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Structuring Your International Sales Contract

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Whether you are an importer or an exporter, having a well-structured international sales contract is crucial to protecting your interests. Besides the basic terms of the transaction, it is important that the sales contract address a variety of issues as follows:

A. Terms

Be specific and adequately detail all the basic terms of the transaction. Designate the currency denomination that will apply and the place of payment. Allocate currency exchange risk between the parties by designating at what point in time price will be established in the applicable currency.

Designate how payment will be made, such as cash downpayment, on account, on delivery of documents or letter of credit. How much will be paid up front and what risk is the seller willing to take? If a letter of credit is used, the letter of credit is a stand-alone document, independent from the sales contract, which will be paid upon satisfaction of the precise terms of the letter of credit, regardless of any defenses to or breach of the underlying sales contract. It is highly recommended that your attorney carefully review the terms of any letter of credit. Many international sellers have been denied payment upon presentation of the letter of credit because of poor draftsmanship.

Specify when payment is due. Is it when product is delivered to the inland carrier or the overseas carrier, or on delivery of the shipped documents, or when loaded on the dock? These terms and others are often covered with the use of “incoterms”, an internationally accepted set of terms that designates these terms and allocates risk between the two parties.

If partial deliveries are contemplated, the payment schedule should be specific as to how much the payment is upon each delivery, when payment for each partial delivery is due, and how each delivery is confirmed.

B. Risk Allocation

As mentioned, the “incoterms” in the contract will often designate risk allocation. If the goods are damaged while being shipped, who bears that risk? Whoever bears the risk is well advised to obtain insurance to cover that risk.

In addition, seller may want to obtain credit insurance to insure the credit risk of the buyer. The U.S. Export-Import Bank, other government agencies and private carriers provide this insurance.

C. Inspection

Buyer will typically want the right to inspect goods at some point in the shipment process. Buyer would prefer inspecting at some point after the goods arrive in its country, while seller would prefer that the inspection occur at some point prior to leaving the dock. If the buyer can object to delivery after the goods arrive in its country, the seller may find its product stuck on the docks or other port of entry in the foreign country of destination. Seller should resist any request by buyer to rely on a certification of inspection by a government agency in the country of destination, since buyer may be able to apply undue influence on or may have connections with that government agency.

If the risk of damage to goods during shipment is borne by the buyer, seller should insist that buyer hire its own inspection quality assurance company to inspect the goods at some point before the goods leave the docks in the home country (i.e., the country from which shipment is made). Typically, the inspections are conducted by private companies hired by one of the parties.

Defective product may not necessarily mean that the buyer does not have to accept delivery. Rather, a defective shipment may only give rise to a right to have items replaced or a credit given to buyer as set forth in the sales contract. The parties must agree on this allocation of risk. The trade finance documentation, such as a letter of credit, must be carefully drafted to address this issue. If the sales contract provides that the buyer must accept delivery despite the defective condition of a portion of the shipment, then one of the conditions of the letter of credit should be the triggering event for payment under the sales contract, not the results of an inspection.

D. Shipment

The sales contract should identify all shipping documents to be presented and whether multiple copies are required. These documents often include the signed commercial invoice, the bill of lading, the packing list, product technical data sheets and certificates of origin.

The sales contract should also allocate the risk of delay in shipment. If penalties are to be imposed for late delivery by seller, these should be specified.

E. U.S. Requirements

Typically the seller is responsible for obtaining any export licenses required by the home country. The U.S. Department of Commerce is the primary agency responsible for export control compliance, although other agencies (such as the State Department for defense items and services) have responsibility for certain specialized types of exports. Failure to obtain applicable export licenses may result in seller’s goods being held up at the port of entry, the imposition of significant fines and penalties, restrictions or prohibitions on future exports by that seller and even criminal charges.

The goods must pass through customs in the country of destination. The sales import duties and taxes, which often is denoted by use of the applicable “incoterms”. In addition, some countries have licensing and inspection requirements for imports. For example, bringing fish and wildlife into the U.S. must pass certain inspections.

The United States has imposed embargoes and comprehensive bans on sales to and imports from certain countries and/or nationals of those countries such as North Korea, Iran, Cuba, Sudan, Syria and Myanmar. Penalties for noncompliance can be severe. Since the U.S. exporter is also responsible for assuring that the foreign buyer does not resell to these countries and nationals, the sales contract should contain a prohibition to this effect and allow the U.S. exporter to monitor compliance.

The sales contract should require that all sellers and payments made by sellers comply with the U.S. Patriot Act and U.S. anti-money laundering requirements. U.S. manufacturers selling to foreign distributors should also include provisions in the sales contract to assure compliance with the U.S. Foreign Corrupt Practices Act.

F. Dispute Resolution

A crucial, but often overlooked, element of an international sales contract is the dispute resolution clause. First, the contract should specify which country’s law governs. Where no law is specified and both buyer and seller are in countries that are parties to the U.N. Convention on Contracts for the International Sale of Goods (CISG), the CISG will apply. The parties can also designate that the CISG apply or can specifically opt of that law.

Arbitration is the preferred dispute resolution mechanism in international sales contracts. This is principally because litigation in many countries is not a transparent process. In addition, a judgment obtained in litigation in one country may not be enforceable in the other. To the contrary, many countries are parties to the U.N. Convention that requires parties to that Convention to honor arbitration awards made in a participating country. However, an arbitration clause must be properly drafted so that one of the countries cannot attack the arbitration clause as unenforceable, which is a common tactic to bypass an arbitration clause.

A proper arbitration clause should designate which forum and rules will be applied. There are numerous arbitration bodies, such as UNCITRAL, the International Arbitration Rules of the American Arbitration Association, the International Chamber of Commerce, the Stockholm Chamber of Commerce, the London Court of International Arbitration and the Singapore International Arbitration Centre, among others. At times a country’s laws may require that the arbitration body be one located in that country. Since the arbitration typically can be conducted at various locations, the location of the arbitration must be designated.

The arbitration clause should state whether it is binding. Some arbitration clauses first require non-binding mediation before a party can avail itself of arbitration.

Some arbitration rules allow the parties to designate the arbitrator or will honor qualifications of an arbitrator, the choice of a panel versus one arbitrator, and the process of selecting an arbitrator.

An arbitration clause can often dictate certain procedural requirements, such as the right to take depositions, the right to have witnesses attend and so forth. Some forums have their own rules, which cannot be varied by contract.

The official language of the arbitration should be designated. It is not uncommon to have a provision that any written documents and any award be in both languages, but usually one language will be the controlling language.

The arbitration clause should specify whether the arbitrator may award attorneys' fees and arbitration fees to either party.

G. Other

A language designation should also be made as the official language for the contract, if the contract is written in two languages. If there is an irreconcilable difference in the contracts, one law should govern over the other.

One "boilerplate" provision which is of particular importance in an international sales contract is a merger clause. Often the parties make numerous communications both orally and in emails prior to the sales contract being entered into. The merger clause clarifies that the sales contract supersedes any prior oral and written communications so that neither party can make the claim that the terms of the contract were altered in a separate discussion or communication.

Since most international sales contracts are not executed in one place by all parties at one time, a "boilerplate" counterpart provision should be included in the contract. Not only should this provision specify that there can be duplicate copies with the signatures of the parties on multiple separate copies, it should also provide that email, pdf and fax signatures are permissible.

When dealing with a party in another country, a sales contract is essential to protect one's rights. Even then, the differences in legal systems and cultures can still produce undesirable results. However, with a carefully drafted sales contract, the risk of loss is minimized.