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# Commentary: The Trajectory of Complex Business Contracting in Latin America

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## COMMENTARY: THE TRAJECTORY OF COMPLEX BUSINESS CONTRACTING IN LATIN AMERICA

CLAIRE A. HILL\*

By some accounts, Latin American contract documentation increasingly resembles U.S. contract documentation.<sup>1</sup> This is puzzling, given that the U.S. documentation has developed in a broader institutional context particular to the U.S. The context includes a particular type of legal training, particular types of law firms, particular legal institutions, and so on. Why is this occurring, and what effect will it have on contracting practice in Latin America? This commentary briefly considers these issues; it considers as well some broader implications of international convergence in contracting practices.

Until recently, Latin American contract documentation was quite short, as is typical for civil code countries where the code itself specifies many of the terms for which parties would want to contract. As more transactions in Latin America involve non-Latin American parties, particularly U.S. parties, the contracts are becoming longer and more detailed, and are containing increasing amounts of boilerplate. This is so whether the contracts are governed by U.S. law or by the law of the Latin American country. Indeed, where contracts are governed by the law of a Latin American country, they may cover matters addressed in the applicable civil code. And they may do so in a manner different than the code provision without expressly superseding the code provision—indeed, even without a thought that there are code provisions that are being superseded. In this commentary, I briefly explore a few implications of this development.

\* Professor, University of Minnesota Law School and Director, Institute for Law and Rationality. I wish to acknowledge helpful comments from participants in the *Law and Economic Development in Latin America: A Comparative Approach to Legal Reform* symposium, which took place at the Chicago-Kent College of Law in April of 2007, and from D. Daniel Sokol. I also want to acknowledge Professor Sokol's assistance in helping me arrange interviews with Latin American lawyers.

1. My stylized description is based on interviews I conducted with several lawyers in various Latin American countries. For expository purposes, I will treat Latin American contracting practice monolithically. I was told in my interviews that the types of contracting practices I am interested in exist principally in Brazil, Chile, Mexico and Argentina—that there were some country-to-country differences, but that they were not significant for my purposes. I therefore mean my account to apply principally to those countries.

I begin with what seems like the easiest inquiry: why might this development have occurred? I reject the idea that U.S.-style documentation is inherently superior, even in the U.S.<sup>2</sup> I argued in two earlier pieces<sup>3</sup> that U.S.-style documentation, and its increasing use in European transactions, is in significant part a product of agency costs within law firms and between law firms and their clients, as well as path-dependency and a prisoner's dilemma-propelled arms race. There are some functions served efficiently but overall, the process is clearly second-best.

The same sorts of explanations I proposed in those two pieces are applicable here. Once one party comes "armed" with a more complex and comprehensive contract, it is difficult for the other party to say "oh, we don't need all that extra verbiage."<sup>4</sup> The countervailing arguments—this level of detail and intricacy signals distrust, this is a significant increase in paper and money without much (if any) added benefit, the poor trees are being chopped down for no good reason, and that the complexity may lead us to overlook something easy and important—are hard to advance successfully. The other side's client is getting these "protections"—surely our client needs them too.<sup>5</sup>

In Latin America, the same explanation holds with greater force. The U.S. lawyer can get his way using very little of the considerable bargaining power he has available on account of his status as coming from the country of "big deals" and big dealmakers. U.S. deal-making has the reputation of being sophisticated and state-of-the-art. Who wouldn't want to emulate U.S. practices, especially a corporate bar trying to "play in the big leagues?" Furthermore, a not-insignificant number of Latin American lawyers obtain LLM degrees in the United States, and may follow this education with a few years of practice at big U.S. firms.<sup>6</sup>

Indeed, for the many contracts governed by U.S. law, the U.S. parties can successfully argue that U.S.-style documentation is needed—because that language is what the U.S. courts (or U.S. arbitrators) are used to inter-

2. Claire A. Hill, *Why Contracts are Written in "Legalese,"* 77 CHI.-KENT L. REV. 59, 60–61 (2001) [hereinafter *Legalese*]; Claire A. Hill & Christopher King, *How Do German Contracts Do As Much With Fewer Words?*, 79 CHI.-KENT L. REV. 889, 890–93 (2004).

3. Hill & King, *supra* note 2, at 890–93.

4. *Id.* at 902.

5. This issue is reminiscent of the linguistic literature by scholars such as George Lakoff regarding the ways in which a debate is framed. See, e.g., GEORGE LAKOFF, *DON'T THINK OF AN ELEPHANT: KNOW YOUR VALUES, FRAME THE DEBATE* (2004).

6. Carole Silver & Mayer Freed, *Translating the U.S. LLM Experience: The Need for a Comprehensive Examination*, 101 NW. U. L. REV. COLLOQUY 23, 24–26 (2006), <http://www.law.northwestern.edu/lawreview/Colloquy/2006/3/>; see also Carole Silver, *Internationalizing U.S. Legal Education: A Report on the Education of Transnational Lawyers* 10 (Berkley Electronic Press, Paper No. 942, 2005), available at <http://law.bepress.com/cgi/viewcontent.cgi?article=4247&context=expresso>.

preting.<sup>7</sup> This is a view I have critiqued elsewhere—there is a lot to this view, but it's not nearly as powerful or dispositive as its proponents believe it to be—but it does have some power. Thus, the arms race begins and continues. Soon enough, even in purely domestic contracts involving only Latin American parties, the longer U.S.-style contracts become the norm.<sup>8</sup>

My first conclusion is this: notwithstanding the resources and intelligence thrown at sophisticated transactional contracting, it is apparently quite difficult for the documentation and contracting practices of complex business transactions to be first best, either in the U.S. or in Latin America. Indeed, in the U.S., there are ways in which second best is actually pretty good. Because of the broader system in which transactions arise, the documentation serves some important and useful functions: helping firms maintain a hiring process in which they can't tell who will be good, but even not-so-good quality lawyers can be useful and better quality lawyers will become visible as such. It's very hard to tell at junior levels who will be a good lawyer; the documents from previous deals that are used as forms can be modified even by people who don't understand the forms exceedingly well, but those who do will do a better job and will be noticed doing so.<sup>9</sup> Moreover, the U.S. needs the type of documentation it has because interpretive practices and conventions create norms, deviation from which may yield inferences as to what a contract means and as to the effectiveness of a lawyer in her representation of her client. In addition, the U.S. is "mechanically" geared up to have the types of contracts it does. The documents already exist on firms' computer systems, and the people involved are used to working with them. None of these reasons or rationales is present to nearly the same degree, if at all, in Latin America; on the merits, the case for U.S. documentation and practices in Latin America is worse than it is in the U.S.

Many questions arise from the foregoing. In this commentary, I want to raise just a few: How will differences among Latin American countries affect the way contracts for Latin American transactions using U.S. documentation are written? How will contracting practices be affected more broadly? The more that is covered by the contract, the more that is potentially open for negotiation. Will the U.S. norms in which "everything" is negotiated be imported along with the contracts? If so, how will this affect the relationships among transacting parties? Will parties become less trust-

7. Critically, contracts increasingly contain arbitration provisions. Who the arbitrator is will depend on the parties and on the governing law of the agreement.

8. *Legalese*, *supra* note 2, at 75; Hill & King, *supra* note 2, at 902.

9. See *Legalese*, *supra* note 2, at 77–78.

ing, for instance? Or will parties become more trusting, as they can specify more precisely their expectations of one another's conduct?

In this regard, the elaborate specification of what is prohibited in U.S. contracts may have led to an ethos which effectively encourages coming "close to the line." For example, if related party transactions are prohibited and a highly detailed definition of "related party" is included in the contract, some may view this language as sanctioning dealings with a party that doesn't technically meet the description but might, in some common sense manner, be regarded as "related."<sup>10</sup> Will this effect also be imported?

Some broader questions should also be raised. In *How Do German Contracts Do As Much With Fewer Words*, my co-author and I argued that homogeneous transacting communities consisting of frequent repeat players may be a necessary precondition for shorter, less extensively negotiated contracts.<sup>11</sup> To what extent does the increasing globalization of markets and transactions, and increasing heterogeneity among transacting parties, make U.S.-style contract documentation inevitable, or at least likely to be adopted in any event? One argument made in the U.S.—an argument we criticize in the *German Contracts* piece—is that because the U.S. potentially involves fifty separate state jurisdictions, more of "the law" that is wanted must be contained in the document.<sup>12</sup> Such an argument may have more plausibility as a transaction document comes to be more of a form for transactions among parties in different countries.

Finally, what determines which types of documentation and transacting practices become dominant? The correlative question is being asked in the sphere of corporate governance, where U.S. and European models sometimes compete, but also sometimes converge;<sup>13</sup> the question has been

10. See Hill & King, *supra* note 2, at 901; see also Claire A. Hill & Erin A. O'Hara, *A Cognitive Theory of Trust*, 85 WASH. U. L. REV. (forthcoming 2007).

11. See Hill & King, *supra* note 2, at 925–26.

12. There, we said:

We are a bit skeptical about the importance of fifty different states' laws, and the need to rebut particular common law doctrines. In our experience, many of the types of provisions that are longest in U.S. contracts are the ones as to which the law will typically honor what the parties agree upon, and there is no applicable common-law precedent.

*Id.* at 924.

13. See, e.g., Lucian Arye Bebchuk & Mark J. Roe, *A Theory of Path Dependence in Corporate Ownership and Governance*, 52 STAN. L. REV. 127 (1999); Brian R. Cheffins, *Current Trends in Corporate Governance: Going from London to Milan via Toronto*, 10 DUKE J. COMP. & INT'L L. 5 (1999); John C. Coffee Jr., *The Future As History: The Prospects for Global Convergence in Corporate Governance and Its Implications*, 93 NW. U. L. REV. 641 (1999); Ronald J. Gilson, *Globalizing Corporate Governance: Convergence of Form or Function*, 49 AM. J. COMP. L. 329 (2001); Jeffrey N. Gordon, *Pathways to Corporate Convergence? Two Steps on the Road to Shareholder Capitalism in Germany*, 5 COLUM. J. EUR. L. 219 (1999); Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439 (2001); Brett H. McDonnell, *Convergence in Corporate Governance—*

far less explored in the context of transacting practices. Do we have the conditions for true competition among models? My guess is that we do not. If the trajectory is influenced by something other than efficiency, what are the determinants of success? Is more convergence possible, or even desirable? These questions will become more pressing as markets globalize further.

