours' may transform an obligation to take specific action into an obligation to produce a particular result, and a requirement to 'mitigate losses' means that the party suffering damage is obliged to take steps to minimise the losses it incurs. Therefore, failing to act is not only as important, perhaps even more so, as doing what is written in the contract!

#### 4. **Personal capacity**

It is important to verify the contracting party's national legislation regarding the **legal capacity of persons**. Not all countries, for example, have opted for the same age of majority. Moreover, it is useful to **check that your negotiating partner is actually empowered to make a legally binding commitment on behalf of his or her company**.

## **5. Screening future partners**

It is recommended that you **gather as much information as possible on your partner's situation** (reputation, financial standing, bankruptcy procedure, etc.) in order to limit your risks.

A large number of operators, such as the Coface rating agency, exist in the market for the purpose of obtaining this kind of information.

## **6. Negotiations and discussions**

This stage should be approached with caution, for there is always one party seeking to dominate the other. The dominant party can impose its language and practices, thereby proposing a contract that corresponds to its own legal vision of the commercial operation. This stage may be formalised by means of a **letter of intent, which is also referred to as a gentlemen's agreement**.

## **7. Form of the contract**

It is recommended that the contract be drawn up in written form for the sake of proof, in accordance with the old legal adage ***Verba volant, scripta manent***. There is also a need to check the legal position regarding electronic content. In French law, for example, an e-mail is equivalent to a paper document. As far as evidence is concerned, on the other hand, it is merely regarded as tentative evidence in court proceedings.

## II. Essential clauses of international contracts

All clauses of a contract are important and therefore merit meticulous drafting. Nevertheless, depending on a company's strategy, its specific needs in terms of protection, the type of contract used and the geographical area in which it is to apply, some clauses are essential.

### 1. Which law applies to the contract?

When one French company concludes a contract with another, there is no doubt or confusion as to the law that applies to the contract; in such cases, only French law is recognised.

The situation becomes more difficult to assess if that French company wishes to enter into a contract with a foreign company. Although the firms are based in two separate countries, the law of only one country can apply to the contract, and so the applicable law has to be determined.

In addition, the contract may be performed in a third country, which increases the options. Provision may even be made for the contract to be governed by a different legal system altogether or by rules of international law, such as those of the Vienna Convention – see ***The rules of international law***.

**Choosing the applicable law of a contract is  
a matter for the contracting parties to  
decide among themselves**

When it comes to international contracts, the rule is that the **parties can determine which law they wish to govern their contract; this is the principle of party autonomy**.

Companies do not always see the need to insert such a clause, since no litigation is pending at the time when the contract is being concluded. That, however, is a basic error because, in the event of litigation, the company could find itself subject to an unfamiliar legal system that might operate to its severe detriment.

In other words, the choice of applicable law is a strategic decision as well as being of paramount importance. Depending on the type of contract a company wishes to conclude, it may, in fact, find it beneficial to consider the law of the country in which its foreign partner is located and to make a comparison. It should also be noted that the parties may decide that different legal systems should apply to different parts of the contract.

#### - The Conflict of laws rules of International law

In the absence of a contractual provision designating the applicable law, the court will make use of International convention in order to determine the applicable law. In such a case, it will apply what are conventionally known as the **conflict of laws rules**, which are derived from various conventions and other international legal instruments.

**The Hague Convention of 15 June 1955 on the law applicable to international sales of goods**, i.e. physical merchandise as opposed to items such as patents, goodwill, services or intangible assets. Not many states have ratified this Convention, but France is one of them. Under

the provisions of the Hague Convention, the law of the seller's country applies unless otherwise indicated in the contract.

- **In the European Union: the principles of European law**

**The Rome Convention** of 19 June 1980 on the law applicable to contractual obligations **recommends that the parties to a contract should exercise their freedom to determine the applicable law. If they have not done so, the contract is to be governed by the law of the country with which it is most closely connected**, that is to say the country of the party carrying out the 'essential' performance of the contract. This will generally mean:

- in the case of a sales contract, the law of the seller's country;
- in the case of a distribution contract, the law of the distributor's country.

The Rome Convention deals with conflicts of law for every type of international contract, not only those relating to the sale of goods.

This instrument, which had largely been ratified by the EU Member States, was replaced in 2008 by a European Regulation known as 'Rome I'.

**It should therefore be noted that the Convention still applies to numerous contracts that were signed before 2010.**

**The ROME I Regulation**

It should be borne in mind that European regulations are directly applicable in the law of Member States of the European Union.

**The Rome I Regulation - Regulation (EC) No 593/2008 of 17 June 2008 on the law applicable to contractual obligations – was adopted with a view to resolving conflicts of law between nationals of different Member States of the European Union (see [http://europa.eu/legislation\\_summaries/justice\\_freedom\\_security/judicial\\_cooperation\\_in\\_civil\\_matters/jl0006\\_en.htm](http://europa.eu/legislation_summaries/justice_freedom_security/judicial_cooperation_in_civil_matters/jl0006_en.htm)).**

The Regulation applies to contractual obligations in civil and commercial matters where there is a conflict of laws. It applies **only to contracts concluded after 17 December 2009.**

In this case too, party autonomy is the general rule.

In the absence of a choice expressed by the parties, the law that applies to the contract is determined under Article 4 of the Regulation as follows:

- a contract for the sale of goods is governed by the law of the country where the seller has his habitual residence;*
- a contract for the provision of services is governed by the law of the country where the service provider has his habitual residence;*
- a contract relating to a right in rem in immovable property or to a tenancy of immovable property is governed by the law of the country where the property is situated;*
- (...)*
- a franchise contract is governed by the law of the country where the franchisee has his habitual residence;*
- a distribution contract is governed by the law of the country where the distributor has his habitual residence;*

(...).

A contract that does not fall within any of these definitions is governed by the law of the country where the party required to effect the characteristic performance of the contract has his habitual residence.

Even if party autonomy is the rule, the Regulation qualifies this principle as a safeguard against the operation of the law of a non-EU country if that law is entirely at odds with European law, if it affords little or no protection or if the country in question has no relevant legislation. The Regulation stipulates that, where the contract relates to one or more Member States, the parties' choice of applicable law other than that of a Member State must not prejudice the application of the provisions of Community law.

## 2. Which court has jurisdiction?

Besides determining which legal system applies to a contract, it is also essential to determine which court has jurisdiction in the event of litigation. In fact, in the event of litigation, you may bring your action before a court of law or a Court of arbitration

Stipulating the court of jurisdiction in a contract avoids wasting time on discussions about the competent tribunal in the event of litigation.

Consideration must also be given to national jurisdiction rules, which may vary from one country to another. In France, for example, actions relating to commercial agents are heard by district courts rather than commercial courts.

The decision delivered by a national court is called a *judgment*, while that of an arbitration tribunal is known as an *award*.

### - National jurisdiction

Where a national legal system has been designated, it is recommended that the court with jurisdiction be indicated in a written agreement.

A clause assigning jurisdiction to a national court is normally known as a *jurisdiction clause*.

A court, moreover, will always be liable to disregard or misinterpret the law governing the contract if it is unfamiliar with the legal system in question. Accordingly, although it is not compulsory, it is good practice to ensure that the law applicable to the contract and the court of jurisdiction in the event of litigation are in the same system.

### - International arbitration

An alternative means of settling disputes is **arbitration**, in which one or more arbitrators – generally three – intervene to make decisions. Arbitrators are judges in the real sense of the term, because their decision is binding on the parties. Arbitration therefore serves to settle disputes by submitting them to one or more individuals chosen by the parties. It is an alternative method of resolving disputes outside the national legal systems.

- **What are the differences between a national court and an arbitration tribunal?**

The choice between a **national judge** and an **arbitrator** is very important. Each option has its advantages. There are three major differences between a national court and an arbitration tribunal, differences that relate to cost, confidentiality and time scale.

**As far as confidentiality is concerned**, judgments delivered by a court in France are public, whereas arbitration awards are not published unless the parties had decided to make provision in the contract for the possibility of appeal to a national court. In such a case, the arbitral proceedings would become public if either of the parties chose to appeal against the award.

**When it comes to cost**, national courts have the upper hand, at least in France, where judicial proceedings are free of charge. Only solicitors' fees and application fees are payable. Arbitral tribunals, on the other hand, are not public bodies, and their charges may therefore be considerable. By way of illustration, the arbitrator or arbitrators may come from a distant country, and the cost of travel, board and lodging and several meetings a month will be chargeable to the parties.

**The time scale** can also vary, and arbitral proceedings can take some time to complete.

In most cases it is unrealistic to expect a solution to a dispute before one year of proceeding

- **Are there any European instruments governing jurisdiction?**

The reference instrument in the European Union is **Council Regulation (EC) No 44/2001 of 22 December 2000** on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (see

[http://europa.eu/legislation\\_summaries/justice\\_freedom\\_security/judicial\\_cooperation\\_in\\_civil\\_matters/l33054\\_en.htm](http://europa.eu/legislation_summaries/justice_freedom_security/judicial_cooperation_in_civil_matters/l33054_en.htm)).

That Regulation adopted in 2000 determines the jurisdiction of courts in civil and commercial cases. It states that judgments delivered in a Member State of the EU must be recognised in the other Member States without the need for any special procedure unless an appeal is pending.

3. **Financial clauses: How do I optimise my prospects of receiving payment?**

- **Currency risk**

Parties may encounter a particular difficulty relating to the value of the contract, namely currency fluctuations.

Currency markets are subject to constant variations that inevitably influence the value of currency and thus pose problems in exchange transactions.

The parties must determine from the outset which currency is to be used. Care must be taken not to omit information identifying the precise type of money chosen. Rather than merely specifying 'dollars', for example, the contract must indicate whether it is referring to US, Canadian or other dollars.

There are various ways, somewhat costly, of limiting currency risk as far as possible. The least expensive way is to insert an indexation clause into the contract.

**Indexation clauses** are designed to make contractual provision for ways of sharing the currency risk in transactions between the buyer and the seller in the event of an intervening variation in the exchange rate.

There are several types of indexation clauses, which vary in the degree of protection they afford the seller and the buyer. Here are some examples:

**Clauses adjusting prices in proportion to exchange-rate fluctuations:**

When the contract is concluded, the seller sets the value of the goods in his currency. If the relative value of the invoicing currency increases, the export price is increased for the buyer, who bears the entire currency risk on the basis of the new exchange rate.

**'Tunnel' indexation clauses:**

The contract sets a minimum and maximum rate between which the invoicing currency may fluctuate without any impact on the price of the goods. If variations in the exchange rate exceed these limits, the price is revised upwards or downwards to reflect the changes.

**Indexation clauses for a currency or basket of currencies:**

The amount payable is pegged to a third currency or to a basket of currencies such as the SDR.\* Such a clause imposes a currency risk on both contracting parties.

**Divided-risk clauses:**

This clause ensures that the two parties share the currency risk. For example, the contract provides for part of the exchange-rate variation occurring between the invoicing date and the payment date to be divided by the exporter so that he meets half of the cost and the importer meets the other half.

**Currency-option clauses:**

A party to the contract may use another predetermined currency in the event of the contract currency falling below or rising above a particular exchange rate.

*\* Special Drawing Right: an artificial unit of account based on a currency basket comprising the US Dollar, the Euro, the Japanese Yen and the Pound sterling.*

- **Payment instruments and methods**

**The payment instrument** is the vehicle used to make a payment, in other words a cheque, a bank transfer, including the SWIFT electronic transfer, an international money order, a bill of exchange or a promissory note.

The choice of instrument is strategic too, which is why you are advised to refer to payment instruments in the contract. Indeed, the cost, time scale and security (solvency, etc.) of each form of payment must be assessed. Some means of payment entail very little or no cost but offer zero security. There is therefore a need to consider every means of payment in order to establish which of them will be most appropriate in a given situation and will provide maximum protection for the commercial transaction.

**Cheques.** Payment by cheque is a particularly French practice and is quite uncommon in other countries. Cheques feature less and less in international trade because of the trend towards paperless payment media. French law certainly regulates this payment method, which is not the case in other countries. Businesses do not incur any charges at the present time when they pay by cheque in France, where banks meet the cost, although the same does not necessarily apply in other countries. The method, however, offers no security at all, as cheques may bounce or be stolen, for example.

**The payment method**, for its part, refers to the procedure that is followed to make payment possible.

**Clean collection:** This payment method is adopted on the buyer's initiative. It has the advantage of low cost and ease of use; conversely, however, it does not offer any real guarantee of payment. It should therefore be used prudently with reliable partners and for trade with non-risk countries.

**Cash on delivery:** In this case, the transporter acts as the financial intermediary and is responsible for collecting the price and passing it on to the exporter. The latter, however, must be certain that the buyer will accept the goods.

**Documentary collection:** (payment on delivery of documents, documentary credit and stand-by letter of credit). This form of payment meets a fundamental need of each party:

- the buyer wants to receive, within the stipulated time limits, the quality and quantity of goods that were ordered;
- the seller wants to have a guarantee that he will be paid.

**FOCUS ON**

**SEPA (the single European payments area)**, an initiative of the European Union. Its purpose is to make electronic payments within the Eurozone as straightforward as national payments, whether payment is made by credit card, debit card, bank transfer or direct debit.

SEPA direct debiting is available in France from November 2010.

### - Term of payment

In principle, the term of payment will be subject to the law you have chosen to apply to the contract. For example, if the contract is governed by French law, the *Loi de modernisation de l'économie* (Economy Modernisation Act) will apply. Under that Act, the term of payment may not exceed **45 days from the end of the month in which the invoice was issued or 60 days from the invoice date**.

If, however, French law has not been chosen, can a French supplier impose the terms of payment prescribed by French law on a foreign purchaser? Conversely, can foreign suppliers insist on their French customers' complying with the Economy Modernisation Act?

The answer from the French General Directorate for Competition Policy, Consumer Affairs and Fraud Control (DGCCRF) is that the French Act is an instrument of public order and its application is therefore mandatory if either of the parties is based in France.

In fact, the DGCCRF, whose task is to uphold public order in the economic sphere, indicated that it would endeavour to ensure that French creditors were not made to accept lengthy payment terms by their debtors, particularly by those who used foreign payment centres for the sole purpose of circumventing national provisions. It added that it would ensure that debtors based in France settled with their creditors who were resident in other countries in such a way as to avoid distorting competition between the latter and operators residing in France.

Once the first judgments on this matter have been delivered, French businesses should learn more about the practical application of these provisions in international cases.

**European rules** are enshrined in Directive 2000/35 on combating late payment in commercial transactions.

That instrument does not harmonise payment terms within the EU, which are always a matter for the national legislature or the contracting parties. It provides for a default mechanism that relates only to the length of time by which payment is delayed beyond the prescribed settlement date.

The Directive defines a reference payment term, set at **thirty days** from the date of receipt of the invoice or of the goods.

In the event of late payment, liability for interest begins **automatically**. It was decided to set a single interest rate in the eurozone, based on the rate applied by the European Central Bank (currently 1%) to which 7% is added.

### **Penalty clause for late payment**

Where the contract prescribes penalties for late payment, it is essential to be rigorous in applying such provisions, even if that may appear to be an obstacle to trade, for the buyer or your trading partner might be inclined to take advantage of your laxity in future transactions and turn an exceptional instance into regular practice.

## HOW TO RECOVER A DEBT IN THE EU

In December 2008, the EU established a new **European payment-order procedure**. This is a means whereby businesses can rapidly recover funds in the event of litigation for the settlement of a debt arising from a commercial transaction with a European partner.

It does not replace national procedures but serves as an additional option.

The **cost** of the procedure must not exceed that of the procedure laid down by the national law chosen by the parties.

**How is it activated?** The applicant completes a form that is available online in all the official languages.

### **Which countries and which types of claim does it cover?**

The procedure can be applied in all Member States of the EU except Denmark. It relates to the recovery of pecuniary claims that are:

- clearly defined;
- uncontested;
- cross-border;
- civil or commercial matters.

The procedure does not cover fiscal, customs and administrative matters, matrimonial regimes, wills and succession, bankruptcy or social security.

**What are the limits on the procedure?** If the creditor opposes the use of the procedure, the only alternative is to switch to a procedure\* under the national law of the country in question.

*\* For more information on the procedure, see:*

[http://europa.eu/legislation\\_summaries/justice\\_freedom\\_security/judicial\\_cooperation\\_in\\_civil\\_matters/16023\\_en.htm](http://europa.eu/legislation_summaries/justice_freedom_security/judicial_cooperation_in_civil_matters/16023_en.htm)

## 4. The fundamental Incoterms clause

When international transactions take place, the movement of goods entails considerably increased risks. In order to provide greater security for traders who engage in international operations, the International Chamber of Commerce in Paris formulated and codified 13 International Commercial Terms, or Incoterms, the most recent version of which dates from 2000. These terms are periodically revised. While they are not compulsory, Incoterms offer the advantage of providing an international vocabulary of trade that enables the seller and the buyer to communicate on the delivery of the goods. Their use enables operators to:

- define the place of delivery of the goods;
- choose the form of delivery, whether entirely by sea or by multimodal transport; this influences the choice of packaging, which is always provided by the seller;
- determine who is to bear responsibility for the main carriage;
- divide the costs incurred between the seller and the purchaser;
- determine the point at which the risks relating to the goods are transferred to the purchaser;

- arrange for customs clearance on departure from the territory of a country and, more significantly, customs clearance on entry to the territory of the purchaser's country, including the establishment of liability for customs duties and taxes;
- load the goods in containers.

Along with other codifications such as revised terms of the Uniform Commercial Code of the United States, Incoterms are now widely recognised throughout the world. In practice, it may be said that they have become both a legal standard for negotiators of contracts and a logistical reference tool for operators.

In descending order of seller's obligations, the Incoterms rules are as follows:

**S = seller; B = buyer**

	EXW	FCA	FAS	FOB	CFR	CIF	CPT	CIP	DAF	DES	DEQ	DDU	DDP
Warehouse Storage	S	S	S	S	S	S	S	S	S	S	S	S	S
Warehouse Labour	S	S	S	S	S	S	S	S	S	S	S	S	S
Export Packing	S	S	S	S	S	S	S	S	S	S	S	S	S
Loading Charges	B	S	S	S	S	S	S	S	S	S	S	S	S
Inland Freight	B	B/S	S	S	S	S	S	S	S	S	S	S	S
Terminal Charges	B	B	S	S	S	S	S	S	S	S	S	S	S
Forwarder's Fees	B	B	B	B	S	S	S	S	S	S	S	S	S
Loading On Vessel	B	B	B	B	S	S	S	S	S	S	S	S	S
Ocean/ Air Freight	B	B	B	B	S	S	S	S	S	S	S	S	S
Charges On Arrival At Destination	B	B	B	B	B	B	S	S	B	B	S	S	S
Duty, Taxes & Customs Clearance	B	B	B	B	B	B	B	B	B	B	B	B	S
Delivery To Destination	B	B	B	B	B	B	B	B	B	B	B	S	S

- **EXW** *named place* = ex-works to agreed place
- **FCA** *named place* = free carrier to agreed place
- **FAS** *named place* = free alongside ship at agreed port of shipment
- **FOB** *named place* = free on board at agreed port of shipment
- **CFR** *named place* = cost and freight to agreed port of destination
- **CIF** *named place* = cost, insurance and freight to agreed place of destination
- **CPT** *named place* = carriage paid to agreed place of destination
- **CIP** *named place* = carriage and insurance paid to agreed place of destination
- **DAF** *named place* = delivered at frontier at named place of destination
- **DES** *named place* = delivered ex-ship at agreed port of destination
- **DEQ** *named place* = delivered ex-quay at agreed port of destination
- **DDU** *named place* = delivered duty unpaid to agreed place of destination
- **DDP** *named place* = delivered duty paid to agreed place of destination

Sales of goods for delivery entirely by sea are performed on an FAS, FOB, CFR, CIF DES or DEQ basis. In practice, the 'FOB port of shipment' deal has been favoured for a very long time by sellers, since it limits their responsibility to transport operations carried out in the territory of their own country.

While maritime transport has developed a great deal in recent years, it is nevertheless noticeable that use of the 'port-to-port' Incoterms is increasingly giving way to the multimodal options, particularly with the containerisation of goods. Multimodal delivery is now riding high, and this trend has greatly popularised FCA sales in particular.

When you negotiate or choose an Incoterm, it goes without saying that the contractual risks must be taken into consideration. At the same time, you must not overlook the effects of banking practices, which have also been codified by the International Chamber of Commerce in instruments such as the UCP 600 rules for documentary credits and the ISP 98 rules for standby letters of credit, which are designed to ensure that the necessary balance is struck between the interests of buyers and those of sellers in order to provide for the smooth functioning of these autonomous guarantees.

In terms of logistics, while it is essential to bear these factors in mind when selecting the applicable Incoterm and place of delivery, that is not enough. Consideration must also be given to the right of non-residents to obtain customs clearance in the country of destination, the safety of freight and trans-shipment operations on each shipping line, local stowage, loading or unloading practices in ports which might increase the risks on delivery or the delivery costs, the rules governing the packing and securing of goods, the use of port facilities that vary in terms of suitability for cargo handling and storage and the possibility of customs procedures under a prior agreement that would enable a local branch to obtain more rapid customs clearance of goods.

More significantly, sales in which ownership is transferred at the place of shipment, whether they involve maritime or multimodal transport, allow the contractual obligations regarding reception of the goods to be fulfilled at that point, thereby ensuring that, at this very early stage, the buyer accepts or rejects the goods, the payment by documentary credit, standby letter of credit or other instrument is effected, ownership of the goods is transferred to the buyer and the term of the warranty given to the buyer begins to run.

### **TO SUM UP:**

- an Incoterm is not a freight contract;
- its use is optional but recommended;
- it is chosen on the basis of the selected mode of transport – traditionally maritime but now chiefly multimodal;
- it will have consequences for the nature of the packing, which always remains the responsibility of the seller;
- it must be defined by reference to the latest applicable version of the ICC Incoterms (currently Incoterms 2000);
- the Incoterms are categorised into four groups – E, F, C and D – with the seller having fewest obligations in group E and most in group D;
- the Incoterms which transfer responsibility for the goods on shipment are EXW, FCA, FAS and FOB;
- the Incoterms which transfer responsibility for the goods on arrival are CFR, CIF, CPT, CIP, DAF, DES, DEQ, DDU and DDP;
- an Incoterm must be defined in relation to a place, e.g. 'CIF New York', 'FCA my forwarding agent in Lesquin' or 'DDP buyer's premises in Frankfurt';
- it may be supplemented to take account of local practices or handling arrangements in any of the world's ports.

*The Incoterms are being revised. A new version, Incoterms 2010, is planned for the autumn of 2010 for entry into force on 1 January 2011.*

*The main amendments will be the abolition of DAF, DDU and DES and the creation of a new Incoterm DAP – 'delivered at place'.*

## - Focus on the transfer of risks

### **Where does the seller's responsibility end and the buyer's begin?**

We shall give you an illustrative example to demonstrate the importance of such a clause. Let us imagine that your contract provides for responsibility to pass from the seller to the buyer from the time of unloading from the ship. In other words, if you are the seller, you transfer responsibility to the buyer at that point. But what if the goods were to fall into the water during the unloading process? Who would be responsible? Let us imagine that the contract did not make any reference to a choice of law or a court of jurisdiction. In the event of litigation, it would take some considerable time for the matter to be resolved.

This is why it is important to include such a clause and to refer to the Incoterms. Responsibility may pass to the buyer at any stage from the factory gate (ex-works – EXW) to the arrival of the goods on the buyer's premises (delivered duty paid – DDP).

## **5. Force majeure and hardship clauses**

### **How to deal with a contingency for which the parties have made no provision**

- **Force majeure clause**: Each country has its own definition of what constitutes *force majeure*. For example, some include strikes as a *force majeure*, while others do not. It is therefore useful to be as explicit as possible about the meaning of the concept; this can be achieved, for instance, by listing specific cases or by referring to the law of a particular country.
- **Hardship clause**: The hardship clause enables either of the signatory parties to demand the renegotiation of the contract if an economic or technological event seriously upsets the balance between the parties' contractual obligations. It is, in some senses, an economic *force majeure* clause.
- Following economic upheavals, such as those caused by an economic crisis, war, hyperinflation or unforeseeable market fluctuations, the equilibrium of the contract may be seriously compromised. Such circumstances are more liable to affect contracts whose performance extends over a lengthy period, such as those relating to major construction projects.

## **6. What is the point of annexes?**

Annexes must not be neglected.

They have the same value as the body of the contract, even though some annexes bear little relation to the substance of the contract. If your trading partner has drawn up the contract, you are advised to examine the annexes carefully and not just the contract itself.

Warning: In French law and in most other legal systems, annexes written in a language that you do not fully understand also have the same legal value as the body of the contract.

## **7. Revision and amendment clauses**

### **What do we do if we want to amend the contract after having signed it?**

It is always possible to conclude an amendment to a contract if each of the parties agrees to do so. The amendment to a contract is an act that partially revises a contract by adapting it or by adding new clauses.

Another option is to provide for a revision clause in the initial contract. For example, the product in question may no longer be marketable, or it may have become impossible to manufacture as a result of changes in the market. You can provide for such eventualities in a revision clause, which might indicate, for instance, that a new product may replace the present one in the circumstances described above.

It is important to specify in the agreement whether the cessation of manufacture of the present product does or does not constitute grounds for termination of the contract.

### **8. Other clauses**

- **Restraint-of-trade clause**: To be valid, a restraint-of-trade or non-competition clause must specify a duration and a geographical area. It plays an important role in the contracts of commercial agents.
- **Confidentiality clause**: To be valid, a confidentiality clause must be subject to time limits, which normally must not exceed a prescribed period.

All clauses are important. Each word used in them, and its position in the text, may be strategic and have extensive implications. Even a comma can alter the meaning of a sentence. The preamble and the title of the contract are important too, because the court may seek to determine the will of the parties from them.

### III. The main types of international contract

In their international commercial dealings, most companies – and SMEs in particular – avail themselves of three main kinds of contract:

- international sales contracts,
- international distribution contracts, and
- international agency contracts.

#### 1. International sales contracts

##### - Legal rules governing sales contracts

As we saw above, the parties can choose the law that applies to their international contract, opting either for the national law of a country or for the provisions of an international agreement.

The most frequently used and best known agreement is the **Vienna Convention of 1980 on Contracts for the International Sale of Goods**.

The Convention, which has been ratified by 74 countries at the time of writing, applies only in the event of problems connected with the formation of a sales contract and regulates the rights and obligations of the contracting parties.

Given the problems involved in choosing the applicable law, its main purpose is to enable parties to choose a **set of neutral provisions** and to **standardise the rules that apply to international sales**.

This Convention radically changed the French legal landscape for the very simple reason that, under the hierarchy of rules, whenever France signs an international agreement, the latter is incorporated into national law and takes precedence over domestic law.

Consequently, where the Convention applies, it has precedence over domestic law, which means that there are a number of circumstances in which the Convention replaces French national law.

Another important aspect is that the Vienna Convention is an additional instrument, which means that the parties can always derogate from its provisions in the contract, although they must do so explicitly (Article 6 of the Convention).

##### - Form of a sales contract

A sales contract may be formed either by a written act negotiated by the parties, by general terms and conditions of sale imposed by the seller or by general terms and conditions of purchase imposed by the buyer.

##### - General terms and conditions of sale

General terms and conditions of sale enable companies to define the legal framework of their commercial transactions. Each exporting company has its own general terms and conditions of sale; **they should not be copied and pasted from national general terms and conditions. They are drawn up either in the language of the buyer's country or in English.**

**If a customer negotiates and requests amendments to the general terms and conditions, they may be supplemented by particular terms and conditions of sale or by a contract providing for certain derogations from the general terms and conditions.**

In order to be recognised and accepted as valid, such amendments must **reach the customer prior to acceptance of the offer.**

If they simply feature on the back of the invoice at the time of delivery, they will be of no value in the event of an action by the customer, who may claim to have had no knowledge of them at the time of purchase.

**One elementary precaution is to obtain a signature on all order forms, which should have the general terms and conditions of sale printed on the reverse. The form should indicate that the signature implies explicit acceptance of the printed terms and conditions.**

- **Contradictions between general terms and conditions of sale and of purchase**

The buyer may wish to substitute its own general terms and conditions of purchase for the general terms and conditions of sale. In French and German law, contradictory clauses invalidate each other in such cases. The Vienna Convention and the law of English-speaking countries, on the other hand, enshrine the principle of the 'last shot', which means that the last terms and conditions to be sent will apply, provided that the receiving party has accepted them, albeit tacitly by taking delivery of the goods or paying the price. The applicable terms and conditions are therefore the last ones to be transmitted before the delivery of the goods. It is obviously desirable that the parties should negotiate terms and conditions of sale in advance and record them in an agreement initialled by each party. Nevertheless, if this were not done, the matter would be resolved in accordance with the applicable law. A clause worded to the effect that 'These terms and conditions shall override all contrary terms and conditions' is an inadequate safeguard.

For example, where French law applies to a contract, under Article L 441-6 of the Commercial Code the general terms and conditions of sale constitute the basis of the commercial relationship between buyer and seller.

Acceptance of an offer

**The sale is validated as soon as agreement is reached  
on the offer and the price**

By accepting the offer, the customer consents to the transaction and paves the way for the conclusion of a contract of sale. The contract does not materialise until the offer has been followed by acceptance.

**As long as no acceptance has been received, the offer may be withdrawn. An acceptance should be communicated in written form** so that the seller obtains a certain guarantee and has evidence in the event of litigation.

In this particular case, acceptance takes the shape of an order form or a contract. **In more and more cases, a simple e-mail is being used to confirm the buyer's acceptance of the offer.**

Every clause in a contract entails a cost and often immediate or latent risks too. In international transactions, of course, the potential risks are far more numerous.

Contact your advisers in order to learn about the merits of a legal system, a court of jurisdiction or an arbitration mechanism before committing yourself.

## Essential clauses to insert in an international sales contract

CONTRACTING PARTIES	<ul style="list-style-type: none"> <li>- Identify the parties (buyer and seller): company registered and trading names, full addresses and names of their respective representatives.</li> </ul>
NATURE OF CONTRACT	<ul style="list-style-type: none"> <li>- Define the subject of the contract (supply of goods or service provision).</li> <li>- Describe the technical aspects, the quantity and/or volume, the weight and, where appropriate, the form of packing, because the buyer can stipulate requirements.</li> </ul>
PRICE AND PAYMENT METHODS	<ul style="list-style-type: none"> <li>- Set the price in euros or in another currency (think about currency risks).</li> <li>- The price will be accompanied by an Incoterm, which determines responsibility for transport costs, customs duties, insurance and the point at which ownership is transferred.</li> <li>- The price of the goods will be set out in detail (unit price and total).</li> <li>- Provide for a means of settlement that provides the seller with maximum security.</li> <li>- Payments on account will guarantee the order.</li> <li>- In the case of a documentary credit, the seller will make note of the credit application.</li> <li>- Lastly, if the applicable legislation permits, a retention-of-title clause may be included in the contract.</li> </ul>
TRANSPORT ARRANGEMENTS	<ul style="list-style-type: none"> <li>- Determine the mode of transport that best suits the nature of the goods and the destination and offers the best security.</li> <li>- The parties' respective obligations are specified on the basis of the selected Incoterm.</li> </ul>
DELIVERY ARRANGEMENTS	<ul style="list-style-type: none"> <li>- Determine the date and place of shipment.</li> <li>- Define time limits on the basis of the entry into force of the contract; adherence to delivery deadlines is one of the seller's main obligations, and provision must be made from the outset for specified penalties for late delivery.</li> </ul>
<i>FORCE MAJEURE</i>	<ul style="list-style-type: none"> <li>- Define the concept of <i>force majeure</i> for unforeseeable events.</li> </ul>
GUARANTEES	<ul style="list-style-type: none"> <li>- Define the guarantees to be given by each party.</li> </ul>
JURISDICTION IN THE EVENT OF LITIGATION	<ul style="list-style-type: none"> <li>- Determine which law is to apply for the resolution of disputes.</li> <li>- French law is not always the best solution, since it is highly protective of buyers. On the other hand, if you opt for the seller's law, familiarity with that law is imperative.</li> </ul>
LANGUAGE	<ul style="list-style-type: none"> <li>- Determine the language of the contract. Both parties should have command of the chosen language. Nevertheless, beware of translation problems.</li> </ul>

## 2. International distribution contracts

**The purpose of a distribution contract is to establish one or more sales points within a geographical area from which goods and services can be offered to a specific clientele.**

It enables suppliers to benefit from existing commercial facilities and to select their trading partners. This commercial model also has the advantage of enabling suppliers to impose sales methods and practices associated with their products or brands.

The distribution contract is a framework agreement, which means that it establishes general obligations for each of the parties over a lengthy period and is supplemented by implementation agreements (sales contracts), which are often annexed to the contract in order to specify the products and/or services in question, prices, delivery arrangements and the rules governing transfer of ownership.

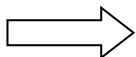
- **Obligations of each of the parties**

The supplier or licensor undertakes to supply the distributor over a fixed period through the conclusion of implementation agreements or contracts, while it is primarily the task of the distributor or licensee to market the products in the relevant territory.

- **Choice of distribution formula**

***Which distribution method to choose***

- If a distributor acts in the name and for the account of the supplier, he is an **agent**, and the appropriate basis for his activity is an **international agency contract (see next heading)**.
- If a distributor acts in his own name but for the account of the supplier, he is a **sales commissioner**, and the appropriate contract is a **sales-commissioner agreement**.
- If a distributor acts in his own name and for his own account, reselling products he has purchased from the supplier, he is a **distributor** in the strict sense of the term and would have a **distribution contract**.



**Distribution contracts may be exclusive or selective.**

***What is meant by an exclusive distribution contract?***

**Under an exclusive distribution contract, the producer undertakes to market its products within a defined territory through a single commercial intermediary – the sole distributor. The distributor is thus handed a competitive advantage within its geographical area.**

***What is meant by a selective distribution contract?***

An **authorised-distributor contract** or **selective distribution contract** is an agreement whereby a supplier, wishing to maintain the reputation of its products, undertakes to supply a reseller selected on account of its aptitude for the distribution of such products.

In order to obtain authorisation, the distributor must meet a number of criteria, relating to factors such as location, layout of premises, storage conditions, after-sales service, the professional expertise of the distributor and its sales team, etc. **This enables the supplier to control the quality of its distribution network by ensuring that its partners possess sufficient skills and resources to market its products.**

**For its part, the distributor benefits from the reputation of its supplier and is also authorised to distribute competing products.**

**It would be wise to expect the distributor in return to commit itself to sales quotas.**

- **Distribution contracts and Community competition rules**

The European competition rules cover **agreements which are liable to impact on trade between Member States and which have the purpose or effect of preventing, restricting or distorting competition** within the common market.

In many cases, exclusive or selective distribution agreements may fall foul of these competition rules.

In order to allow companies to go on developing their distribution network, an **exemption regime** was established by **Regulation (EC) No 2790/1999** to cover what are known as **vertical agreements**.

**Vertical restrictions** are agreements or concerted practices concluded between two or more companies operating at different stages in the production and marketing process; the restrictions relate to delivery, purchase of goods for resale or processing or the marketing of services. Such agreements govern the conditions in which the parties may buy, sell or resell particular goods or services.

**The exemption granted by the Regulation applies only if the supplier does not command more than 30% of the relevant market in which it is selling the goods or services covered by the contract.** In the case of exclusive distribution agreements, however, it is the distributor's market share which is taken into consideration and which cannot exceed 30%.

In some cases, distribution agreements are not eligible to benefit from exemption.

If the agreement contains any of the **clauses enumerated in Article 4 of Regulation (EC) No 2790/1999, the whole agreement is ineligible for exemption** and is therefore null and void, even if the companies' share of the market does not exceed 30%. **These are known as the blacklisted clauses:**

- a. clauses imposing a fixed or minimum resale price on buyers; clauses which provide for a maximum resale price or a recommended resale price, on the other hand, are admissible;
- b. clauses restricting the buyer's scope for resale territorially or in terms of clientele;

There are, however, **four types of admissible clauses** in this category, namely:

- clauses prohibiting active sales in a territory which the supplier has reserved for itself or allocated to another buyer;
- clauses prohibiting wholesalers from reselling to end users;
- clauses prohibiting a distributor, in a system of selective distribution, from selling to an unauthorised distributor;

- clauses prohibiting a purchaser of components intended for incorporation into end products from reselling such components to the supplier's competitors;
- c. clauses restricting active or passive sales to end users by retailing members of a selective distribution system;
- d. clauses used by the supplier to restrict cross-supplying between members of a selective distribution system;
- e. clauses containing restrictions imposed, in this case, by the buyer to prevent suppliers of components from selling them as spare parts to end users or unauthorised repairers.

### **Clauses that do not affect the agreement in its entirety**

Article 5 of Regulation (EC) No 2790/1999 lists three types of clause which are not eligible for exemption and must therefore be declared null and void but which, unlike the blacklisted clauses, do not nullify the entire contract. These are:

- a. **non-compete obligations the duration of which is indefinite or exceeds five years** and which apply during the term of the contract;
- b. **non-compete obligations causing the buyer to refrain from manufacturing, buying, selling or reselling goods or services after the agreement has terminated;**
- c. obligations causing members of a selective distribution system to refrain from selling the brands of particular competing suppliers.

#### **New exemption regulation to apply from 1 June 2010**

On 20 April 2010, the European Commission adopted a new Regulation on the exemption of categories of vertical agreements and concerted practices in the realms of supply and distribution. This instrument, accompanied by guidelines, will replace the current exemption regulation (*Commission Regulation (EC) No 2790/1999 of 22 December 1999 – OJ No L 336 of 29 December 1999*), which expires on 31 May 2010.

The basic principle remains unchanged, in that producers will still be able to choose the distribution method for their products. To benefit from exemption from the prohibition of vertical agreements and concerted practices, however, they must not command more than a 30% share of the market, and their distribution or supply contracts must not provide for price-fixing or other defined types of restrictive practice.

The main change made by the new instrument relates to the **establishment of the same 30% ceiling for distributors and retailers, which is designed to take account of the constant increase in the purchasing power of distribution giants**. According to the Commission, this change will benefit small and medium-sized enterprises, which would otherwise be squeezed out of the distribution market.

### Essential clauses of a framework distribution contract

Designation of products	The range of products must be precisely described.
Use of brand names	Specify the conditions and duration.
Designation of territory	To be specified in the case of exclusive distribution.
Authorisation conditions	To be specified in the case of selective distribution.
Court of jurisdiction	To be specified, otherwise Regulation (EC) No 44/2001 on jurisdiction applies by default.
Applicable law	Parties' choice (national law or Vienna Convention).
Term of the contract	Incorporate the aspect of termination and compensation.

### **3. International agency contracts**

Commercial agents are **self-employed** professionals who act **in the name and for the account of their principal**. They are generally remunerated by means of commission and are entitled to a termination payment. Their main objective is the conclusion of contracts between their principal and third parties (its customers). They pursue their activities on a permanent basis under fixed-term or open-ended contracts, unlike brokers or sales commissioners, who normally operate on an *ad hoc* basis.

#### **- The status of a commercial agent in European law**

The European Economic Community formulated a set of common rules governing the activity of self-employed commercial agents in 1986 (Directive 86/653/EEC). That instrument applies to all commercial agents pursuing their activity in a Member State, more or less regardless of whether their principal is based there. This harmonisation of the status of commercial agents, besides simplifying matters, established a **system of safeguards for commercial agents** with which any company wishing to use that form of commercial representation ought to be familiar.

## Major clauses in agency contracts

<b>Preamble</b>	The contract should be defined as an agency contract, and the purpose of the business relationship should be explained; it might, for example, be motivated by the principal's desire to establish itself in the territory in question.
<b>Identification of the parties</b>	This should include names and addresses. Specify whether they are principals or agents. In the case of companies, their registered office must be indicated.
<b>Legal requirements</b>	For countries in which agents have to be registered, for example at the Commercial Court, it is necessary to add a declaration to the effect that such registration has taken place, specifying the place and date of the agent's registration.
<b>Purpose of the contract</b>	Agents' functions with regard to the promotion of sales should be clearly indicated; it is also necessary to state whether the agent is empowered to conclude contracts directly with customers. Mention should be made of any obligation to inform the principal of action taken to follow up contacts, etc.
<b>Specification of products and/or services</b>	The products and/or services to which the contract applies must be precisely detailed. There is also a need to provide for the eventuality of the product or service being modified or replaced by another. Provisions regarding after-sales service and guarantees should also be included.
<b>Definition of the territory covered by the contract and exclusivity</b>	The territory in which the agent is to operate must be clearly defined. It must be clearly indicated whether the agent is the only person authorised to operate in the territory (sole agent) or whether other agents have been appointed.
<b>Performance of the contract</b>	The obligations of the principal and of the agent must be explicit with regard to the supply of information on products, the supply of information or promotion material, advertising, stock management, the delegation of responsibilities and the acceptance of orders.
<b>Payment of commission</b>	Commission is generally paid for each transaction. Various commission rates are possible: A. for transactions transmitted by the agent to the principal; B. for transactions concluded within the territory but not involving the agent; C. for transactions which the agent have not been transmitted to the principal, but are effected with customers identified at the outset by the agent. The intervals at which the agent is to be paid should be stipulated.
<b>Termination of the contract</b>	The contract may be concluded for a fixed term or may be open-ended. In the case of an open-ended contract, it will be necessary to define required periods of notice for each of the parties (one month for the first year, two for the second, and three months in subsequent years).

<b>Compensation</b>	Provisions should be inserted defining the circumstances in which compensation or remuneration is not payable, such as cases in which the agent has been guilty of serious misconduct, the agent has terminated the contract or the agency contract has been transferred.
<b>Non-compete clause after the expiry of the contract</b>	Any clause imposing restraint of trade after the expiry of the contract must be set out in writing and must be limited to the subject of the agency contract, for example the marketed product, and to the agent's territory. The duration of such restrictions, moreover, must not exceed two years.
<b>Applicable law and courts of jurisdiction</b>	When an international agency contract is concluded, it is advisable to choose the legal system that will govern the contract and to determine which countries' courts will have jurisdiction in the event of a dispute.
<b>Amendments to the contract</b>	The contract may include a declaration specifying that any amendment must be made in writing and be signed by both parties.

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# ENTERPRISE EUROPE

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