Rahim Mohtaram
Rob Howard

International Sales Contracts

An Issue Spotting Manual for International Traders

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Rahim Mohtaram, Ph.D., MBA, CITP FIBP®, CIFFA, CCI, FIATA

(rahim.mohtaram@gmail.com)

linkedin.com/in/rahim-mohtaram

Rob Howard, J.D., BComm International, CITP FIBP® -

(robhoward@intbizpros.com)

www.linkedin.com/in/rob-howard-law

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INTERNATIONAL SALES AND PURCHASE CONTRACTS

Introduction – Who Is This Book For?

This book is meant to serve as a reference for those of us that work in international business but may be too busy to memorize all of the nuances that combine to make up international contracts. It's a reference book to assist the reader in issue spotting and to help identify potential conflicts early in the process. The book is not necessarily meant to be read cover to cover and it can be used as a reference to whatever individual sections you may want to use it for.

Nothing in this production is meant to be specific legal or financial advice applicable to the reader's individual needs. For that, please reach out to the authors directly as we would love to discuss your projects in more detail.

What Exactly Is An "International" Contract - And Why Does This Distinction Matter?

In short, it affects which set of rules might be applied to a contract. This is because different legal systems have different criteria for interpreting what a contract means.

So, when then does a contract count as "international" for purposes of determining which set of rules will apply to that contract? Frankly, it's complicated. All contracts are inherently tricky, and they invariably become more complicated when dealing across multiple legal systems.[1]

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1. This shows one reason that working with a competent lawyer is important in working with international contracts.

In this book, for simplicity, we assume that the contract is "international" if it involves a sale between parties located in two different countries.[1]

STRUCTURE OF A SALES CONTRACT

What General Aspects Should Negotiators Talk About First?

All international contracts generally involve some combination of **(1) technical**, **(2) commercial**, **(3) financial**, and **(4) legal** aspects. How then, do we know which ones to focus the parties' attention on first?

The most common (and avoidable) errors that we've witnessed as negotiators have often been related to a general lack of structure in the discussions leading to wasted time. Having a logical sequence of talking points and priorities up front can help us to avoid the need to "renegotiate" items that were initially agreed upon based on previous assumptions that were misunderstood.

For example, imagine that we start negotiations by defining a product's technical specifications, and then agree on a price, and then afterwards the parties realize that there was a misunderstanding as to whether a warranty was included. The seller says that the agreed price did not include a warranty while the buyer says that they assumed a one-year warranty was included. The seller then states that the price would have to change to reflect this new warranty commitment.

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1. While there is unfortunately no universally applied definition of "international" in determining when a contract is international, there are norms that are often applied internationally as a baseline. Often, legal systems will consider common factors including the "place of business," the nationality of the parties involved, and (in some situations) when the goods are transferred across more than one country. This subject is addressed in article one of United Nations Convention on Contracts for the International Sale of Goods (UNCISG). Article one of United Nations Convention on Contracts for the International Sale of Goods (UNCISG) seems to suggest that the main factor for defining a contract as international is the "place of business" factor.
To further complicate matters, some countries simply don't follow the "norms" as applied by the UNCISG and some contracts explicitly exclude the UNCISG definition in the contract (often in the Governing Law article).

Then what happens? We must circle back and agree on the details of the warranty and then again talk about the price. These are non-necessary repetitive negotiations that could have likely been prevented if we had drafted a proper agenda for the meeting.

The details of this issue will be discussed in the negotiation chapter, and I will present a structure based on my personal experiences, but as general advice, follow the below sequence in your negotiation meetings:

1. Technical aspects
2. Commercial aspects
3. Financial aspects
4. Legal aspects

Side note: We know many lawyers that would disagree with the above sequence and believe that the very first stages of the negotiation should be spent on the legal aspects of the deal (…shocker that lawyers might feel that way). Their reasoning does have some merit in the sense that, without an agreement as to something as fundamental as the contract's Governing Law (meaning an agreement as to which set of laws will apply to everything in the contract), we simply can't determine anything else in the deal without that part being established.

To some extent, their reasoning here is correct, but it's also important to consider that we are businesspeople trying to do get a deal done, rather than lawyers who are being paid for their opinions on being risk averse. If we start by discussing potentially contentious legal issues up front then (1) it might distract from the substance of the deal, and (2) negatively affect the tone of negotiation right from the start. This is one example of why businesspeople are sometimes reluctant to bring lawyers into a deal and how lawyers have gained a reputation as being bad for business by "blowing up" otherwise high-potential collaborative deals.

Which Articles Should Be Negotiated First?

In which order do the articles of a contract generally appear?

While (perhaps unsurprisingly) there's no on-size-fits-all model for the order in which a contract's articles should appear in the text, I generally expect a contract to follow a sequence similar to this one:

Suggested Sequence of Articles in a Contract			
Number	Description	Number	Description
1	Title of the Contract	12	Retention of Title
2	Parties	13	Contract Documents
3	Goods Sold	14	Force Majeure
4	Price	15	Cancelation/ Termination
5	Incoterms Rule	16	Consequences of Termination
6	Payment Conditions	17	Liability for Delay
7	Time of Delivery	18	Liability for Non-Conformity
8	Transportation Details	19	Applicable Law
9	Shipment Documents	20	Dispute Settlement
10	Inspection of the Goods	21	Miscellaneous
11	Languages and Notices	22	Signatories and Copies

Table 1: Sales Contract Articles

We usually start with the preamble, then continue with a section on the goods/services, and then continue to the miscellaneous articles. Most professional negotiators and lawyers prefer to write legal articles such as governing law and dispute settlement at the end of the contract.

The sequence of the articles generally has (relatively) little influence on the substantive terms of the contract, but when you draft your agreement in a familiar format it's easier to follow and generally comes off as more professional.

Specific Articles Within a Contract (and what they mean)

PREAMBLE

In this section, we introduce the who, what, where, when, and why of the contract. It's the background of the contract and should tell us what the parties are attempting to accomplish. It seems simple, but if not done correctly can lead to inaccuracies and ambiguities that create avoidable conflicts later. An example of this could include naming a similar but incorrect entity in the contract. Another could be if a Limited Liability Company were to forget to add the letters LLC when identifying themselves (which could mean they lose their entire limited liability protection).

Title

A contract's title is important because it can be used to interpret the original intention of the parties. So rather than naming the document something basic like"Contract" or "Agreement," it helps to be more specific. By using a title like "SALES AND PURCHASE CONTRACT" we are more clear about the nature of the contract.[1]

Parties' Introduction

Understanding and naming the specific entities that we are dealing with can tell us a lot about our counterparties in revealing ways that may not have been initially understood. Sometimes companies will use multiple entities to help shield themselves from liability (which is usually not illegal). It's important to understand though, that the operating company for which you are contracting with, for example, may or may not be the entity that owns the intellectual property that you think it does, or the building in which the office is located, or even have any assets at all for that matter.

1. There are more than 200 types of contracts in international business and each has its own name.

For this reason, it's not uncommon in contracts to see a seemingly unnecessarily long combination of words used to identify the parties. The parties should be introduced precisely and should generally include the following items:

- Legal name
- Abbreviated name (if any)
- Nationality (as in where the counterparty company is organized)
- Type of organization (LLC, Corporation, Partnership, Sole Proprietorship)
- Registration number
- National and industrial numbers (VAT, EXIM, BN, unique license numbers);
- Date of registration

Additional Important Points in Preamble:

When writing this section, pay attention to the following points:

- Do not translate local names to the English language.
- Do not write abbreviated names without writing the full names.
- If dealing within a foreign set of laws (Governing Law) as it pertains to different corporate entities, it helps to search the local Business Code for context regarding the counterparty's corporate structure and how that may affect your deal.1
- Watch for recent and/or future changes in registrations to corporate structures. Require that counterparties inform you of any changes within a certain period of time should they happen.
- Add the registration information of all parties as attachments to the contract. If you want to go one step further, you might even request that your counterparty file the documents with the local chamber of commerce and/or your country's embassy.

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1. For example, in a Turkish contract it may be helpful to understand the differences between "private stock companies" and "limited liability companies" under the Turkish rules.

- If special government licenses are required to fulfil a counterparty's contract obligations (like an FDA license in the US) and your counterparty claims that they have those licenses, you can require them to include that license information in the contract and attach a certified copy.

Contact Information:

Contact information for each party should include a legal domicile address, principal place of business, telephone and fax number, email address, website, and the appropriate legal authorized representatives for each party.

Domicile address and place of business information is especially important in international contracts because this might affect which country's laws apply (Governing Law) and how disputes will be settled (dispute settlement procedures). Domicile information for a specific contract can be easily misunderstood when we are dealing with a company that has offices in multiple countries.

Notice should be required by all parties if there are any changes in their address.

Email correspondence should be done through addresses that are written in the contract and/or can be easily attributable to the company. For example, email addresses look something like abc@companydomain.com or any other address legally related to our partner. We should not correspond to general email addresses (such as abc@yahoo.com or abc@gmail.com) unless they are specifically introduced in the contract. This is because we need to be able to show that our correspondence with these emails can be attributed to your counterparty that they had reasonable notice if future problems arise.

Role in the Contract: (Buyer or Seller)

After detailing the registration and contact information of the parties, we usually assign a name/term to each party based on their role in the deal and the nature of the contract. For example, in a sales and purchase contract, the parties would likely be labelled something like "Buyer" and

“Seller” for obvious reasons. In a Sales Contract, it may not be correct to write "Manufacturer" and "Distributor" as the parties' roles.

Notice how the first letter of these terms have been capitalized. Capitalizing the first letter of a term in a contract generally means that the term has been defined somewhere else in the contract.[1] In this case, the Buyer and Seller have each been defined earlier by their full names.

Notice also how we include a "the" before the name/term/role in all sections of the contract text. Using a “the” means that we are referring to a specific Buyer or Seller that is unique to what we are talking about.

If we don’t label the parties by their function and instead chose a generic label like “Party A” and “Party B.” This is generally poor practice as the terms are ambiguous and can lead to confusion later in the agreement about which party is which.[2]

Current Business:

In this section, we can define the “main business” of each party such as manufacturer, distributor, wholesaler, or any other type of economic activity they may claim to be in. This can be helpful because we can use this opportunity, for example, to require that our counterparty commit in writing that they are in fact the actual manufacturer of a product and not an intermediary (which may presumably be a less desirable party to negotiate with). This information regarding an entity’s “main business” is a kind of representation and if a counterparty is unable to commit to this in writing then that provides us with some additional context on the deal.[3]

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1. As a general principle, it’s usually a good idea to read the corresponding definition anytime that you see a capitalized term by cross-referencing it in the “definitions” section of your contract. A lot of what specialist contract lawyers spend their time arguing about is related to how terms are defined.

2. If for whatever reason it is necessary to use the terms "Party A" and "Party B," then I always write my client as the first party (Party A) and myself as the second party (Party B).

3. If our counterparty were to provide us with misleading information on this point, then there could be consequences related to possible misrepresentation.

Authorized Agent in This Contract:

A contract needs to be signed by a legally authorized person within each company that has been officially granted the power to sign a contract on behalf of a company.

In this section we include the authorized agent's full name, legal position in the company, and (especially for international contracts) some kind of national ID, passport number identifying each party, or some kind of a proving document number). At this point, we are informed as to the official title and organizational position of the person who is signing the contract. Depending on the contract, a signatory might be a high-ranking manager type or a member of the board.

Often, contracts will include specific writing that requires each signatory to warrant that they do actually have their company's official authorization to enter into this type of agreement.

Joint and Several Liability

Joint and several liability is a legal term meaning that responsibility is shared between two or more parties. It generally means that a harmed party may sue any or all of the (jointly and severally liable) parties for the entire amount owed.

Whereas Clauses

In this part of the preamble, we write the overarching objectives of the parties for participating in this contract.

Now Therefore Clause

In this clause, all the parties officially announce their intention to execute the contract and to be bound by its terms.

Example of a Preamble:

SALES AND PURCHASE CONTRACT

PREAMBLE:

This contract is made on this ___day of _______2021 by and between ------ CO., LTD, located at No … Road ,… with registration no. ---- hereinafter referred as the" Seller"; represented in this act by ------ as director manager of Seller Company as per document number ---------- dated ----------- attached to this contract as annex number ---, being the duly authorized signatory on behalf of the above-mentioned company

and

------ CO., LTD, located at No … Road ,… with registration no. ---- hereinafter referred as the" Buyer"; herein represented in this act by ------ as director manager of Seller Company as per document number ---------- dated ----------- attached to this contract as annex number ---, being the duly authorized signatory on behalf of the above-mentioned company.

WHEREAS, seller, which is a ---- company existing under the laws of -------- and involved in the production and manufacturing of --------------, desires to sell the Products of this contract to the buyer,

WHEREAS, the buyer is a ----- company established under the laws of ---- and involved in trading and marketing of --------------products, accepts to purchase the Products under the terms and conditions stipulated in this contract;

NOW, THEREFORE, in consideration of the mutual covenants contained herein, the parties hereto have agreed to execute this contract as per the following terms & conditions.

The Articles Related to Technical Aspects

Product

Writing the product and its related details are crucial in sales contracts. Many aspects of the product should be defined precisely and accurately to avoid nonconformity and future problems. If the description or specifications are not written correctly, parties may encounter misunderstandings and conflicts.

The following details should be noted in writing this article:

Description

A product description should be written accurately enough to sufficiently describe the products that we are contracting for. This description itself needs to contain a minimum level of specificity and detail for it to be useful. For example, a generic description of "table" for the product could mean many different types of tables. Instead, we could include some some additional details on the function of the table to improve our accuracy (coffee table, kitchen table, computer desk, etc.).

Quantity – units of supply and partial shipments

Quantity details specified in the contract include how we define our units of supply, whether we accept partial shipments, and how partial shipments might affect any scheduling and/or payment details.

Quantity is usually defined as units of supply based on whatever is common in the industry. For many products the unit is counted based on pieces or numbers. For some others, it might be litre, kilogram, cubic metre or foot, etc.

In addition to defining the units, whether or not partial shipments are acceptable should also be agreed upon by the parties. These details could include either a minimum and/or maximum of each shipment or possibly a determined quantity for each shipment.

Note that if a buyer agrees to allow for partial shipments without further details, then those partial shipment details are usually just decided on by whatever is most convenient to the seller. In other words, the seller usually decides in the case that this is not explicitly agreed upon by both

parties. If the seller sends one piece, the buyer is obligated to pay for that one piece, and if the seller chooses to ship all the products in one shipment, the buyer might have to pay the total amount.[1]

When partial shipment is allowed, it's helpful to define the way that affects how payments should be made. A typical solution is for the payment to simply be proportional.

In some exceptional cases, such as with a revolving documentary credit arrangement, the parties can agree that order fulfillment is either cumulative or non-cumulative. If they agree that the orders are cumulative, and if the seller is not able to send a specific shipment at the agreed time, then the seller probably has the right to simply double the quantity for the next order. If the orders are non-cumulative, and if the seller does not send one shipment at the right time, that previous order quantity cannot simply be sent along with the next order(s).

Quality

Depending on the nature of the goods and the parties' expectations, one or more of the following criteria might be used to determine what makes a product's quality contractually acceptable:

Defining a Quality Standard:

Standard is a contractual term used to define an acceptable quality metric for a product. When we define a minimum specific quality standard in a contract, we can clarify what the seller is expected to deliver in conformity with that standard.

Often, products are subject to some form of local quality regulation and/or mandatory standards that can also be used to define a minimum acceptable quality standard for a wide range of products. The criteria and test method for each criterion are often defined by a country's local authorized organizations. For example, we might select "DIN" as a

1. It's typically good practice to have the parties agree on a shipment schedule ahead of time.

German standard or "JIS" as a Japanese standard for a wide range of products.

When defining a product's minimum acceptable quality standard, we also need to specify the number, kind, and version of the standard. For example, "EN 60335 version 2014" might be used for gas compressors, where "EN" is a type of European standard, "60335" is the identifying number of the standard, and "2014" is its version.

Defining a Quality Inspection Procedure:

After defining whatever quality standard we intend to use, we need to define an appropriate inspection procedure for determining whether that standard has been met.

In most countries and situations, an independent testing entity or inspection agency is used to inspect the quality before it ships. After testing the product, that independent inspection agency issues a certificate of inspection or verification of conformity based on some kind of test report. These inspection reports are then delivered on an accredited laboratory letterhead in preparation for shipping.

More explanation on these documents can be found in the "Shipment Documents" section of this book.

Certificates of Analysis and Related Documentation

For some highly scrutinized products, like consumables or chemical products, we will likely need to include some additional quality documentation. This is usually up to the seller to provide by issuing something like a Certificate of Analysis for their products.

The Certificate of Analysis includes different information such as ingredients and/or formulation of components of a given product. Some additional documents like "Mill Test Certificate" (MTC), "Technical Data Sheet" (TDS), and "Analysis Certificate" (AM) might be used in different industries such as the chemical, metal, or grain industry.

As an example, the following specifications may be used for rice.

11---- Rice (---- COLOUR)

- Min. average precook length in mm(L): 7.85
- Min. average precook breadth in mm(B): 1.7
- Min. L/B ratio: 4.25
- Max. moisture content: 11.5%
- Max. damaged discoloured grain: 1%
- Max. chalky grain black kernels: 2.0%
- Max. broken & fragments : 1.5%
- Max. foreign matter: 0%
- Max. other grain: 5%
- Max. under milled & red striped grain: 3.5%
- Max. immature grain: 1.5%
- Max. paddy grain: 0%
- Max. elongation ratio (after cooking): 1.5
- Max. green grain: 0%
- Max. red grain: 0%
- Max. black grain: 0.3%
- Max. yellow/amber grain: 0.5%
- Purity: 80%

Size as a matter of quality control

Specifying and evaluating product dimensions for size (length, width, and height) can be a crucial aspect of quality control in a contract and needs to be specified here. Product dimensions can affect price, end use, logistics, and customs classifications.

Industry examples of how dimensional specifics are crucial could include engineering products that built to a certain spec, wood products that are built to fit together under certain dimensions, and food products like pistachio nuts for which their value may vary based on their size.

Logistically, measurements affects stuffing, loading, and discharge. We also need an exact size for requesting a quotation on freight, especially in air transport.

Customs classifications may vary depending on dimensional specifications. This may change the product's tariff code, customs value, and import duty rates in different countries.

Even one-millimetre of disconformity to dimensional requirements might change the whole deal. For this reason, it's helpful to specify dimensions in the contract. This may mean including specifics on inner dimensions, outer dimensions, and any variation due to packaging requirements.

Weight

Net weight, gross weight, and the method that weight is measured needs to be specified in the contract. Weight can be used as a metric to calculate quantity and also used as a qualitative measure.

In some contracts, a price may be quoted based on weight. For example, most metals are priced for each Kilogram, pound, or metric ton.[1]

The method of measuring the product's weight also needs to be decided in advance. One way is to simply use a scale (assuming the nature of the product allows for that). If using a scale is not possible (for example, if dealing in high tonnage bulk commodities) then traders sometimes use a method called a "draft survey."

In a draft survey, inspection companies calculate a shipment's weight by loading it onto a ship and calculating the amount of water that has been displaced by a ship after adding the additional weight. This method requires a fair amount of estimation, and therefore often has a some amount of tolerance for inaccuracy built into the calculations. For this reason, this method is usually done by neutral third parties such as inspection agencies. Note that it is generally not a good idea to authorize a shipping company as the third party for such an activity, because weight is directly related to the shipping company's own obligations.

1. Never forget to write "Metric Ton" in case you are using ton as a unit of weight, because there are three types of Tons. A Metric Ton=1000 Kg, compared to a Short Ton= 907.19Kg (North American system), compared to a Long Ton= 1016.05Kg (British system).

Some products like petrol may have some degree of ordinary loss in weight or regular leakage. Even though the goods' gross and net weight should be determined in the contract, in some products like commodities, a given percentage of variance is usually acceptable (+-0.05).[1]

Defining Packaging

Product packaging can affect many different aspects of a sales contract including preventing physical damage to the product during transport, logistical considerations, marketing, and how customs categorizes the product.

It's helpful to contractually define the packaging as exact as possible, especially for delicate and perishable products, by including various details and specifics about how the product should be packaged. The responsibility for appropriately packaging the product often falls on the responsibility of the seller, but these details should really should be defined in the sales contract by both parties in advance. Packaging details to agree on could include how many layers of packaging will be used, different packaging types, materials, specifications, marking, and how to label the packages.

Packaging Layers

When a product is sold to an international customer, it may have a few layers of packaging. For example, toothpaste is packed in a tube, then each tube is put in a paper box, then 12 paper boxes are packed in a small carton, then 24 cartons are placed in a bigger carton, then 32 big carton boxes on a wooden pallet, then the pallet is wrapped by a plastic cover, and then finally, it is all sealed by three plastic belts on the plastic sheet. As another example, toothpaste may be packed in an intermediate bulk container without any other packaging. Each layer may affect the

1. This is based on article 30 of uniform customs and practices for documentary credits (UCPDC 600). It's not unusual for contracts to include language like "about" or "approximately" when describing weight.

finished cost, and all these layers should be defined in a packing instruction.

Packaging Types

Different packaging types are available. In the example above, layers of packaging for toothpaste could include tubes, boxes, and pallets. The packing material and its technical specifications, such as size, density, and moisture, should be defined. Some of the many types of packaging are listed in the following table in alphabetical order.

Packaging Types			
Number	**Description**	**Number**	**Description**
1	Bag and Sack	11	Drum
2	Bale	12	Pail
3	Barrel	13	Paper can
4	Box pallet	14	Plastic can
5	Bundle	15	Pallet
6	Cage	16	Post Pallet
7	Can/Tin	17	Roll
8	Carton	18	Tube
9	Coil	19	Two-Way Pallet
10	Cylinder	20	Wooden Box

Table 2: Different Packaging Types

Packaging Labels

Marks, labels, and signs on the packaging related to stocking, protecting, handling, or using the product should be indicated on the different layers of a product. If a product may be categorized as a “hazardous material” under the International Maritime Dangerous Goods code then a standard label should be included on the product in all angles of the packages.

Using ambiguous and qualitative expressions such as "Export," "Suitable," "Seaworthy," "Reinforced" for packing is a common mistake in defining packaging requirements within a contract.

Packing often constitutes a considerable portion of the finished cost of a product. Write exact packaging instructions as an article or an attachment to your contracts. Do not assume that the seller knows and is willing how a buyer wants the product packaged. Some vendors may decrease the quality of packing to reduce the prices.

Packaging and Customs Agencies

Packaging may also have an effect on how customs agencies treat your shipment and may affect areas like tariff classification, customs valuation, weight calculation, and import/export licenses.

Country of Origin

Country of Origin is a metric that essentially indicates where the product was made and is classified based on a series of different calculations.

In a world with global supply chains and free trade agreements, this metric basically tells customs agencies where the goods are coming from. It involves a series of calculations and rules based on how much of a final product was made in a specified country. A product from China imported into the US, for example, is treated differently by customs than a product from Canada partly because Canada is a party to the USCMA trade deal and therefore usually has more desirable trade treatment by the US. Country of origin is essential in determining tariff treatment, customs valuation, and other customs compliance issues.

Country of origin can also be important for marketing purposes as the end user may perceive imported products from one country to be more desirable than another. For example, our customers may be looking to purchase crystal dishes that were made specifically in the Czech Republic.

This metric is especially important to specify when dealing with trading companies that may be purchasing their product from a broad range of countries.

Parties can explicitly specify country of origin requirements for their products in a contract. To further protect themselves, we can request a "certificate of origin" stating where the product originates.

HS Code

HS codes are used by different customs agencies to classify products using a standardized international system. Each product has a code based on the Harmonized System of Coding and classification that ranges from 6 to 12 digits. This code affects customs clearance and import license issuance. This code should conform to the description of goods and is usually determined by specialized experts like licensed customs brokers.

Product Code

In some industries like auto parts, each product has a unique product code. Where applicable to our industry and products, it usually a good idea to specify this product code in our contract. This code will be a combination of letters and numbers.

Year of Production/Crop Year

Specifying the year of production or crop year is essential in some industries, like grains or automobiles, because this can change the perceived quality of the product. Depending on the product, we might prefer that it be manufactured in a specific year.

Where practical, some products (like tires for example) may have their date of production indicated right on the actual product. The consumer is shown the exact year and maybe even the week of production.

Some products might have a limited shelf life. For these products it's especially important to confirm a production year so we can know that product isn't passed its prime. For example, an implant might have a total shelf life of five years, and we can contract to only purchase products with at least four years of shelf life remaining.

The automobile industry provides another example of how a product's year of production (model year) affects its perceived value and its marketing. This is why the car's model year is always mentioned in the associated sales and purchase contracts. Further, depending on the

month, a brand-new automobile might be sold cheaper in the second half of each year.

If the purchaser is intentionally contracting for a model that was made in a previous year, it should be clear whether the product's condition is used or unused. We might be dealing with an older albeit unused product that was simply stocked in a warehouse for a while, or a used product that is now second-hand.

Some traders may prefer to purchase the used or older products if they believe there is value there. In those cases, it's especially important to collect the proper documentation for determining the year of production. These documents should be included in the article entitled "shipment documents," and it's usually the seller's responsibility to deliver that information.

The Performance or Guaranteed Figures

Performance and guaranteed figures is a contractual way for a buyer to be assured that a product will perform to a certain standard. If a product's real performance does not conform with this standard, then the seller can be deemed liable for damages.

When a party purchases a set of machines, certain performance factors such as capacity, energy consumption, inputs, and outputs should be guaranteed during the warranty period or throughout the optimum life of the device. A buyer's engineers and their technical team usually calculate these factors. These are often specified in the contract as an article or included as an attachments of the agreement.

Three typical factors of machine performance are production capacity, inputs, and outputs. For example, when you purchase a small-sized power plant compacted in a 40feet container, you expect it to consume a given amount of gas, produce a specific amount of electricity, and need a determined period for maintenance each year. If the actual gas consumption is more than the agreed quantity or the electricity production is less than the agreed amount, the buyer may lose money, and the seller could be held liable for damages.

The details of this article may vary based on the specific product and industry. Having a professional technical team is crucial for writing this section of a contract. In some situations, there may be dozens of specialized pages added to the agreement as an enclosure, annex, attachment, or schedule.

Technical Supports

Generally, this article refers to after-sales service, including the designing, installing, erecting, testing, commissioning, exploitation, training, spare parts provision, and proper management of a product.

These technical support details are often attached to contracts and may be priced separately in addition to the main product. In most contracts, the buyer withholds some amount of money as performance or good performance retention. In some other situations, the seller may insist on receiving payment for these technical support services in advance. In that case, the buyer may protect themselves by requesting a performance bank guarantee, good performance bank guarantee, or even standby letters of credit.

The buyer's technical team should anticipate their ongoing requirements for technical support early in the negotiation process. If the goods are expected to require technical support, all those related details should be clearly indicated in the contract.

Brand

If the goods are expected to be produced under a specific brand name or trademark, that should be specified in the contract.

If the brand is introduced by the buyer, then it should also be registered, and the buyer should legally be the owner of the intellectual property (or at least have a valid license or authority from the original owner of the brand). If the brand is introduced by the seller, it should be authorized to use the brand name.

Unfortunately, some traders may use unregistered brands, or the brands of other companies, or even fake brands. This issue should be reviewed by intellectual property and legal experts to avoid potential conflicts.

Intellectual property registered in one country often doesn't mean that your product maintains that copyright for the same goods exported into another country. For this reason, it is recommended that we explore what is involved in registering our brand in the countries where we plan to send our export. As a starting point, this registration can be done based on the Madrid Protocol for protecting our trademarks.

If we are signing a supply contract with a manufacturer, we should explicitly indicate that the supplier is not entitled to use our brand or logo for any other customer.

Commercial Aspect Articles

Date of Delivery

The date the product needs to be delivered is usually a seller obligation. Delivery date can be as specific as a particular hour or may provide a window for the seller to complete delivery. For example, we might contract for a very specific delivery time such as the 10th of January 2020 at 22:30 am at the XYZ airport. A buyer might also allow for delivery to fall between a less narrow window such as between the 10th and 15th of January.

In the case that delivery is delayed, the seller may be liable for damages. This could include consequential damages that could have been foreseeable to the seller at the time of contracting. In some cases, the parties might allow for a grace period in which delays are tolerated without penalty.

Sales contracts are typically not intended to create an ongoing obligation over a longer period of time compared to other contracts like agency contracts or distributorship agreements that might be valid for a year or more extended periods.

Shipment or Transportation Details
Departure:

This items defines where the goods will be shipped from. In some Incoterms rules such as EXW and FCA, this item is especially important because the Buyer should take care of logistics from that point. In the Incoterms CFR, CPT, CIF, and CIP the departure location might represent the place where liability for damage shifts from seller to buyer.

Mode, Route, and Destination of Transport:

Here we specify how and where the shipment will be transported.

Typically, the buyer chooses the destination and then its up to the seller to consider some kind of suitable packaging, the transport mode, and the route to the chosen destination. These details might affect freight charges, transit time, risks associated with transportation, and even rules and regulations governing the importation and exportation clearance.[1]
Example: Imagine that a buyer purchases 15,000 laptops from a company in California for import into Canada and the parties simply defined their Incoterms as CPT Ottawa, Canada. This is ambiguous to a few important details including the requested mode of transport (road, rail, air, multimodal, etc.), which US/Canada border crossing should be used, and where the final destination in Ottawa should be. Based on CPT rules, if these details are not specified contractually, then the seller usually can usually just chose whatever is in their best interest.

Transshipment

Transshipment generally refers to when a shipment's vessel is changed before the shipment reaches its end destination. This can happen due to a variety of legitimate reasons related to technical, economic, and cargo insurance considerations.

1. For example, if a shipment is going to be cleared under the NAFTA/USMCA rules into Canada, then customs may have some particular shipment requirements under the agreement which should be looked into.

Some shipments pass through large hub ports around the world on large ocean ships that can carry thousands of containers at a time. Larger ships will often be so big that they have a water draft that outsizes the depth of smaller ports. Even if the depth of the port was sufficient to handle these larger ships, it would not be economically feasible to send a 22000 TEU container to a port with the purpose of unloading a mere eighty TEUs.1 For this reason, these larger ships might unload thousands of containers at a time with the expectation that those containers will be loaded onto smaller "feeder" ships. Those smaller vessels can then distribute those shipments through a network of smaller ports. This process is known as transshipment.

The place of transshipment, the period that the goods will be kept at the intermediary port, and the costs and effects on tariff treatment can be specified under this article.

Partial Shipment

Partial shipment refers to delivering one order in two or more shipments. If the seller is entitled to do so, the parties should indicate it in the contract and define the details.[2]

Means of Transport

The means of transport article generally refers to the specifications of the vessel required to transport the product.

This could refer to factors like the age of the vessel, classification certificate, fuel consumption, whether the vessel is geared or gearless, the flag of the vessel (as in where the vessel is registered), and other

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1. Twenty feet Equivalent Unit
2. See previous section on Partial Shipment for more details.

details. Most of these issues affect transit time, cargo insurance, and the risks that threaten the product during transportation.[1]

As an example, in the transport of livestock via roads, we might need to specify what type of truck is appropriate for transporting live animals.

Container Type and Spec

Containers are often categorized into types based on size, application, and material. If a shipment requires a container, the container type should be determined in advance.

Specifying container details is especially important if the container is not a general purpose (GP) container. Some containers called “reefers” (or refrigerated units) have unique functions like temperature control or special stuffing requirements . Another type of container related to dangerous goods (DG) might be used for hazardous materials such as inflammable solids and liquids. In other situations, a shipment might be overweight and require parties to use heavy-duty (HD) containers.

The size of the container should also be agreed upon contractually. For example, some countries might be used to dealing in 53ft containers, while other countries might not readily have suitable equipment (like spreaders and gantry cranes) to handle these containers.

An example of an avoidable mistake might involve a seller shipping their product in two 53ft containers while the buyer is expecting to receive three 40ft containers at the destination.

Loading and Discharge

Loading and unloading are important considerations because a majority of any possible damage to the goods while in transit usually happens during these loading and unloading stages.

Depending on the route and possible transshipment requirements, the cargo may need to be loaded and unloaded a few times. Loading and

1. Furthermore, when the seller is responsible for marine transport such as in CFR and CIF, it is suggested that the buyer specifies the type of the ship, whether it is liner or tramp.

unloading specifications are usually especially important to define when dealing with bulk, overweight, and oversized products.

Loading charges in the ports are usually referred to as Terminal Handling Charges at the Port of Loading (THC POL), and it includes lift on, movement on the dock, and loading on the vessel. If the agreed place is a port, clearing the goods from customs requires unloading the products from the vessel and paying the THC of the port of discharge.

While incoterms are generally meant to determine the details of the allocation of risks and costs, it's good practice to specify the details accurately and not to rely on the generic incoterms rule.1 Great attention should be paid to loading costs and risks in EXW, FCA, FAS, FOB, CPT, and CIP, and we also should be careful about unloading in CFR, CPT, CIF, CIP, DAP, DPU, and DDP. Based on DDP, the buyer is responsible for unloading.

Loading and unloading obligations are often more complicated than what most practitioners anticipate. For example, when applying the EXW incoterm rule, the buyer is supposed to be responsible for loading the product at the agreed departure place. In reality though, the buyer usually doesn't have a suitable instrument to load the product at the seller's factory, and it is usually done by the seller.

Shipment Schedule:

A shipment schedule is important because errors here may lead to demurrage charges, additional handling and warehousing charges at ports, and increased delays in delivery.

Specifications to detail in this section relate to aspects like when the ship is expected to berth at the port of departure, when will the loading will be complete, and how long the ship's transit time will be.

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1. Note that in some situations, however, incoterms are silent on this issue. This is why the parties should define their loading and unloading requirements in the agreement to avoid ambiguity.

Shipment schedule details are especially important if the parties are going to charter their own vessel or have a fixture note. For a charter party contract, the contract should include additional details like laycan, laytime, a notice of readiness, demurrage/dispatch, and vessel specifications.

In Incoterm rules that start with an E or F (EXW, FCA, FAS, and FOB), the buyer is responsible for arranging shipment schedules, and is expected to inform the shipment details to the seller. In C and D Incoterm rules (CFR, CPT, CIF, CIP, DAP, DPU and, DDP), the seller is responsible for the shipment schedules.

Insurance

Cargo insurance can be purchased to protect goods during transportation. Generally speaking, there are more than 45 major things that could go wrong and threaten shipments in transit including fire, stranding, heavy weather, theft, piracy, and barratry.

The risk transfer point is usually determined based on the Incoterm rule that was chosen and the seller is responsible for keeping the product safe up to that point. After that point, the risks of damage during transport transfers to the buyer. A buyer is generally not legally required to obtain insurance for the products, but it is usually to their benefit to do so.

If the parties agree to use Incoterms CIF or CIP, then the seller is required to obtain insurance for the product up to a specified amount. The CIF rule allows for a seller's coverage amount to be the minimum coverage (this is institute clause C). With CIP, the required coverage amount is generally the maximum coverage available (this is institute clause A). In both rules, the amount covered should be at least 110% of the invoice amount.

When insurance is required for the product, the insurance details such as coverage amount, currency, franchise, exceeding, departure and destination should be agreed on in an article.

Generally speaking, there are often liability limitations on damages in favour of transportation companies, meaning that their coverage may not be enough to cover the full value of the products that they transport. For

this reason, traders should explore obtaining their own cargo insurance coverage and not trust the shipping company's insurance to compensate them for potential damages occurring during transportation.

Inspection

Inspection services provided by a third-party testing body can be used to confirm the quality or quantity of a shipment before it is shipped.

Inspection services are helpful for small businesses that may have chosen their suppliers online and want to have their supplier evaluated in person. Third party inspection on overseas venders is also common with large businesses with thorough quality control requirements.

The following items should be contractually defined in this article:

Type and Scope of Inspection

There are different options available for inspection services based on the time of inspection and the application of the inspection results. These options include: during production inspection, pre-shipment inspection (PSI), mandatory standard inspection, price verification inspection, seller's credibility inspection, quantity, weight inspection, and project inspection.

In each of the above inspections types, the scope of inspection needs to be defined and is usually summarized in a test plan document. Scope of inspection usually refers to quality, quantity, packing, and loading metrics. The details of the scope of inspection should be referenced in the contract if applicable. As an example, an appropriate inspection may simply be a visual inspection, or it may require a more precise testing process based on some standardized testing methods.

Inspection or Testing Company

Choosing the inspection company is usually up to the buyer. Typically, a buyer signs an inspection contract with the testing body and then introduces that inspection company to the seller.

This unfortunately can present an incentive for collusion between the buyer and their chosen inspection company. If the terms of payment are based on a documentary credit, for example, and the buyer later simply

wants to renege on their contractual obligations for whatever reason, then the buyer and inspection company could chose to simply not issue a favorable inspection.[1] In such a situation, the seller would not be given the inspection certificate and would have a significant problem in fulfilling their requirements under the documentary credit.

To remedy this, if the terms of payment are based on a documentary credit, then the inspection company should either be liable to both parties (not just the buyer) for completing a proper inspection, or the seller should be entitled to select a new inspection company to do the procedure. This condition should be noted specifically within the documentary credit text.

Inspection Documents Verification

The parties define what documents are required to prove a shipment has passed inspection. Often, the seller receives the favorable inspection report from the third-party inspection body and then delivers them directly to either the buyer or the banks.

Inspection documents might include a certificate of inspection, verification of conformity, or a test report. Inspection documents should be issued on the formal letterhead of the inspection company. In some situations, governmental organizations might force the parties to attest the certificates in the local chamber of commerce and/or the embassy of the buyer. The parties determine these details in the sales contract.

Other Inspection Details:

In addition to the details mentioned above, the parties are should determine which party will pay the inspection fees. Inspection fees pricing varies from company to company but is mostly based on man/day rates. Based on Incoterms, the inspection fee is usually paid by the buyer (which is logical as the inspection is mostly meant to protect the buyer). In some special situations, it is possible that the seller pays the inspection fee.

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1. The buyer can indicate the name of inspection company in field 46a of MT700 of documentary credit.

Sellers may pay the inspection fees when DDP Incoterm rules are used (more on this later), or in case the parties for whatever reason agree to this, or in case the inspection is required based on the rules of the seller's country. Generally speaking though, because the inspection company is basically checking the quality of the seller's performance, it's best not to expect the seller to have authority to approve the inspection agreement and/or pay the associated inspection fees.

Another consideration for the parties is how samples for inspection will be chosen. In large contracts, the parties are advised to determine the sampling method, sample quantity, and to maintain sample records. After testing the samples, the products should be sealed to prevent the seller from manipulating or replacing the products. The inspection company supervises the stuffing into the containers and seals the vessels. The seal number is written in an inspection certificate, and the buyer can know it was unaltered when opening the containers at the destination.

The parties should also decide on the place of inspection, which may be at the departure or destination. The sellers' preference is to avoid inspection or do it at departure, but in some situations, mainly when DDP Incoterms are used, the parties may agree with the inspection at the destination. It should also be specifically noted in the contract that in the event the inspection result shows "nonconformity of the goods" then the transport company won't start their delivery process. In other words, buyers request the transportation company only start the shipment process after receiving a release note issued by the inspection company.

Shipment Documents:

Defining shipping documentation is especially important in sales and purchase contracts for dealing with customs and government organizations. Most problems that arise with these agencies are usually somehow related to a problem with the shipping documents.

International sales contracts should clearly define the following points:

1. What documents do we require?

2. How many original and additional copies of each document are needed?
3. Which party is responsible for issuing and/or certifying the documents?
4. What details should be indicated in each document?

The documents required depend mostly on the nature of the product and national regulations of the buyer's country. As negotiators, we typically should verify documentation requirements with our trade compliance experts.

In most situations, and for a majority of products, buyers will expect to receive four documents. These typically include a transport document (bill of lading, waybill or couriers receipt), certificate of origin, commercial invoice, and packing list. Depending on additional product and national regulations, the buyer may request the seller to provide some other documents which will be discussed in the next pages.

Bill of Lading

A bill of lading (B/L) is a document of the title. It is issued by the shipping company to prove that a product was in fact delivered to that shipping company for transporting the goods. They also function as negotiable instruments, meaning that a product's ownership can be transferred to third parties through "endorsing" the B/L. These documents are usually issued along with marine transport, and in most situations (especially when dealing with letters of credit) the B/Ls should contain the following:

Full Set: The number of original B/Ls are always mentioned in the document. All copies should be delivered (the seller can't keep any). Usually, there are three original copies of the B/Ls issued. Also, rather than specifying a certain number of B/L copies that are to be delivered, it's usually better to simply indicate "Full Set" B/L copies.

Clean: When cargo is delivered to the shipping company for transportation, the company is responsible for providing the product in the same condition at the destination. If the product is defective, broken, or has any sign of damage at departure, the shipping company indicates those losses on the B/L. In such a situation, the B/L is described as

"Claused." If no condition about defection or damage of the cargo is written on the B/L, then that B/L is referred to as "clean."

Onboard: This phrase indicates that the cargo is loaded onboard the vessel. In some countries, when the mode of transport is via roadway, freight forwarders might mention the phrase "En Route" on the FIATA bill of lading (FBL). Indicating on board on the B/L is an important condition for banks in letters of credit based on UCPDC 600.

Date of Issue: The B/L, like all other documents, needs to mention the date of issue. This date is relevant for when later working with letter of credits. Date of issue might be the commencement date of some obligations, such as a payment date in the open account method. Furthermore, the B/L should usually be delivered to the banks or the buyer within 21 days from the issuance date, unless otherwise it might be deemed as a "stale B/L."

Freight Payment: the type of freight payment should be indicated on the B/L. This may be either "Prepaid" or "Collect." If the Incoterms rule is based on E or F rules, then the corresponding freight payment is "Collect," which means that the buyer shall pay the freight. If the agreed Incoterms rule is one of the C or F rules, then the freight payment will be "Prepaid," which means that the seller needs to pay the freight.

To the Order of: The consignee or receiver of the cargo should be indicated on the B/L. The person that the B/L is issued "to the order of" is the cargo owner when it receives the original full set B/Ls. The owner can transfer the title of the products by endorsing the bill of lading. In some contracts, when the total amount of the price is not settled, the seller might request that the transport company issue the B/L to the order of the seller itself, or they may indicate "To order of the shipper" on the B/L. On a B/L, Shipper means the party who delivers the product to the shipping company that is usually the seller. In other words, the seller might try to retain the product's title by the B/L.

Waybill:

Most air and rail carriers issue waybills instead of B/Ls. Based on the mode of transport, this document might be an air waybill (AWB), a road waybill (CMR), a rail waybill (CIM), or a sea waybill (SWB). Although issued by transportation companies, this document is not a document of title (and is therefore not a negotiable instrument). Waybills are issued in numerous copies, and the validity of different copies are not the same. For example, AWB has various copies, and the "Shipper" copy is the only valid one, and other copies can not be used for delivery or submission to customs. If the parties elect to use a waybill as their transport document, then they should verify with their customs compliance team that this is permitted under the relevant national regulations.

Commercial Invoice

The seller issues a commercial invoice in one to three original copies. One electronic copy is usually enough in most countries for customs clearing and accounting purposes. In some situations, this document might need to be attested/legalized/confirmed by the local chamber of commerce and embassies.

Packing List

The seller issues this document in one to three copies. In most countries, an electronic version of this document is enough. The seller indicates the cargo packing details on this document and they are needed during the customs clearance process.

Although packing lists are formatted differently and the details are determined based on the product and the agreement of parties, they usually contain the following data:

Item or number, container number, description, quantity, package quantity,package number, gross weight, net weight, size and volume, specifications,country of origin, and remarks.

The more details mentioned in this document, the fewer issues you will have at customs and other controlling departments. This document does not need to be certified by third parties in most countries. Packing lists can be very simple when dealing with shipments of bulk products.

Certificate of Origin

Certificate of origin documentation acts as a declaration of where the goods where "made." This is especially important when dealing with customs agencies as it affects tariff classification and general trade rules for the import. A local chamber of commerce usually issues a certificate of origin in the seller's country, but in some situations, the seller or the buyer might issue this document based on their own knowledge. In most countries, this document is issued in one original copy. If there is any preferential tariff treatment or anti-dumping tariffs, then the customs authorities might request the importer to present a consular certificate of origin. The country of origin is determined based on the WTO agreement on rules of origin, national rules, or regional agreements like the USMCA/CUSMA/NAFTA in North America.

Classification Certificate of the Vessel

This document is used to show when a vessel is seaworthy, or in other words, that it is suitable for marine transport. Third-party agencies control the standard of specifications, classify the ships into different categories, and issue a classification certificate.

Classification certificates are used by insurance companies to protect themselves from shippers using "unseaworthy" vessels.[1] Banks will also likely request this document when using documentary credits, especially for bulk products and when a ship is chartered for a voyage.[2]

Certificate of Inspection

This document is issued by a testing body or inspection company and indicates that the cargo has been inspected and is in conformity with a related purchase order or proforma invoice. In most countries, the issuance of this document should be done after the B/L date, while the

1. Based on article 5 of London Institute Clause A, the underwriter or insurer company may deny covering the losses because of the vessel's unseaworthiness.

2. This is done in field 46a.

time of inspection indicated on this document should be before the B/L date. This document is issued in one original copy and might need to be certified by the chamber of commerce and the embassy of the buyer country in the seller's country.

Fumigation Certificate

Fumigation of certain goods, packages, and in some situations the means of transport may be necessary. For example, if the product is packaged on a wooden pallet, some countries require that the importer present a document that shows that the pallets were fumigated at the departure country. This depends on the regulations of the buyer's country and should be reviewed by a customs compliance team. Fumigation certificates are usually issued by inspection companies or government departments and are issued in one original copy.

Vaccination Certificate

This certificate is needed in some countries when dealing with livestock. It is usually issued by governmental organizations and proves that the animal is vaccinated for particular diseases before starting the transportation.

Pedigree Certificate

This certificate is used in dealing with livestock to prove the blood purity and the pedigree of the animal. It is issued in one original copy.

Health Certificate

This document is relates to products that are under increased regulatory scrutiny by national health agencies. These regulatory agencies request that importers present a health certificate to assure that the goods are up to a standard that is suitable for human consumption. This document is issued by authorized bodies in most countries and is usually needed to be certified by the chamber of commerce and embassies. It is usually issued in one original copy.

Certificate of Analysis

This certificate is issued to certify the technical specifics of a product. It is often used in industries like chemical products that deal in highly technical

materials. They are usually used for quality control and, in some situations, might be also used for tariff classification at customs. Certificates of Analysis are generally issued in one copy by the seller. They can also be certified by third-party labs if necessary.

Shipping Advice

Shipping advice is issued by the transportation company and announces the actual time of departure (ATD). It is used to inform the buyer that the shipment of the cargo is started. On some occasions, this document is sent to the insurance company to notify them of the effectuation (start) of their insurance coverage. Its role is just informative, and governmental departments such as customs rarely require this document. In some countries, when the cargo arrives at the border or an internal customs office, the shipping company may issue another certificate called an arrival notice.

Insurance Policy

Documentation proving insurance coverage details may be required in some deals. Details of coverage may include a description of the cargo, the covered risks, the covered amount, currency, franchise, exceeding, exclusions, departure, and destination should be indicated in the contract.

The seller is obligated to deliver this document when using CIF or CIP Incoterms rules. In other Incoterms rules, generally neither the seller nor the buyer is automatically responsible for presenting their insurance coverage to the other party.

Incoterms Rules

Incoterms are a standard set of international trade rules and regulations that were developed by the International Chamber of Commerce. Incoterms are composed of three letters and are meant to define details such as transfer of risks, allocation of costs, export/import clearance, and similar details.

Choosing the appropriate Incoterm is usually defined by the parties in the sales contracts. All international trade and negotiation practitioners must understand Incoterms to some degree.

The parties should consider three important points when choosing Incoterms.

1. The parties should specify the locations as accurately as possible. If an exact location is not defined, the seller will be entitled to chose a location that suits best for his/her objectives.

2. We have to specify which year's version of Incoterms the parties are dealing with. For example, many companies will use Incoterms 2020 (which is the latest version as per the time of this writing). If the parties for any reason prefer to use a previous year’s version of Incoterms, that is possible but should be clearly defined in the contract.

3. The parties may agree to make some changes from the Incoterms standard rules. For example, in EXW rules, the buyer is technically responsible for loading the product on the collecting vehicle at the place of the seller, but this is often inefficient and impractical for both parties. The buyer likely has no means or human resource to do the loading at the location of the seller (while the seller probably would have this ability). In most purchases, even in EXW deals, it is the seller who accepts the responsibility to load the goods on the collecting vehicle (even though it’s not technically their responsibility in EXW rules) . In case the parties agree to legally transfer this obligation to the seller, which seems logical to do so, the parties are recommended to define this in their respective sales contract.

In the above example, the parties should include some contractual language similar to the following:

EXW Incoterms 2020, --- (place), --- (point), the goods to be loaded on the collecting vehicle at the risks and expenses of the seller.

Based on the above phrase, in case the parties wish to make any change to Incoterms rules, they should write the party that is going to accept "the risks and costs" of the changed obligation.

Additional Important Points for Incoterms:

Except in EXW, export clearance should always be done by the seller.

Except in DDP, import clearance should always be done by the buyer.

In F rules (FCA, FAS, and FOB), the buyer selects the transportation company and signs the shipping contract. The buyer is responsible for informing the seller about the name and detailed information of the shipping company, means of transport, and transportation details.

In the C rules (CFR, CPT, CIF, and CIP), the seller arranges international transportation. In case the buyer has particular considerations about the means of transport or the transportation company, they should be indicated in the contract. For example, if the type, flag, or classification of the vessel matters to the buyer, it should be stated separately in the agreement.

In the C rules, the buyer should pay the costs of discharge or unloading at the destination. Furthermore, in case any loss happens to the cargo, this cost will be borne by the buyer except in special situations like inherent loss or packaging weakness.

In E, F, and C rules, delivery to the shipping company at departure means delivery to the buyer, and the risks transfer to the buyer at that point. Though, in D rules (DAP, DPU, and DDP), the seller must deliver the products to the buyer at the destination.

Selecting a suitable rule of Incoterms depends on the parties' capabilities, nature of the goods, risk acceptance, the distance between parties, national regulations, and governmental restrictions, and some other factors.

A simple rule of thumb for Incoterms:

Whichever party can handle the responsibility faster, cheaper, and with lower levels of risk should generally be in allocated those responsibilities. This will generally keep things quicker, more affordable overall, and with lower risks.

Incoterm Examples

The remainder of this section is an introduction to the different Incoterms rules. Also mentioned are some recommendations from the perspective of the **buyer** for each set of rules.

EXW: EX Works

The buyer is responsible for loading the goods at the seller's place.

The buyer is responsible for export clearance, so should be aware of what's required for that in the seller's country.

The buyer should specify the place and point as specifically as possible.

FCA: Free Carrier

The seller is responsible for export clearance.

If the agreed location is not the seller's place, then the buyer has to arrange for delivery on the arriving vehicle, which means it would be responsible for unloading and reloading or transshipment of the cargo from the arriving vehicle onto the collecting vehicle.

CPT: Carriage Paid to

A buyer has two critical considerations in this rule, one for the transfer of risks that pass at the departure, and another for the transfer of costs that should rationally occur at the destination. We have to define both of them.

In CPT rules, the buyer will likely want to have suitable insurance coverage for the cargo because the risks transfer to the buyer at the departure. Even if the seller pays the freight charges here, they have no liability for the risks and damages that may happen during international transportation.

CIP: Carriage and Insurance Paid to

With CIP rules, even though the seller is obliged to insure the cargo and deliver the insurance policy, it has no obligation in case of damage. In other words, the seller pays the insurance premium and provides the insurance policy to the buyer, but it does not assume the risks and, if

damage happens to the cargo, the buyer must follow up with the insurer or underwriter themselves.

This may be risky for the buyer, because the seller's insurance company may or may not even be active/present/operating in the buyer's county, effectively making the insurance policy useless. For this reason the buyer should check whether the insurance company is active in their country or not.

Based on Incoterms 2020, the insurance clause should be the Institute A clause in CIP rule, and it should cover at least 110% of the cargo value. The parties should define other details of the insurance policy.

DAP: Delivered at Place

In DAP rules, the seller not only pays the costs but also accepts the risks associated with delivering the goods to the destination place mentioned in the contract.

The costs and risks of cargo unloading at the agreed place are to be allocated to the buyer.

If the buyer wants the seller to present an insurance policy for when the goods are being cleared through customs, then the buyer would need to contractually define this. If not, the seller is not obliged to present an insurance policy to the buyer.

DPU: Delivered at Place Unloaded

In DPU rules, the seller is obliged to discharge the cargo while the risks and costs are to be borne by the seller. As the buyer, if you agree to do the discharge, and you expect the seller to pay the charges, you have to notify the seller in advance.

Although this rule was added to Incoterms for the first time in the 2020 version, it is similar to the DAT rule of Incoterms 2010. Regardless of the agreed place, import clearance should be done by the buyer.

DDP: Delivered Duty Paid

All the costs and risks are to be borne by the seller except the unloading at the final selected place.

This rule may seem like a favorable option for the buyer, but is often also expensive and might not be very cost efficient. If relying on a seller for most of the trade process, then the finished cost and time might be much more expensive than if the buyer handled more of the process on their own.

Non-resident importers often use this rule and accept all the obligations up to the place of the buyer.

FAS: Free Alongside Ship

In FAS rules, the seller is not responsible for the costs and risks of loading and terminal handling charges at the port of departure.

This rule can be a bit ambiguous because it's not clear how the parties are intending to allocate port charges which depends on the different customs of the port. It may vary from one port to another. For example, loading details for containerized, bulk liquids, grains, and break-bulk products are likely different. The tools and cranes and their costs are not the same, and this can lead to misunderstandings.

In case we are trading high volumes of bulk commodities or large quantities of goods based on this rule, it's better to define the exact details in our contract.

FOB: Free on Board

Based on FOB, the seller loads the goods on board the vessel. This rule is usually recommended for bulk and non-containerized cargoes.

After loading, if the goods need trimming, lashing, stowing, and/or dunnage, then the buyer would be responsible to pay the associated costs.

CFR: Cost and Freight

CFR means FOB plus marine transport freight. In other words, the seller pays the freight charges to the destination, but does not accept the risks associated with transportation.

CFR is only applicable for marine transport.

The buyer is recommended to provide suitable insurance coverage for the products from the moment that the goods are loaded on the vessel or from the date of delivery at the port of departure.

CIF: Cost, Insurance and Freight

CIF means CFR plus insurance. The seller is obliged to provide insurance for the cargo from the port of departure to the port of destination.

Keep in mind that the seller is only obligated to provide an insurance policy that has minimal coverage (which is institute Clause C).

The seller pays the freight charges to the port of destination, and the transport mode should be solely marine transport.

Financial Aspects and Articles

Price

Price is (of course) the amount of money paid for purchasing a specific product. This article has many aspects that are discussed below.

Price Type

Parties might use different types of pricing for different products. These are:

Unit Rate Price:

In this type of pricing, a given amount is specified for each unit of the product. It might be based on each number, kilo, ton, or any other unit. This type of pricing applies to most finished goods.

Lump-sum Price:

In this pricing method, all the machines or sections of a production line or factory equipment are priced in one big lump sum. This type is usually used for machinery or complicated equipment.

Cost-plus Price:

In cost-plus pricing, the seller bases their price on their finished costs, and then adds an additional percentage on top of that amount. This type of pricing is common in construction and engineering projects.

Reimbursable Price:

This pricing is often used when compensating human resource services for things like installation, erecting, or training. In this method, a given price is quoted for each man per day worked (or man/week or even man/month). For example, the parties may agree on 800USD/day for a technician.

Details that should be contractually defined here include the total required time (for example 20 days), legal deductions for things like insurance and tax, good performance deductions, and what is defined as a “day” within the agreement (meaning a calendar day, business day, working day, weather working day, absence day, etc.).

Optional Price:

This type of pricing usually gives the buyer the future right to purchase a given product at a specific price.

Royalty

This type of pricing is used in some contracts, such as licensing or franchise. A royalty might be a fixed or variable amount paid to the licensor or franchisor for using intellectual properties such as a brand or recipe. In some situations, it is written in the form of an expanded formula.

Unit Price and the Total Amount

In most sales and purchase contracts, the price is quoted based on unit price (as in price per piece). The standard unit measurement that we chose depends on the nature of the product.

In addition to the unit price, we have to determine the total amount. To calculate the total amount, we simply multiply the product quantity into the unit price.When indicating the total amount in sales contracts, we usually write the amount both in numbers and letters or words. This is to ensure the numbers are the same. When the numerical and written amounts aren't the same (likely due to an error) most lawyers believe that it's the written amount that applies. This is because it's less likely that an error was committed using the full written name compared to numbers.

When the parties allow for partial shipments, payments are usually expected be paid proportionally to whatever amount has shipped so far. The partial shipment details should be defined in the corresponding contract.

Currency and Exchange Rate:

In international contracts, our price needs to specify which currency we are quoting. It might be the currency of the seller, the buyer, or even a totally unrelated country (like USD or EUR).

Usually the parties are entitled to select whichever currency they want to transact in based on their sole discretion. In some situations, the parties may agree to later modify their requested currency.

When deciding which currency to use, the parties should consider factors like fluctuation risk, the currency's acceptance globally, and possibly any regulatory limitations on the transaction requiring a certain currency.

For exchange rates, the parties should specify a date and method for which the rate will be calculated. For example, the parties may agree to use a rate from a website like www.xe.com, at the date the bill of lading is issued, and based of the average rate announced at the end of the day.

Price Revision Formula

The price of some products may fluctuate throughout the lifetime of a contract. When dealing in such products, the parties may agree on a price revision formula.

This formula might contain revisions for different variables such as the price, currency exchange rate, or inflation. For example, the price of some commodities may change daily or there may be different qualities of product batches which need to be accounted for.

Terms of Payment

"Terms of payment" refers to all the conditions surrounding payment, including the timeline for that payment. Payment terms are generally closely related to pricing. Terms of payment appears in pretty much every contract.

Time of Payment

When is the payment expected to be made? Is the money transferred before, at the same time, or after the products are shipped? Generally speaking, there are four types of terms for payment as below.

Payment in Advance

In this method, the amount of money is paid before the delivery of goods. This mean s the buyer takes most of the risk and pays the amount before production or before shipment. Although it might seem strange, this method is used, especially in many small and medium-sized companies. The instrument used for paying in advance might include be bank transfer via MT103, electronic transmission, draft (clean collections), documentary credit (Red clause documentary credit), of cheque.

The buyer can request for an advance payment bank guarantee (APBG) for securing the amount. If using an APBG, it is suggested that the parties agree on an appropriate interest rate for the APBG and then add the interest amount to the bank guarantee. In case the seller does not deliver the product at the agreed time, the seller should be required to pay the

buyer's original amount back plus an interest amount for the period that it had kept the advance payment amount.

Buyer's can evaluate the credibility of a potential seller prior to agreeing to payment in advance. The following techniques might be used in this regard as due diligence on a potential seller:

- Searching on the net
- Technical visit to the company
- Export development agencies
- Embassies of the seller's country in the buyer's country
- The buyer's country's embassy in the seller's country
- Local Chambers of commerce
- Inspection companies
- Seller's partners in other countries

Open Account

In this mechanism, the seller accepts all the risks and delivers the product without receiving the money in advance or at the time of delivery. The product is shipped to the buyer, and the buyer then pays the amount after a certain period. This method is named open account because the seller opens a statement in the accounting system for the buyer, and this account remains open until when the buyer settles the amount. Payment instrument options for this method could include documentary credits (by acceptance or by deferred payment), bill of exchange or drafts (time drafts), bank transfer, or cheque, or etcetera.

The payment period (or due date) and the commencement date should be specified. For example, the parties may agree that payment will be made no later than 180 days from the B/L date. In that case, the period is 180 days, and the commencement date is B/L date. The commencement date can be B/L date, shipping date, documents presentation date, or any other agreed time. The crucial point is that this date shall not be after the date that risk is passed to the buyer on the base of Incoterms.

For example, if a product is sold based on FOB, a port in your own country, it is not correct to agree on receiving the amount 180 days after the arrival of the goods at the destination. This is because, based on the FOB rule of Incoterms, the seller is not liable for the risks on the route, and even if the goods are not delivered at the destination or are delivered partially damaged, the seller is not responsible. Therefore, if the case is based on FOB, the commencement date should be the date of shipment, B/L date, or another date prior to the transfer of risk.

As the buyer, it is not correct to accept the invoice date for the commencement date. Imagine that you have signed a contract for purchasing 1,200 sets of pumps, and the payment term is based on a 30-day open account from the date of the invoice. We also assume that the agreed lead time for the product is 45 days, which means that after submission and finalizing the order, the seller needs 45 days for production. At first sight, the buyer thinks that 30 days delay is suitable for payment, but five days after signing the contract, the seller issues the commercial invoice and sends it to the buyer. Now, the seller has 40 more days to deliver the product, and the buyer has 30 days to pay the amount. This would mean that the seller will get the amount ten days before delivery.

In short, it's essential that both duration of the term and its commencement date are appropriately matched. Most people default to thinking that the invoice should be issued after shipment, but this assumption is not necessarily correct.

Payment Against (on) Delivery

In this rare method, both parties or their representatives go to the same location and (simultaneously) the seller delivers the cargo at the same time the buyer pays the amount. The payment might be made in cash or via third parties like banks or exchange companies. This method might be used for small transactions in neighboring countries at the border. In this method, the payment risk is divided more in a more balanced way than the previous methods.

In case you are using this method, especially for perishable products and produce, pay attention to the fact that you might not be able to return the

goods to your premises because of high costs and fast perishability of the product. If the buyer delays and/or does not accept delivery of the perishable product, then that shipment might be partially or fully damaged.

Mixed Payment

In many deals, the parties may agree to settle the amount via a mixed payment method. In other words, the parties agree to pay the amount in different installments by using more than one of the above ways. For example, a specific amount might be paid in advance, some percentage at the time of delivery against shipment documents, and the rest will be paid 60 days after shipment or B/L Date.

Payment Installments

If the parties are using a mixed payment method, then the amount should be paid in different installments as a percentage of the total owed and over a specific amount of time. Payment installments can be designed to be paid after achieving some kind of milestone for the transaction. The buyer is usually expected to propose logical and acceptable conditions to the seller. To have a simple framework, the following milestones and related installments might be used.

No	Milestone	Instalment
1	Order submission	Advance payment: in some situations, the seller may receive a given percentage of the total amount to officially accept/finalize the order.
2	Production completion	Progressive payment: The seller informs the buyer that the product is ready for delivery, and the buyer pays a specific proportion of the amount at this stage. This instalment is usually paid before shipment.
3	Shipping	Payment upon shipment: This instalment is paid after the shipment documents are produced. This is the especially important if paying through documentary credits.

No	Milestone	Instalment
4	Installation and erection	Provisional Acceptance Certificate (PAC) retention: The buyer may withhold a given percentage (usually 5 to 10%) of the total amount payable to be released when the agreed services are provided. After finishing the installation and commissioning process, the buyer issues a PAC. Through this document, the buyer confirms that the delivery has been temporarily completed. At this moment, PAC retention is relieved and paid to the seller, and the warranty period starts. This instalment is often used with deals involving complex machinery with complicated installation requirements.
5	End of the warranty period	Final Acceptance Certificate (FAC) retention: The buyer may retain about 5% of the total amount until the end of the warranty period. During this period, the performance of goods sold (usually machinery and equipment) is monitored throughout a product's warranty period. When/if the product passes the guaranteed performance figures throughout the end of the warranty period, then the buyer then issues the FAC and clears whatever amount has been retained.
6	Any given time	Interim payment: The parties may agree that the seller shall pay a percentage of the amount after a specific time from date of delivery (or any other commencement date). This is different than progressive payments, where a working milestone needs to be met for the amount to be paid, regardless of the exact time. Interim payment is not dependent on a special milestone and is usually paid after a given time period.

Payment Instruments

How the payment is made could include various financial and banking instruments such as a simple transfer of funds, or a bill of exchange, and documentary credits. These are introduced below.

Transfer of Funds

This instrument is a transfer of funds done between banks. It is usually used for lower amounts. Most banks typically use MT103 of SWIFT texts for this type of transfer. It is usually good practice for the buyer to include information like the purchase order or proforma invoice number and the description of the goods in the field 70 of MT103 under the heading "Remittance information."

Drafts, Bill of Exchange, or Collections

A bill of exchange is an unconditional written order from one person to another to pay a specified amount of money to a designated person. Generally speaking this is done via two types of collections – Documentary collection and Clean collection.

In documentary collection, the seller accepts the risk of sending the goods to the buyer's country before receiving the payment. After shipping the cargo, the seller delivers the documents to a designated bank along with a draft. If/when the buyer accepts the draft, the bank then confirms it, and the shipment documents can be delivered to the buyer to obtain possession of the shipment. Otherwise, the seller can have also retain control over the shipment documents and return the goods to the departure. Bill of exchanges are popular in international trade and are used via banks.[1]

On some occasions, if the seller trusts the buyer they can simply send the shipment documents directly to the buyer. This allows the seller to

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1. The ICC has a set of standard rules governing collections. These are called the Uniform Rules for collections as per publication number 522 (URC522).

discount financing costs by assuming more of the risk that the bank would otherwise take on. This type of draft is named clean collection.

Collections are also categorized in terms of time and due date. These two categories are Sight and Time drafts.

If the draft is at sight (documents against payment), then the buyer is expected to pay the amount when they see the documents. If the draft is a time draft (documents against acceptance), then the buyer accepts and agrees to pay after a specified period. In time drafts, the seller can discount the draft and use it as a tool for accounts receivable financing.

It's generally up to the seller to define the type of draft. If we are working with a time draft, in addition to the period, the seller also has to consider the commencement of maturity or due date. Clear conditions are important to include in the sales contract because those conditions when the seller ships the cargo before receiving any funds. If a buyer were to not accept the draft and avoid paying, the parties need to allocate costs such as shipping charges and damages to the product. This method of payment is not usually a good fit for sellers dealing with new customers without a solid credit history.
The reliability of the buyer and the availing bank is critical in determining the discount rate or percentage that the financing bank might request for discounting the draft.

Documentary Credit

Documentary credit is a payment instrument in which a bank commits to pay a specific amount to the beneficiary within a specified period when the beneficiary presents a set of complying documents. In other words, if the beneficiary proves that it has done its obligations by presenting the compliance documents before the expiration date, the issuing bank is obliged to pay the amount of the documents to the beneficiary. If the terms of payment are based on documentary credit, it is important to contractually define what the conforming conditions are for payment. A typical process for a documentary credit payment is the following:

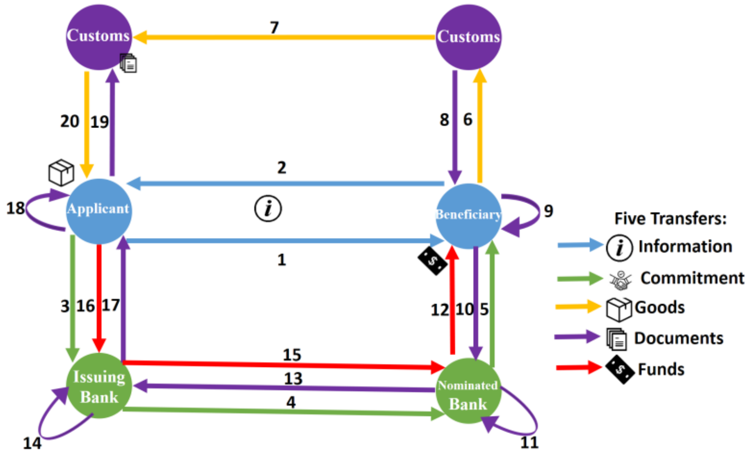

Figure 1: Process of a Documentary Credit

Steps of a Documentary Credit

Based on the above process, the steps of a routine documentary credit are as follows:

1. Purchase Order or Request for Quotation
2. Proforma Invoice or Sales Confirmation
3. DC Application
4. MT700 Notification
5. DC Advised
6. Delivery and Clearance
7. International Transportation
8. Documents Preparation
9. Documents Completion
10. Documents Presentation
11. Documents Checking
12. Documents Negotiation
13. Documents Mailing
14. Documents Checking

15. Reimbursement

16. Settlement

17. Documents Endorsement

18. Documents Completion

19. Customs Declaration

20. Customs Clearance

Important Points About Documentary Credits

The following points should be considered when drafting a contract and using documentary credits:

1. Verify there are no contradicting conditions between the contract and the letter of credit.

2. In some situations, experienced companies will attach their desired text for the documentary credit to the contract.

3. The shipment documents mentioned in the documentary credit text in field 46a of MT 700 should fully conform with the shipment documents indicated in the sales contract.

4. If you are the buyer, be aware that the documentary credit does not obligate the seller to deliver the cargo. Documentary credit is just a right for the seller and does not create any type of obligation for the seller. That obligation should be made in the corresponding sales contract.

5. If you are the seller, don't allow for the buyer to control the issuance of any of the documents mentioned in the documentary credit.

As an example, if the buyer's direct confirmation on quality is indicated in the letter of credit, and the buyer avoids issuing this document for any reason, then the banks will not pay out the amounts because the seller wouldn't be able to deliver one of the documents.

As another example, if the buyer selects a local inspection company, and that inspection company chooses not to complete their inspection because the buyer unilaterally tells them not to, then the bank would not be able to pay the seller because the seller wouldn't be able to satisfy the condition of delivering the inspection certificate.

It should be noted that the documentary credit is an independent commitment from the issuing bank to the beneficiary (seller). If the bank receives the compliance documents, then it pays the related amount.

6. Uniform Customs and practice for documentary credits (UCP600) has 39 articles and manages documentary credits. If you are the seller, study UCP600 as accurate as possible, because the conditions of this set of rules should be obeyed in shipment documents.

Documentary Credit Types:

Various types of documentary credits are available for different types of transactions. Some of the main kinds of documentary credits are briefly introduced herein as follows.

Revocable Versus Irrevocable

If the documentary credit is revocable, it means that the issuing bank will be authorized to cancel the documentary credit unilaterally on behalf of the buyer. The main positive characteristic of the documentary credit is the obligation of the bank to the seller or beneficiary. Therefore, if it is revocable, this obligation might be cancelled quickly, and the main advantage of the credit becomes null.

As the seller, it's generally not a good idea to accept a revocable documentary credit and a buyer should not expect you to. Note how irrevocability here just refers to the buyer's obligation, and the seller has the right to cancel or deny the documentary credit at any time. In other words, documentary credit does not create any commitment to the seller. In case the seller presents compliance documents, the issuing bank has to pay the value of the documents unless otherwise, the bank will not pay the amount.

Confirmed Versus Unconfirmed

In general, the issuing bank is the only bank that commits to the beneficiary for paying the amount. If the seller is not sure about the ability or the tendency of the issuing bank to pay the amount, it might request the buyer to open a confirmed documentary credit. In a confirmed DC, the issuing bank asks the advising or the seller's bank or any other

bank introduced by the seller to confirm the DC. This means that the confirming bank will also be liable to the seller for payment. The confirming bank usually asks for high charges and reimbursement to confirm the DC.

Generally speaking, a bank charges much more for a confirmed and its process is more complicated. Therefore, as the buyer, it's often helpful to avoid accepting confirmed DC as the payment method in the contract if possible.

At Sight Versus Deferred

Documentary credits are divided into four categories in terms of the time of payment or payment term. These are at sight, deferred, by acceptance, and by negotiation.

In sight DC, the seller receives the money a few days after presenting the compliance documents. In other words, the seller is not expected to wait to receive his cash after presenting the compliance documents.

In deferred and by acceptance DCs, the seller receives the money after an agreed period from a set date such as documents presentation date or shipping date.

In by negotiation DCs, which are not very common, the negotiating bank pays the amount from its own sources and does not withdraw the money from issuing or reimbursing bank accounts before the payment.

It's generally in the seller's interest to use at sight DC. The buyer generally prefers deferred or by acceptance DC.

As the seller, consult with your bank. You might be able to use the DC for financing at your bank with low-interest rates. For example, a buyer from a developing country may agree to add a 12% annual interest rate to the price if you accept 360 days by acceptance DC. On the other hand, your bank may finance this account receivable at a rate of 9%. In such a situation, not only have you supported your customer, but also you have enjoyed a benefit in discounting the DC.

Back to Back and Transferable

These types of DCs are usually used when the seller is an intermediary or middleman.

Back to back DC means that the seller (beneficiary) uses an opened DC as security or guarantee for opening another DC. The new or fresh DC is named back to back, which means that it is opened along with another DC, and the first one is used as the security for the second one.

Transferable DC is a credit under which the seller (first beneficiary) requests its bank, which is preauthorized in the DC text, to transfer the credit, wholly or partly, to the secondary beneficiary or beneficiaries.

Revolving DC

A revolving documentary credit is usually used when a product is sold repetitively to a specific customer. A revolving documentary credit covers multiple sales over a longer period to that same customer.

In other words, when a company sells a given product to the same buyer on a regular and repetitive basis, this type of documentary credit may be a suitable method for payment. When the applicant (buyer) opens this type of documentary credit, the beneficiary can present the shipment documents and receive the amount of documents, and the credit is recharged automatically for the next transaction. The number of repetitions (recharges) and the schedule of obligations should be determined in this type of documentary credit. Furthermore, it might be cumulative or non-cumulative. This documentary credit is opened ~~basically~~ at sight.

Red Clause DC

This instrument is a combination of payment in advance and documentary credits. In this type of documentary credit, the issuing bank allows the beneficiary to receive a percentage (or even the total amount of the credit) before shipment and presenting documents.

There are sometimes restrictions in specific countries about the advance payment percentage and the probable securities that the seller or its bank

shall prepare to make this credit operative. For example, in some countries, banks are not allowed to pay more than 30% of the total transaction value in advance. Additionally, in some countries, this type of documentary credit is not operative on the issuance date. The issuing bank requests the advising or nominated bank to issue a counter bank guarantee for the advance payment amount to make the documentary credit operative.

This kind of documentary credit is suitable for transactions in which the buyer insists on receiving some advance payment. This type of business may be common in some markets, such as fresh produce or livestock.

Standby Letter of Credit

Standby documentary credits are similar to bank guarantees. They are usually used as a plan B for payment from the seller. The parties have at least one additional payment mechanism in addition to the standby letter of credit (which is used as a backup).

The first payment method is generally based on trust that the buyer will pay within the payment term. For example, the payment might be a 90-days open account without any draft or banking interference expected. If the buyer were to not honor its promise to pay, then the seller can activate the standby documentary credit. Therefore, this type of documentary credit is an undertaking that is activated only if there is a conflict between the seller and the buyer, and the first expected payment mechanism does not take place.

Other Methods

A wide range of traditional and modern payment methods might be used in international trade between different countries. Besides the methods mentioned above, some other instruments could include bank payment obligation (BPO), cheque, bank cheque, cryptocurrencies, electronic transfer, fintech solutions, and initiative methods. Also, the parties might elect to use some older methods such as barter, offset, or turnkey models.

Seller’s Bank and Account Information

It can be helpful for the parties to include the sellers bank account information in the sales contract. This would include the bank's name, branch, telephone number, SWIFT code, account number or IBAN, and account owner or beneficiary

Legal Aspect and Related Articles

Liquidated Damages

A liquidated damages clause is an initially agreed upon amount of money that a party would have to pay if that party were to breach their obligations under the contract. These clauses often act as a type of penalty (although for policy reasons, courts generally don’t like to call them penalties).

Liquidated damages clauses can be useful in situations when it’s tough to accurately measure the damage caused by a breach. With liquidated damages, the parties can agree to an amount ahead of time.

In writing liquidated damage provisions, we consider the percentage amount to be paid, time base (day, week, or month), and value base (delayed goods or total value of the contract). If one party were to cancel the agreement, then the other party would likely be entitled to claim a fixed amount or percentage of the contract value.

If a liquidated damages amount is set irrationally high, then it’s possible that a court would deem the clause unenforceable. To know how a court might react to an unusually high liquidated damages clause amount, we have to study the local contract laws. In some legal systems, a court may modify the irrational liquidated damage amounts or they might throw out the provision all together.

In international sales of goods contracts, liquidated damages usually come up after there’s been a delay in delivery and/or order cancelation. In this situation, damages are often calculated based on a daily, weekly, or monthly basis.

Governing Law

Governing law refers to which country's laws will apply to the contract. This is obviously more important when dealing with international contracts. Consulting with local counsel in the jurisdiction of the contract is helpful (if not necessary). Typically, both parties push to use their own country's laws to govern the contract. Sometimes, international parties will choose to apply the governing law from a neutral third-party country. They may do this so that neither party has the home country advantage. They may also do this because that third party country's laws may be more developed and generally clearer on a specific industry.

Dispute Settlement

Contracts be used to pre-emptively agree on how disputes will be settled. Dispute settlement mechanisms may include amicable negotiations, expert team negotiations, conciliation, mediation, arbitration, mini-trials, and litigation.

Negotiation

In the event of a dispute, contracts can require that the parties come to the table and negotiate in good faith to try to find a solution before moving on to more contentious methods of resolution. This is helpful when the parties want to maintain a cordial business relationship. It's also helpful if the parties want to avoid public litigation for reputation reasons. Negotiations are meant to be amicable. They can also sometimes involve hired experts to represent each side.

Ideally, in an amicable negotiation, the parties talk like friends to solve their problems. Their discussions are usually friendly, and one party may simply waive some defaults or grant some concessions in contrast to the contract.

In an expert team negotiation, the parties' agents negotiate with each other to understand where the fault lies based on the contract. Because professional experts are involved, they can often better understand the legal consequences of whatever is causing the dispute. Ideally, whichever party is at fault becomes persuaded and accepts the agreed upon consequences. This method may take more time than an amicable

negotiation without expert representation. It also usually results in a resolution that is closer to the literal meaning of the contract.

Conciliation and Mediation

A conciliator or mediator is used to help the parties reach an agreement to a dispute without requiring that the parties be bound by the decision of the third-party neutral. The difference between these two methods is that the conciliator usually suggests some solutions and initiatives for solving the problem, but the mediator does not propose solutions. A mediator tries to help the parties to find solutions and resolve the dispute.
This dispute mechanism is often applied to smaller issues rather than to complicated high-value transactions. For larger issues, it seems to work best when the third-party neutral has the power to bind the parties to a decision.

Arbitration

Arbitration is often the most desirable method for solving international business disputes. This is because arbitration is comparably fast, less expensive, and because the award is final, binding, and enforceable in most countries based on the New York 1958 Convention. When writing this article, define the following points.

- Scope of arbitration: What type of disputes are solvable by arbitration?
- Type of arbitration: will it be organizational or ad hoc arbitration?
- The number of arbitrators: how many arbitrators do we need? One or three?
- The venue of arbitration: where should the arbitration take place? In which arbitration center?
- Cost of arbitration: Who is in charge of paying the costs of arbitration? The plaintiff, the loser, both parties, or do the arbitrators decide?

- Final and binding award: it is suggested to explicitly write in the contract that the award will be deemed final and binding.
- Severability of arbitration: the arbitration clause shall be severable from the remainder of the contract, and it will stay in full force even if the agreement is terminated.

Litigation

Litigation or judicial mechanism is done via state judicial or legal systems of the countries. In other words, this method is done by entities that are related to governments. It is not a suitable method for solving international business disputes because other governments usually question their enforceability, and because of political relations, most countries do not accept the sentence of other countries' legal systems. Furthermore, it is time-consuming. If both parties are located in one country (with different nationalities), this method might work and be suitable. In such a case, the parties usually accept that specific country's rules as governing law.

A widespread mistake in international contracts is that the parties might use a dual mechanism and mix arbitration with litigation. In other words, the parties agree on arbitration as the first method and then state that, if one party does not agree with the arbitration award, it can refer the case to a court to be solved via judicial procedures. This is a mistake and causes a waste of time for arbitration because the loser usually decides to refer the case to a court. So, we should not mix arbitration with litigation.

Termination and its Consequences

Termination might happen in international contracts for reasons such as bankruptcy, breach of material conditions, long-term force majeure, or some other circumstances indicated in the agreement or governing law.

The most common reason for termination in sales contracts is a delay. We have to consult on this article with local lawyers. In case a delay in delivery occurs, the buyer may be entitled to claim for liquidated damages. In case the delay is longer than a given time, the buyer may declare the contract as terminated or avoided. We should not accept the

change of management, ownership, and control as the cases that lead to termination.

Let's imagine that a contract is terminated. What happens next? Based on the terms of payment, some money might have been transferred, or the product might have been shipped. The parties are advised to determine the consequences of termination in different fields. Confidentiality, arbitration clause, intellectual property rights, advance payments, and consignment products that are delivered to the buyer without pay, are the most critical issues in a situation like this.

Force Majeure

In most legal systems, force majeure means unforeseeable, unavoidable, and uncontrollable events. If a party of a contract encounters a force majeure case, the contract will be suspended, and the related party will be relieved from doing its obligations for a specific period. If the effects of the force majeure case endure more than the mentioned period, the contract will be deemed terminated. The cases of force majeure should be defined by explicit wording in the agreement, or the parties can refer to a standard clause such as the International Chamber of Commerce Force Majeure clause.

Notices and languages

Execution of the contract requires arrangements and needs the parties to transfer messages to each other. In other words, the parties send some notices to keep the other party informed of the necessary information. What is the official and correct method or medium for sending these messages? The parties define their communication channels such as mail and email address, telephone, fax, or any other medium. Furthermore, they usually introduce the right contact person of each party in the contract.

This article is crucial for avoiding future misunderstandings. Furthermore, it helps the parties to prevent the phishing of third parties.

On the one hand, an international contract means that there are two sides to two countries in business relations, and they probably have two

different languages. On the other hand, the parties exchange various items, and it is essential to determine the language. As an Arabic company in Dubai, imagine that we have received three thousand pages of technical instructions in the Chinese language. Though your first priority might be Arabic, most probably you accept the English version of the instructions. Therefore, it is crucial to determine the language of different subjects, including correspondence, shipment documents, technical guidance, training, and in-person sessions, negotiation meetings, and the contract text. The parties can quickly write the following sentence in the contract: "The language for all documentations, relations, and aspects of this contract shall be solely in English."

If the contract is written in more than one language, it would be possible that the different versions have contradicting meanings or translation conflicts might happen. In such cases, it is crucial to stipulate the languages of the contract and decide on the issue that in case any contradiction occurs between the visions, then which version or language shall prevail.

Miscellaneous Article

This article is written in most contracts and contains a few clauses. Some standard provisions such as confidentiality, non-bribery, non-assignment, entire agreement, non-waiver, severability, interpretation, and intellectual property could be written in this section. If one of these subjects is highly essential in a given contract it can be written in a separate article. The negotiators usually write the conditions that are not related to other items in this article.

Signatories, Articles, and Pages

In the last article, the parties write the number of official copies of the contract, number of pages, number of articles, and the authorized signatories of the agreement. If there is any attachment or annex in the contract it should be indicated that the main text priority and attachments should be clear. In other words, the parties shall clarify that if any contradiction happens between the main text of the contract and different attachments, which one shall prevail or what is the hierarchy of priority between contract documents.

Conclusive Remarks

Hopefully, this discussion has provided additional context to some of the issues that one might run into while working with international parties and contracts.
Again, nothing in this discussion is meant to be specific legal or financial advice applicable to the reader's individual needs. For that, please reach out to the authors directly as we would love to discuss your projects in more detail.

International contracts are complicated. Let us help you.

Figure 2: Framework of International Sales Contract