International purchases.
The question of which law applies?

e-zette
aija email magazine

Almudena Álvarez Otero, July 2008

An important question which often arises during an international transaction is what law applies to a contract of sale between parties from different countries. Much too frequently, the parties to an international agreement fail to include what is known as a "choice of law" provision. The failure to include such a clause may result in unexpected problems to both parties, especially in the context of debt collection.

On May 18, 1992, Spain joined the Rome Convention of 1980, which addresses the issue of what law applies to a contract between parties from different countries. According to Article 2 of the Rome Convention, it has universal character, which means that a court that sits in a country that has adopted the Convention will, in the case of a dispute before it, apply the law of the country as required by the Convention, regardless of this law belongs to country which has not joined the Convention.

As an initial matter, the Rome Convention of 1980 establishes the freedom of choice of law by the parties. However, when the parties fail to specify what law applies, Article 4 therein states that the contract shall be governed by the law of the country with which it is most closely connected. It is further presumed that the contract is "most closely connected" with the country where the party who is to effect the performance which is characteristic of the contract has, at the time of contract, his habitual residence, or, in the case of a business entity or corporation, its headquarters. If the subject matter of the contract is a right in immovable property or a right to use immovable property, it is presumed that the contract is most closely connected with the country where the immovable property is situated.

In most of cases, the performance considered "characteristic" of the contract is the performance that is not payment, and in cases of purchases, specifically, the characteristic performance would be delivery. Typically, therefore, it is the law of the seller's country that is applied. This principle, however, is not expressly stated in the Rome Convention, but it is instead the result of judicial interpretations of the Rome Convention. Accordingly, what the Rome Convention says versus what the Rome Convention means depends heavily on judicial interpretation of its provisions.

More recently, Regulation No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations was published in the Official Diary nº L 177 of 4 June 2008, which replaces the Rome Convention and is known as "Rome I." [1] This Regulation will apply to contracts signed after December 17, 2009. However, this Regulation has not been adopted by Denmark and the United Kingdom. Meanwhile, the Convention of Rome will apply to the contracts signed by these two countries and also to the countries which have already signed "Rome I "".

Rome I specifically states what law applies to eight (8) different types of contracts. In the case of contracts for sale, specifically, Rome I states that the applicable law will be the law of the country where the seller has his or her usual residence. This article establishes what it is been said before by the judicial interpretations.

The following is a simple and practical hypothetical which illustrates the application of Rome I: a Turkish company sells clothes to a Spanish company. The Turkish company delivers the goods, but the Spanish company does not pay for them. The Turkish company sues the Spanish company before the Spanish Court. The Spanish Court will have to apply the Turkish Law because the seller is from Turkey. Based on the foregoing, it is irrelevant that Turkey has not signed the Rome Convention, because as Spain it is a signatory, the Convention would be applied in this case, and the Spanish Court would apply the Turkish Law.

Indeed, the default application of Rome I has both advantages and disadvantages for both sellers and buyers.

On the one hand, Rome I offers legal security to a seller in an international transaction. Indeed, a seller bears the most risk in a purchase and sale transaction because the seller's obligation is to send the goods being purchased to the buyer, who in an international transaction, is likely located in a different country, whose laws the seller might not be familiar with and the seller really can only hope and expect to subsequently receive the payment from the buyer. If the buyer does not pay after the goods are delivered, the seller is already damaged by having sent away the goods. Obviously, the buyer is not similarly situated because if a seller does not fulfil his/her deliver goods in the manner prescribed by his agreement with the buyer, then the buyer would simply withhold payment. There is no economic damage to either party.

Notwithstanding the protection allotted to a seller by Rome I, a disadvantage to the buyer is that he or she might have a sense of being unprotected by not knowing, for example, the deadlines for checking the goods' quality and in the case of defective goods, the deadlines to complain about those goods under the seller's national law.

Additionally, another problem arises when there is a breach of a contract for sale and the aggrieved party must go before a court that will have to apply foreign law. As noted above, pursuant to Regulation (CE) n° 44/2001 of the Council, of 22 December 2000 and Spanish law, an aggrieved party will have to go to a court located in the debtor's residence country; however, that court will have to apply the law of the buyer's country. In order for a Spanish court to apply foreign law, a certificate of law must be presented by two lawyers to the court. The document must be officially translated and notarized.

[1] *Rome II is the Regulation (EC) No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations.*

***NEXT** page >*

< PREVIOUS page

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As such, an aggrieved party seeking relief from a court pursuant to foreign law bears additional expense in terms of time and money in order to initiate the appropriate procedure.

In order to avoid these types of problems in international purchases, it is advisable to specify the law that governs the parties' agreement at the outset of the parties' relationship and especially in the controlling agreement between the parties. It is clearly the most efficient and secure manner to proceed, particularly in debt collection matters or in cases by governed by the EC Small Claims Procedure which will applies as of January 1, 2009.

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