

Recent Trends in Cross-Border Trade Transactions

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Notwithstanding the growth of international trade at an astounding rate over the last 20 years, it has been affected in a big way by the recent financial crisis. The credit crunch and shortage of trade financing funds affect both exports and imports even to the point of stoppage. It goes without saying that the number of cross-border trade transactions involving Ukrainian companies or commodities recently fell greatly. Moreover, the chances that suppliers are faced with Ukrainian customers that are, or may be, dealing with financial difficulties are growing. As the number of such customers is increasing, the number of concerns for foreign suppliers has also expanded. For these reasons, the question of how to advocate the interests of a foreign supplier or seller without making a transaction too expensive is becoming more critical to every transaction.

In this article we do not intend to cover all available contractual structures that may be used to protect foreign sellers, but concentrate mainly on recent trends in protecting the seller by emphasizing the applicable provisions of Ukrainian law. Understanding all legal issues while choosing the right instrument for advocacy for the seller and possible preventive actions for a particular transaction can take time to discover.

Know your Potential Buyer

Prior to entering into supply or sale and purchase agreements with a new partner, a foreign seller is always trying to gather as much information as possible about a potential buyer, for example publicly available information as well as information from various information agencies, etc. Such information provides a seller with an opportunity to evaluate whether a potential buyer is a reliable partner, potential risks of default thereof as well as to identify the assets of a buyer to be used as collateral in a transaction.

Payment in Advance of Delivery

It is well known that a seller can eliminate risks related to non-payment of a buyer for products by introducing into a supply agreement a provision in respect of payment of the entire amount for products or at least part thereof in advance of delivery.

Letter of Credit

Settlement by means of letters of credit has recently come to be regarded as a very convenient and secure vehicle for a seller, especially if confirmed by a reliable bank. While choosing this instrument a foreign seller shall thoroughly analyze and provide in detail directly in the supply agreement all terms and conditions applicable to the letter of credit (e.g. a list of documents to be submitted, a presentation period, applicable law, arbitration clause etc.). However, it should be noted that such bank operations are quite expensive and there are a few reliable banks in Ukraine issuing letters of credit, especially those to be further confirmed by a foreign bank.



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Suretyship

Suretyship is another vehicle to ensure proper performance by a buyer of payment obligations. Such a vehicle is frequently used in Ukraine due to the following: (a) any reliable company or even an individual may act as a surety; (b) suretyship may be instituted between a surety and a seller in different forms e.g. by including respective provisions in a supply agreement to be sealed and signed by a seller, a buyer and a surety; or by a separate suretyship agreement; (c) co-suretyship or mutual suretyship is allowed; (d) suretyship may be instituted as to all obligations of a buyer under a supply agreement or only as to a part thereof, etc.

However, the ability to take advantage of suretyship requires keeping abreast of a myriad of applicable Ukrainian legal issues whilst drafting a suretyship agreement. Ukrainian law leaves a lot of terms and conditions to the discretion of the parties. For example, a surety and a buyer shall bear joint and severable liability if a subsidiary liability of a surety is not specifically agreed upon; a surety shall be responsible for a buyer's main obligation under a supply agreement as well as for compensation of damages, payment of interest, penalty; if otherwise not provided for in a suretyship agreement, etc.

Pledge and Mortgage

Pledge and/or mortgage are frequently used forms of collateral in Ukraine. However, to ensure validity and enforceability of pledge and/or mortgage in Ukraine, a seller shall bear in mind the following:

(i) The registration requirements. Failure to register pledges does not entail invalidity thereof, but it does affect the priority of rights satisfaction. Moreover, all mortgage agreements in respect of immovable and land plots shall be notarized;

(ii) To be pledged or mortgaged, property shall be owned and capable of being alienated by a pledgor. For such purpose, a seller shall verify whether a pledgor enjoys title to the property, or whether there are any rights of third parties in respect of property to be pledged;

(iii) If property subject to pledge is in joint ownership, the permission of all co-owners is required;

(iv) The foreign supplier shall give consideration to a number of applicable Ukrainian law issues e.g. if otherwise not provided in a pledge agreement, property subject to pledge may be replaced only upon consent of a pledgee; a pledgor is entitled to alienate or provide in use property subject to pledge only upon the consent of a pledgee; further pledge is permitted; levy of execution upon property subject to pledge shall be performed on the basis of a court decision, etc.

Guarantees and Standby Letters of Credit

To mitigate risks of non-payment by a buyer, a seller may request issuance of a guarantee gaining a number of advantages compared with suretyship e.g. independence of a guarantee from a buyer's main obligation in the event of termination or invalidity, increase or decrease thereof without a seller's consent, assignment of a buyer's main obligation to another person. However, prior to agreeing upon a guarantee, a seller shall take into account that in Ukraine: (a) only banks, insurance companies or other financial institutions are entitled to issue guarantees;

(b) a guarantee shall contain a definite sum to be paid to a seller in the event of a buyer's breach, list of documents to be submitted by a seller to a guarantor to substantiate occurrence of a buyer's breach; term of a guarantee validity, etc.; (c) guarantees may be conditional or unconditional; irrevocable or revocable; (d) a seller is not entitled to assign its right to claim against a guarantor to another person if otherwise not set out in a guarantee, etc. Due to the financial crisis the National Bank of Ukraine has strengthened requirements as to issuance of guarantees. Therefore, it may be virtually impossible for some buyers to obtain guarantees from banks. Moreover, such bank operations are quite expensive. Therefore, at present the practical enforceability of a guarantee shall be additionally negotiated between a seller and a buyer.

Another securing vehicle that can be used is a standby letter of credit. In the event of a buyer's breach of obligations under a supply agreement, its (issuing) bank shall pay under a standby letter of credit subject to receipt of a seller's payment demand within the term of a standby letter of credit along with documents confirming the buyer's breach. In order to eliminate the risk of non-performance by a Ukrainian (issuing) bank under a standby letter of credit, it is advisable to request for confirmation of this by a reliable foreign bank.

Factoring and Discounting or Sale of Promissory Note

Ukrainian law allows both factoring and discounting or sale of a promissory note (as under Ukrainian foreign currency regulation in relations with a seller — non-resident, a Ukrainian buyer is entitled to issue a promissory note only, but not a bill of exchange, we will refer herein to a promissory note). The said instruments may facilitate a trade transaction both for a seller being able to receive payment for products within the desired term (even prior to delivery) and transferring risks of non-payment by a buyer to a bank as well as for a buyer receiving deferred payment conditions.

While deciding on an effective contractual structure and choosing the said instruments a supplier shall, among other things, carefully consider applicable Ukrainian regulatory requirements and a number of practical issues e.g.: (a) only specially authorized financial institutions are entitled to be engaged in the said schemes; (b) the said instruments are quite expensive (e.g. commission for services, interests for using credit, significant discounts may be applicable); (c) the amount under the said instruments may be paid not by single payment but in installments;

(d) the authorized institutions set forth very strict requirements applicable to supply agreements, documents con-

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firming actual supply of products and may require insurance of supply agreement performance or other collateral, etc.

Final Remarks

Broadly speaking, in arriving at the present time at an answer for the right and effective contractual structure and instruments for protecting the seller's interests in a foreign trade transaction with a Ukrainian buyer one must, among other things, carefully consider not only regulatory requirements and legal complications, payment and securing instruments used, but also give consideration to a number of practical issues such as the cost of such instruments, availability and complexity acquiring them. Focus on examining the proposed protective and preventive instruments from all commercial, legal and practical angles can make a difference in protecting the interests of sellers in foreign trade transactions. The latter is very important for choosing the most effective and efficient instruments and contractual structures to cater for the supplier's needs taking into account the buyer's facilities.