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Practical Considerations in Drafting F.O.B. Terms in International Sales

Alain Frecon
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by

Alain Frécon†

INTRODUCTION

Shipping terms in a contract for the international sale of goods assign the parties' rights and obligations with regard to transportation of the goods. The common understanding of a "Free on Board" (F.O.B.) shipping term is that the goods will be delivered onto a carrier free of charge. However, use of the F.O.B. term has other legal effects, including the determination of which party will bear the cost of shipping, who must bear the risk of loss of the goods, and whether a trader may utilize the foreign tax credit. Despite the important legal implications of its use, international traders often employ the F.O.B. term in a perfunctory manner with little, if any, regard for its meaning and potential effect. In failing to draft shipping terms that accurately reflect their bargained-for expectations, the parties risk misunderstandings, increased taxation, and, in some cases, costly litigation. The potential for dispute is particularly acute where the parties are unaware that the trade practices of their respective countries do not coincide.

† Partner, Popham, Haik, Schnobrich, Kaufman and Doty, Ltd. Member of Minnesota, American, Federal and International (London) Bar Associations. The author gratefully acknowledges the assistance of the editorial board of the International Tax and Business Lawyer in the preparation of this Article.

1. For purposes of this Article, "contract for the international sale of goods" or "international sale" shall mean a contract between parties whose places of business are in different states or countries.

2. Black's Law Dictionary defines the term F.O.B. as: "free on board some location (for example, F.O.B. shipping point; F.O.B. destination); the invoice price includes delivery at seller's expense to that location. Title to goods usually passes from seller to buyer at the F.O.B. location." BLACK'S LAW DICTIONARY 578 (5th ed. 1979)(citing U.C.C. § 2-319(1)).

3. In the introduction to the INCOTERMS 1980, the International Chamber of Commerce states: "Frequently parties to a contract are unaware of the differences in the trading practices of their respective countries. The existing diversity of interpretation is a constant source of friction in international trade, leading to misunderstandings, disputes and references to the courts with all the waste of time and money that these entail." INCOTERMS 1980, infra note 5, at 6. In Miami Purchasing Serv. Corp. & Miami Aviation Serv., Inc. v. Comm'r of Internal Revenue, 76 T.C. 818 (1977), petitioners stated that they "attached no special legal significance to the use of the term 'F.O.B.' The individual who served as president of both petitioning corporations testified that he knew that the term meant 'free on board', but that he had 'never heard of the Uniform Commercial Code in all of the time that he had been in the exporting business.'" Id. at 827.
International traders can allocate their mutual shipping rights and duties unambiguously by considering pre-established sets of shipping terms, the meanings of which have been elucidated by national and international trade conventions. The Uniform Commercial Code (hereinafter the UCC), the Revised American Foreign Trade Definitions (hereinafter the RAFTD), and the Incoterms of 1980 constitute important reference points for the drafting of shipping term definitions.

The purpose of this Article is to alert the parties to an international sales contract to the substantial differences existing among the available uniform shipping terms and to present various considerations central to the proper use of such terms. Part I of this Article discusses the similarities and differences

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4. The Revised American Foreign Trade Definitions [hereinafter cited as R.A.F.T.D.], which updated definitions first developed in 1919, were adopted July 30, 1941 by a joint committee of the National Foreign Trade Council, the National Council of American Importers, and the U.S. Chamber of Commerce. For excerpts of the RAFTD, see 1 A. LOWENFELD, INTERNATIONAL PRIVATE TRADE DS-151-58 (1977). The organizations which originally promulgated the RAFTD now refer members businesses to the Incoterms. International Chamber of Commerce, GUIDE TO INCOTERMS 3 (1980); telephone conversation with a representative of the National Foreign Trade Council, New York, New York (January 27, 1986). Reasons for the limited utility of the RAFTD as a sole source for shipping terms include the lack of a RAFTD term for shipment by aircraft and the apparent desire to use the multilateral, uniform definitions of the Incoterms rather than the nationally-oriented RAFTD terms.


6. These three sources are not exhaustive of the available definitions from which to choose. Many countries have enacted statutory definitions to which their nationals may refer in executing their international sales contracts. The French Civil Code, for example, sets out the statutory delivery rights and obligations of buyers and sellers based on the legal theory of res perit domino under which the buyer bears all the risks of delivery (including risks of destruction by force majeure). See CODE CIVIL [C. CIV.] 1138, 1604-1624 (1984); CODE COMMERCIAL [C. COM.] 100 (1984). The parties to a sales contract may, however, alter these statutory provisions by contractual agreement. See 2 H., L., & J. MAZEAUD, LECONS DE DROIT CIVIL 170-71 (1968). Certain countries have enacted exclusive national definitions to which the parties must defer where the transaction involves their country or nationals to a designated degree. In the Union of Soviet Socialist Republics, all foreign trade is carried out by Foreign Trade Organizations. See generally S. GARDNER, SOVIET FOREIGN TRADE: THE DECISION PROCESS 4 (1983). The People's Republic of China has Foreign Trade Corporations which until the late 1970s monopolized foreign trade. But other institutions and local enterprises are now involved. See generally KLENNER & WIESEGAR, THE CHINESE ECONOMY: STRUCTURE AND REFORMS IN THE DOMESTIC ECONOMY AND IN FOREIGN TRADE 103-31 (1983).

Other international promulgations concerning delivery and shipping term definitions include the United Nations Convention on Contracts for the International Sale of Goods, March 10-Apr. 11, 1980, U. N. Doc. A/CONF. 97/18 (April 10, 1980), reprinted in 19 I.L.M. 671 (1980), and the Warsaw-Oxford Rules, which were adopted by the International Law Association in 1928 and revised in 1931 to assist buyers and sellers using C.I.F. contracts. For the original rules, see INT'L LAW ASS'N, REPORT OF THE THIRTY-FIFTH CONFERENCE 272-82 (1929). For the revised rules, see INT'L LAW ASS'N, REPORT OF THE THIRTY-SEVENTH CONFERENCE 433-46 (1933). Although this Article does not address these considerations, the parties to an international shipping contract should investigate the limitations and definitions a particular nation may impose before adopting a set of shipping terms.
among these definitions with special emphasis on the term "Free on Board" (F.O.B.) and outlines the legal consequences of their application. An analysis of tax implications follows in Part II. Finally, Part III discusses the business and commercial considerations that influence a shipper's choice of shipping terms from among the available sources.

I
THE UCC, RAFTD, & INCOTERMS: SIMILARITIES & DIFFERENCES

A. The UCC, RAFTD, and Incoterms as Sources of Definitions

The UCC, RAFTD, and Incoterms represent perhaps the most recognized sources of shipping term definitions among traders. In drafting international sales contracts, traders often refer to these sources without incorporating them wholesale. By 1979, the UCC had been adopted by all states except Louisiana. The RAFTD had been approved by the National Foreign Trade Council, the National Council of American Importers, and the U.S. Chamber of Commerce in 1941. While these organizations now direct their members to consult the Incoterms, the RAFTD still provides a useful framework for analysis of the implications of shipping terms. The UCC and RAFTD, thus represent national efforts to unify commercial standards for international trade. The Incoterms, on the other hand, incorporate the most recent definitions enacted by the International Chamber of Commerce (hereinafter the ICC). First issued in 1936, the Incoterms remain popular among traders from many countries. Furthermore, they are unique in that they include definitions reflecting considerations and contingencies of contemporary trade relations, such as "F.O.B. Airport" and "Delivered at Frontier". The UCC, RAFTD, and Incoterms thus encompass the most extensive and comprehensive definitions available to international traders today.

7. This Article focuses on the F.O.B. shipping term because it appears in many international sales contracts and involves the greatest variety of practical, legal, and tax issues. A similar analytical and comparative approach should be undertaken when selecting any other shipping term.
8. See supra note 4.
9. The International Chamber of Commerce consists of national committees from over 50 countries. See INTERNATIONAL CHAMBER OF COMMERCE HANDBOOK (1978).
10. For a discussion of the "F.O.B. Airport" term, see infra notes 28-29 and accompanying text.
11. "Delivered at frontier" [named place of delivery at frontier] means that the seller's obligations are fulfilled when the goods have arrived at the frontier but before reaching the customs border of the country named in the sales contract." INCOTERMS 1980, supra note 5, at 70. This term is used mainly when goods are carried by rail or road but can be used with any other means of transportation including barges, ships or airplanes. Id. It is advisable to specify the frontier by naming the two countries adjoining the border. For example, U.S. goods can be sold to Canada "delivered at U.S./Canada frontier Detroit" (or any other city).
The UCC, RAFTD, and Incoterms have as their common purpose the elimination of uncertainty in international trade practices. They accomplish this aim by standardizing the meanings of commonly used shipping terms. In the event of misunderstanding or dispute over the meaning of an F.O.B. term, for example, courts rely on the parties' express statements of intention in the contract in determining their respective rights and obligations. Where the parties have failed to include qualifying language in the contract or shipping documents, courts attempt to ascertain the intended legal effect of the F.O.B. term from the facts and circumstances surrounding the transaction.

Since customary usage of the F.O.B. term often differs among countries, parties to international contracts can avoid problems of jurisdiction by stipulating in advance which law will apply or by choosing to interpret the terms according to the UCC or Incoterm definitions. Where the parties have stipulated that the F.O.B. term is to be interpreted under one of these sources, the issue becomes whether the parties have fulfilled their obligations accordingly.

B. Comparison of the UCC, RAFTD, and Incoterms

Although the F.O.B. definitions contained in the UCC, RAFTD, and Incoterms reflect many similarities, substantial differences exist as well. Parties to an international sale of goods must understand these differences in order to choose the definition most suitable for their particular transaction, to distribute risks rationally, and to avoid the surprise of unforeseen costs.

1. The UCC

The UCC provides three definitions from which the parties may choose to qualify the legal effect of the F.O.B. term. The parties' rights and
obligations will differ depending on whether the sale is designated "F.O.B. Place of Shipment", "F.O.B. Place of Destination", or "F.O.B. Vessel, Car, or Other Vehicle".

Under an "F.O.B. Place of Shipment" term, the seller's liability for ensuring safe shipment and paying shipping fees terminates upon delivery of the goods to a named carrier. There is no further obligation of the seller to load the goods on board the carrier. Under an "F.O.B Place of Destination" term, the seller must bear these risks and expenses until the goods reach their stipulated destination. Where an "F.O.B. Vessel, Car, or Other Vehicle" term is used, in conjunction with an "F.O.B. Place of Shipment" or "F.O.B. Place of Destination" term, the seller is also responsible for the risks and costs of loading the goods on board the carrier. Whichever of the three alternative terms is chosen, the buyer must reasonably provide any instruction necessary for making delivery, including the location of the loading berth, the name of the vessel, and its sailing date. Failure to do so may be treated by the seller as a failure to cooperate.

2. The RAFTD

The RAFTD distinguishes between the inland point of departure, the point of exportation, the port of shipment, and the country of importation. Although the sponsoring organizations no longer actively support the use of the RAFTD by international shippers, the distinctions made among the RAFTD terms provide a useful framework for analysis. In this connection, the RAFTD provides six variations of the F.O.B. term:

a) "F.O.B. (named inland carrier at named inland point of departure)";

b) "F.O.B. (named inland carrier at named inland point of departure) Freight Prepaid To (named point of exportation)"

c) "F.O.B. (named inland carrier at inland point of departure) Freight Allowed To (named point)"

d) "F.O.B. (named inland carrier at named point of exportation)"

e) "F.O.B. Vessel (named port of shipment)"

f) "F.O.B. (named inland port in country of importation)"

The parties' obligations differ among these terms in a number of ways.

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21. In contrast to the use of the term in the UCC, see supra note 16, the RAFTD terms were intended to be "price terms". That is, they designate who will pay which cost to what point without addressing the parties' legal obligations.
DRAFTING F.O.B. TERMS

(a) F.O.B. (named inland carrier at named inland point of departure). Under this term, the price quoted applies only at the inland shipping point, and the seller's responsibility for safe delivery and transportation expenses terminates upon delivery of the goods to the inland carrier for loading. The inland shipping point is often the seller's manufacturing plant, warehouse, or place of business, but it can be any other designated place. The buyer of the goods is thereupon responsible for safe passage of the goods and payment of all costs from the inland point of departure to the point of exportation (the place from which the goods will be shipped overseas), as well as to the ultimate place of destination. This term is similar to the UCC's "F.O.B. place of shipment", in that costs incurred in obtaining any document issued in the country of origin or of shipment or of both, which are required for purposes of exportation or of importation at the place of destination, are charged to the buyer. Although the seller must render any assistance requested by the buyer in obtaining these documents, the buyer must bear any extra costs thereby incurred.

(b) F.O.B. (named inland carrier at named inland point of departure) Freight Prepaid To (named point of exportation). Under this term, the seller's obligations are the same as in (a) above, except that he is also required to quote a price which includes inland freight costs in transporting the goods to the place of exportation. The seller assumes no responsibility for the goods after he obtains a clean bill of lading at the named inland point of departure. The buyer does not pay freight expenses from the loading point of exportation but will pay all transportation expenses incurred from the point of exportation to the place of final destination. The buyer also bears the risk of loss of the shipment from the inland point (or the seller's warehouse) to the ultimate place of destination.

(c) F.O.B. (named inland carrier at named inland point of departure) Freight Allowed To (named point). Under this term, the parties' obligations are the same as in (b) above, except that the buyer also pays for the inland freight costs (which are deducted from the seller's invoice) for transportation to the "named point" (the point of exportation).

(d) F.O.B. (named inland carrier at named point of exportation). Under this term, the seller's responsibility for safe delivery and transportation expenses terminates upon delivery of the goods to the named point of exportation. The buyer must therefore load the goods onto a vessel and bear all associated costs and risks. Otherwise, the obligations of seller and buyer are similar to those in (a) above.

(e) F.O.B. Vessel (named port of shipment). Under this term, the seller's responsibility for safe delivery and transportation costs terminates after the goods are loaded onto the vessel at the point of exportation. In all
other respects, the parties’ obligations are identical to those in (d) above. This term is also equivalent to the UCC’s “F.O.B. Vessel, Car or Other Vehicle”. Failure of the buyer to give adequate notice of name and sailing date of the vessel constitutes a contractual breach.

(f) **F.O.B. (named inland point in country of importation).** Under this term, the seller’s responsibility for safe passage and transportation costs does not terminate until arrival of the goods at the named inland point in the country of importation. He therefore accepts most of the responsibilities, costs, and risks associated with international shipping transactions, including export taxes, fees or charges, marine insurance, and war risk insurance, certificates of origin, consular invoices and other documents issued in the country of origin or of shipment, all costs of wharfage and landing, customs fees, duties, and import taxes, if any. The seller is also responsible for any loss or damage until arrival of the goods in the country of importation.

The advantage of drafting a shipping term along the lines of the RAFTD terms is that the exact point at which the seller’s risks and duties are transferred to the buyer is precisely designated. Compared to a single, broadly defined “F.O.B. place of shipment” term under the UCC, the RAFTD offers more precise definitions. If the parties choose to employ a UCC or Incoterms definition, it is advisable that they consider the RAFTD definitions for guidance in specifying the boundaries of their mutual obligations.

3. **The Incoterms**

Under the “F.O.B. named port of shipment” term of the Incoterms, the risk of loss of the goods shifts to the seller upon passing of the rail of the vessel designated by the buyer. In this respect, the Incoterms definition is equivalent to the “F.O.B. Vessel, Car or Other Vehicle” term of the UCC and the “F.O.B. Vessel Named Point of Shipment” term of the RAFTD. Under the Incoterms definition, however, the seller must also obtain at his own risk any export license or other governmental authorization necessary for export of the goods. The seller must also pay any taxes or fees that may be levied by the country of exportation. These incidental costs are not automatically charged to the seller if the parties have adopted a UCC or RAFTD definition.

Technically, the Incoterms do not provide an “F.O.B. Place of Destination” or “named inland point in country of importation” term. If the parties wish to have the seller pay the costs and freight of transporting the goods to the place of destination, they should refer either to the RAFTD “F.O.B.

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22. *See U.C.C. § 2-319(1)(a)(1977).* Under the RAFTD, “F.O.B. Place of Shipment” may be defined as an inland point of departure, point of exportation, country of importation or point of shipment. Also, the RAFTD’s use of the term “port” of shipment clearly refers to a place of shipment; the UCC may apply either to the place “to where” or “from which” the goods will be shipped. R.A.F.T.D., *supra* note 4, at art. II.

23. **INCOTERMS 1980, supra** note 5, at 34.

24. *Id.*
(named inland carrier at named point of departure) Freight Prepaid To (named point of exportation)" term or to an Incoterm designation such as "Cost and Freight ("C & F") Named Port of Destination" which includes only cost and freight, or "Cost, Insurance and Freight (C.I.F.)". Under a "C & F" term, the seller is not obligated to procure marine insurance against risk of loss of, or damage to, the goods during carriage, because such risks are transferred to the buyer when the goods pass from the ship's rail at the port of shipment. If the seller is to bear all shipping obligations (marine insurance included) and risks of loss or damage, the term "C.I.F. Named Port of Destination" must be used.

In 1980 the Incoterms incorporated a "free carrier (named point)" term which permits the parties to designate the point at which the shipping obligations and risks of loss of, or damage to, the goods are transferred from the seller to the buyer.\footnote{Id. at 100.} Under this term, "carrier" means any person with whom a contract of carriage by road, rail, air, sea, or any combination of modes has been made. The "free carrier" term offers the flexibility of allowing the parties to designate any point at which the seller can deliver the goods into the custody of the carrier.

The Incoterms' equivalent to an F.O.B. vessel shipment term under the UCC is the "Ex Ship Named Port of Destination" term.\footnote{Id. at 58.} Under this term, the seller must load the goods on board the ship and bear the full cost and risks associated therewith until the arrival of the goods at their destination named in the sales contract.

Only the Incoterms provide specific terms for different modes of transport. For example, when goods are transported by rail, the term "F.O.R./F.O.T. (named departure point)" can be used.\footnote{Id. at 22.} F.O.R. stands for "Free on Rail" while F.O.T. stands for "Free on Truck", which in fact refers to railway wagons and not to trucks. This term is most commonly used in Europe when goods are carried by rail. If the goods are transported by air carrier, the Incoterms provide an "F.O.B. Airport (named airport of departure)" term.\footnote{Id. at 92.} Under this term, the seller's risks and obligations terminate upon delivery of the goods to the air carrier of the buyer's choice.\footnote{Id. at 92.} The seller is not, however, responsible for loading the goods onto the aircraft. In this respect, this term is distinguishable from the Incoterms' "Named Port of Shipment" term, the UCC's "F.O.B. Vessel, Car, or Other Vehicles" term, and the RAFTD's "F.O.B. Vessel (named port of shipment)" term, all of which obligate the seller to load the goods on board the designated carrier.

\footnote{Id. at 100.}
\footnote{Id. at 58.}
\footnote{Id. at 22.}
\footnote{Id. at 92.}
\footnote{If the buyer fails to specify a carrier, the seller may deliver the goods to a carrier of his choice. Id. at 92.}
C. Considerations in Application of the Terms

With the possible exception of some of the RAFTD terms, most of the shipping definitions described above contain certain ambiguities. To avoid any potential misunderstandings, international traders should not hesitate to qualify and clarify their intent through additional contract provisions.

1. Use of the F.O.B. Term

The parties to an international contract should first avoid using an F.O.B. term without designating precisely the point at which the obligations and liabilities will pass from the seller to the buyer (e.g., port of importation, inland carrier, or place of seller's business). An F.O.B. destination term, for example, should designate the exact city of destination (e.g., Venice, Italy or Venice, California).

The parties should also clarify the scope of their obligations. For example, the use of an F.O.B. country or place of destination term which assigns the seller responsibility for securing transport of the goods in question to their final destination does not in itself imply that the seller is legally or contractually required to obtain marine and cargo war risk insurance. If the buyer expects the seller to insure the shipment against these risks, he should explicitly obligate the seller to do so on his behalf in a contractual provision (either in the contract for sale of goods or in the shipping documents) or through the use of another shipping term, such as the C.I.F. term of the Incoterms.

Some of the pre-established sets of definitions are also ambiguous as to which party is responsible for certain incidental expenses. For example, if a New York manufacturer agrees to an international sale under an "F.O.B." named place of shipment term under the UCC, it is unclear whether the manufacturer or the foreign buyer must bear the expenses of obtaining a certificate of origin and of paying the consular costs. Under the UCC, for example, the shipping obligations of the seller terminate upon delivery of the goods to the carrier in New York. Because the relevant documents are required upon delivery of the goods to the carrier in New York, however, the

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30. The typical marine insurance policy covers losses or damage caused by accidents, fire or action of the seas, and does not cover war risks (resulting from the capture, seizure, arrest, confiscation, requisition, nationalization, or destruction of the vessel caused by any weapon of war). Since a carrier is not an insurer, it is of the utmost importance that appropriate insurance (covering both the risks insured and the losses covered) be secured by either the buyer or the seller.

31. A certificate of origin discloses the nationality of the goods, i.e., the country in which they were manufactured. When goods are assembled in one country with parts originating from another country, it is sometimes necessary to specify that the goods were assembled with parts from that country. The primary purpose of the certificate of origin is to determine whether the "most favored nation" preferential customs tax and duties are applicable. It has also been used by some countries as a tool to enforce boycotting regulations against other countries. E. McGovern, INTERNATIONAL TRADE REGULATION: GATT, THE U.S. AND EUROPEAN COMMUNITY 184 (1982).

32. Consular costs are fees charged by consular officers for the issuance of special forms or documentation required by some countries upon the importation of goods.
seller may be forced to secure them. The seller can argue that, since these documents are required by the buyer's country for his receipt of the goods, the buyer should bear the issuance costs. If the parties had established clearly their mutual contractual obligations, or if they had selected, for example, the "C.I.F." term of the Incoterms, the buyer would be justified in demanding that the seller bear not only the legal obligations, but also the expense of obtaining the documents, since all costs incurred are encompassed within the C.I.F. term. Regardless of which set of definitions is considered, the parties should negotiate in advance who will bear any incidental expenses and either qualify the F.O.B. term in the contract according to their agreement or choose another term.

The parties should tailor the F.O.B. term as closely as possible to the particularities of their transaction. For example, shipping fresh eggs overseas requires different packaging, labelling, and transportation considerations than does the shipping of grain or chicken feathers. If the parties designate the sale as "F.O.B." without further qualification, it is unclear which party is responsible for packaging the eggs, designating the mode of transportation, or naming a carrier.

Certain considerations, however, aid in the resolution of such questions. Commercial customs, for example, imply that the seller must pack the goods. If eggs are shipped to Jeddah, Saudi Arabia from Fresno, California, the mode of shipment is crucial, and the parties must reach agreement as to the need for refrigeration of the eggs all the way to their final destination in Jeddah. If an "F.O.B. Place of Shipment" or "F.O.B. Vessel" term is chosen, the seller is responsible for packaging the goods since his obligations continue until delivery of the goods to a carrier. An unscrupulous seller, aware that the risk of damage to the goods passes to the buyer upon delivery to a carrier, may choose inadequate or otherwise inappropriate packaging and slow modes of transportation. Since the buyer under these circumstances stands to lose if the eggs are damaged en route, he should safeguard his investment by requiring sturdy packaging, by demanding that the shipment be marked with refrigeration labels, and by specifying transportation by air carrier. On the other hand, if an "F.O.B. destination" term governs the transaction, the seller bears all shipping risks and obligations until the goods reach the country of importation and can be expected to select the appropriate shipping requirements.

33. Among international traders, it is common practice for the buyer to pay for the issuance of the certificate of origin and the consular documentation. Less sophisticated parties may be unaware of this practice and consequently fail to adjust the contract price in consideration of these incidental expenses.

34. Under a C.I.F. term, the seller's quotation includes marine insurance and all transportation costs necessary to deliver the goods to the named point of destination. International Chamber of Commerce, GUIDE TO INCOTERMS 52-53 (1980). However, war risk insurance is not automatically included and must be secured by separate binder if it is desired.
2. Use of Letters of Credit

The parties should clarify both the point at which title to the goods passes and the due date of payment for the goods. In this connection, letters of credit serve a useful purpose. Typically, the seller desires payment in full before relinquishing title to and control over the goods, while the buyer wants to defer payment until he is assured of receiving conforming goods. The parties can usually resolve this potential conflict by stipulating when and how their respective obligations will be satisfied. The seller can specify, for example, that although he has relinquished physical control over the goods, he retains legal title to the goods until he receives payment in full. To this end, a seller can request an irrevocable letter of credit from the buyer payable upon the buyer’s receipt of the shipping documents or goods.

The buyer can attempt to include certain conditions precedent to the payment of the letter of credit such as receipt of the goods ordered, but the buyer’s remedies are typically limited to rejection of the goods or claiming loss or damage incurred as a result of non-conforming goods. Banks usually leave the buyer little freedom to insert such conditions into the letter of credit, unless special characteristics of the transaction permit or require such conditions precedent. Furthermore, sellers usually refuse to accept such conditional letters of credit, unless a history of trust and multiple business contracts exists with the buyer.

The terms of the contract and the letter of credit should coincide in meaning with the shipping term chosen. Unfortunately, international traders often execute the sale or purchase contract, the order, the letter of credit, and the shipping documents separately, thereby increasing the risks of inconsistency, misunderstanding, and dispute. For example, if a French businessman purchases computer graphics software during a visit to California, he should address the issue of full compatibility of the American software with his French-built computer prior to the conclusion of the sale. If a test is necessary to determine such compatibility, he should stipulate in his purchase order or purchase contract that his obligation to pay will mature only after such a test is conducted in France and proves satisfactory. Despite the inclusion of a testing provision in the order or contract, however, acceptance by the buyer of a shipping document specifying the sale as “F.O.B. Cupertino, California,” with payment due in full upon presentation of a bill of lading, presentation of the bill of lading in Cupertino, California will trigger his obligation to pay. He may not, therefore, refuse to pay, even if the compatibility test has not been effected. However, if the sale is made “F.O.B. Paris” (buyer’s place of business), with payment in full upon receipt (not delivery) of the goods, the buyer can wait until the test is completed before acceptance of the goods.

35. For a general discussion of international letters of credit, see 1 A. LOWENFELD, INTERNATIONAL PRIVATE TRADE 129-83 (1977).
thereby triggering his obligation to pay only after the software proves satisfactory. Similarly, he can reject the goods and avoid payment if the software proves incompatible with his computer system in Paris.

3. Force Majeure Clauses

Although the parties may have clearly stated their respective rights and obligations and specified the shipping term most appropriate for their transaction, the execution of their obligations may be frustrated by unforeseen circumstances referred to as force majeure. Since no pre-defined shipping term addresses these events, it is important that the parties agree upon their rights separately in the contract of sale or letter of credit.

Several important legal questions arise in negotiating force majeure clauses. A threshold issue is what type of event will constitute force majeure. Second, the parties must resolve whether force majeure will constitute a temporary or full excuse of performance. Finally, the clause should also stipulate which of the parties will bear the resulting financial burden and whether the injured party will be compensated. Failure to address these questions may result in serious disputes which may prove difficult to resolve equitably. Unfortunately, parties to an international sale routinely adopt standardized force majeure clauses which may not satisfactorily cover their transaction.

4. Conclusion

Given that each international sales transaction reflects its own characteristics and requirements, it is critical that both parties develop and maintain a

37. In French, the expression force majeure, which literally means “superior force”, is commonly defined as an “event which one cannot prevent and for which one is not responsible.” See Petit Larousse Illustré 426 (1984) [“Force majeure, cause à laquelle on ne peut résister; événement qu'on ne peut empêcher et dont on n'est pas responsable”]. Under French law, one cannot be compensated for damages if “as a result of a superior force or an inevitable event, a debtor has been prevented from giving or from doing what he was obligated to do or did what was prohibited to him.” See C. civ. art. 1148 (1984). Force majeure has also been defined by legal scholars as an “anonymous, unforeseeable and irresistible event.” See 2 H., L., & J. Mazaud, Leçons de Droit Civil 582 (1973). Under the U.N. Convention, “a party is not liable for a failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that he could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome it or its consequences.” See U.N. Convention on Contracts for the International Sale of Goods, supra note 6, at 4. See also, A.L. Corbin, Corbin on Contracts §§ 642, 1324 (1957).

38. A typical clause reads as follows: “Force majeure shall mean any event beyond the control of the parties, including, without limitation, fire, flood, riots, strikes, epidemics, war (declared or undeclared and including the continuation, expansion or new outbreak of any war or conflict now in effect), embargoes, and governmental actions or decrees.” A clause drafted “without limitations” could arguably include a sudden and unexpected change in the prime interest rate or in the foreign currency exchange rate as a force majeure. A drought, an earthquake, or a civil upheaval could also constitute a force majeure under that clause. If the parties fail to discuss this issue ahead of time, their expectations might differ on these points. When dealing with communist countries, for example, a strike is usually not considered to constitute a force majeure.
clear and thorough understanding of their mutual rights and obligations. In this respect, the selection of a particular shipping term may have far-reaching legal consequences which can be anticipated with accuracy only if the parties reach a common understanding. While individually-drafted contractual provisions may offer more flexibility and room for creativity with regard to the extent and scope of the parties’ rights and obligations, such provisions also open up the possibility of dangerous ambiguities or oversights. Institutional definitions such as those of the UCC or the Incoterms, which are for the most part easy to understand and apply, may eliminate many of these uncertainties, especially when used in conjunction with supplemental contractual provisions.

II
TAX CONSIDERATIONS

In addition to the careful selection and qualification of pre-defined shipping terms, U.S. sellers should consider the use of such terms to establish unambiguously the source of income derived from foreign transactions, thereby insuring that available U.S. tax benefits will accrue. F.O.B. terms not only designate the contractual rights and obligations of the parties, but also dictate important U.S. and international tax consequences which may or may not comport with the legal and commercial objectives of a particular transaction. The following discussion does not attempt to resolve these uncertainties; rather it attempts to alert the U.S. seller to the tax implications of selecting certain shipping terms.

A. U.S. Tax Considerations

Under the Internal Revenue Code, U.S. citizens, residents, and domestic corporations are taxed upon their worldwide income, irrespective of the geographic source of that income. Gains and profits resulting from foreign transactions and operations are therefore taxable in the United States.39 They may also be taxable, however, in the foreign country in which they were realized, since most countries tax income arising within their borders. In order to alleviate such double taxation, Congress in 1918 authorized U.S. taxpayers to credit the amount of tax paid to a foreign government against their foreign source taxable income.40 This credit is known as the foreign tax credit.41 Although as an alternative to the credit U.S. sellers may deduct foreign paid

41. For current provisions on the foreign tax credit, see I.R.C. §§ 901–908, 960. For an excellent study on this subject, see Foreign Tax Credit — Qualification and Computation, TAX MGMT. (BNA) No. 5–4th (1979).
taxes from their worldwide income, the credit may often prove more advantageous. The foreign tax credit is available only to U.S. sellers meeting certain qualifications. Moreover, the amount of credit allowed is subject to certain reductions and limitations. Generally, larger amounts of taxable foreign source income will generate greater authorized credits to offset U.S. federal income tax. To maximize their credit, U.S. sellers may therefore be tempted to categorize as foreign source income their gains derived from any and all transactions involving foreign countries. One way to do so is to adopt an "F.O.B. country of destination" shipping term so that title passes to the buyer in the foreign country, thereby generating foreign source income. Unfortunately, this step may prove insufficient in some cases, as the U.S. tax authorities apply additional standards in determining whether a particular transaction generates foreign source income.

Until recently, U.S. sellers executed most of their international sales of goods through domestic international sales corporations (DISCs), and the situs of the sale was deemed to be outside the United States. Since the abolishment of the DISCs, the determination of whether a transaction has occurred within or outside of the United States becomes more critical to the determination of the source of income.

I. Transfer of Title Test

The Internal Revenue Code (hereinafter the IRC) itself provides little guidance as to whether a sale will be deemed "foreign" for foreign tax credit purposes. Under the IRC, foreign source income is defined as "gains, profits, and income derived from the purchase of personal property within the United States."

42. I.R.C. § 164(a).
43. The decision to choose between a credit or a deduction can only be made on a case by case basis. However, since the deduction allowed for foreign taxes only reduces the amount of income subject to tax, a credit might be more advantageous as it operates as a direct offset against the U.S. tax. At the normal domestic tax rate of 46%, the true benefit resulting from a deduction will be limited to 46% of the foreign tax while the credit applies to 100% of the foreign tax paid or accrued. See I.R.C. § 11(b)(5). Once the credit is chosen, the taxpayer will be prohibited from deducting foreign taxes from his U.S. income for that year. I.R.C. § 275(a)(4); Treas. Reg. § 1.164–2(d) (1960). A taxpayer can change its election from deduction to credit, and vice-versa, in different taxable years. I.R.C. § 901(a).
44. I.R.C. §§ 901(c), 931(g).
45. A U.S. taxpayer who participates in a foreign boycott, for instance, will lose part or all of the available foreign tax credit. See I.R.C. §§ 908, 999.
47. For the source of income rules, see I.R.C. §§ 861–864 and the corresponding Treasury Regulations.
48. Taxes paid by DISCs to foreign authorities were entitled to foreign tax credits. See I.R.C. §§ 992, 993, 995. DISCs were replaced by Foreign Sales Corporations (FSCs) in 1984. Deficit Reduction Act of 1984, Pub. L. No. 98–369, § 801, 98 Stat. 494 (1984). FSCs may not claim foreign tax credits or deductions for foreign taxes on their taxable income from eligible export transactions. I.R.C. § 901(h).
49. Id.
States and its sale or exchange outside the United States." 50 The Treasury Regulations (hereinafter the Regulations) prescribe that the source of income is established by reference to its "situs", that is, the place where the "rights, title, and interest of the seller in the property are transferred to the buyer." 51 This method of determining whether the proceeds from a sale constitute foreign source income is known as the "transfer of title" or "title passage" test. Under this test, tax authorities look to the place where the beneficial ownership of the goods passes, rather than to the place where the goods are shipped. 52

In applying the IRC "transfer of title" test, courts have held that title passes where the parties expressly intended it to pass. 53 Tax authorities have held that since shipping terms such as F.O.B. and C.I.F. have well-defined, commercially recognized meanings, these definitions will determine the situs of a transaction. For example, when the parties use the term "F.O.B. destination", the judicial presumption is that transfer of title will occur when the goods reach that destination. 54 The parties' use of the term "F.O.B." without further reference or clarification has been held to mean that title passes from the seller to the buyer upon delivery of the goods to the carrier. 55 If the parties wish to change the situs of transfer, they must so indicate. 56 It is therefore important that the parties precisely define the term chosen in their contract, as courts will uphold any clear contractual statement even if it changes the generally accepted legal and commercial meaning of the terms. 57 In the absence of an expression of clear intent, however, courts have refused to rely on a "substance of the transaction test", under which all factors of the transaction, such as the situs of the negotiations, the location of execution of

51. Treas. Reg. § 1.861-7(c) (1960).
52. See Treas. Reg. § 1.861-7(c) (1960). "[N]o suitable substitute test providing an adequate degree of certainty for taxpayers has been proposed. . . . But [the passage of title test] does provide for a certainty and ease of application desirable in international trade." United States v. Balanovski, 236 F.2d 298, 306 (2d Cir. 1956), cert. denied, 352 U.S. 968 (1957).
53. See, e.g., Barber-Greene Americans, Inc. v. Comm'r, 35 T.C. 365 (1960). In A.P. Green Export Co. v. United States, 284 F.2d 383 (Ct.Cl. 1960), the court held that title passed where the parties intended it to pass and looked at the express intention of the parties as embodied in their sales contract. If a transaction is organized solely for tax avoidance purposes, the passage of title rule will be disregarded. Courts will scrutinize all the surrounding facts in accordance with the "substance of the sale" test. Treas. Reg. § 1.861-7(c) (1960).
54. Miami Purchasing Service Corp. v. Comm'r, 76 T.C. 818, 830 (1977) ("Title passes to the buyer at [the specified F.O.B. point] and risk of loss during the course of any further shipment is on the buyer."); also see Treas. Reg. § 1.861-7(c) (1960).
55. In United States v. Balanovski, 236 F.2d 298 (2d Cir. 1956), cert. denied, 352 U.S. 968 (1957), the court stated, "When documents of title, such as a bill of lading, are given up, the presumption is that the seller has given up title, together with the documents." Id. at 305.
56. See Treas. Reg. § 1.861-7(c) (1960).
the contract, and the location of the goods are considered. Recent cases confirm that courts continue to rely heavily on the transfer of title test. The only instance in which tax authorities currently will disregard this rule is one in which the transaction itself is purposely organized to avoid tax. In this case, all of the surrounding facts mentioned above to ascertain the substance of the sale will be scrutinized.

2. The Transfer of Title Test When Parties Fail to Conform with Term

Even where the parties adopt a pre-defined shipping term that clearly provides for title to pass outside the United States, it is unclear how courts will interpret the expression of intent where the parties' actions do not conform to the rights and obligations as defined by that stipulated term. For example, U.S. manufacturers sometimes agree to ship their goods overseas on behalf of, and at the expense of, their smaller foreign buyers. Shipping costs may either be incorporated into the quoted price or billed separately. The most common explanation for this practice is that U.S. manufacturers or sellers are more experienced with the intricacies of international shipments and can often secure better shipping prices and conditions because of the total volume of dealings they may have with a particular carrier. Often, the sellers also insure the goods until their arrival at the port of destination.

As a result of these commercial practices, it is not unusual for a shipping document or invoice to be labelled “F.O.B. Point of Shipment” or “Point of Departure” when the seller in fact secures and pays for the shipping and insurance costs and may even retain title to the goods until they arrive at their final destination in a foreign country. Since courts typically base their inquiries on the passage of title test, it is likely that a U.S. court would find such a transaction to be made within the United States for U.S. tax purposes. This interpretation might result even though the seller in reality had retained title to the goods until their delivery to the place of final destination. To avoid these unexpected tax consequences, U.S. sellers wishing to use the

58. United States v. Balanovski, 236 F.2d 298 (2d Cir. 1956).
59. Hammond Organ Western Export Corp. v. Comm'r, 327 F.2d 964 (7th Cir. 1964); Pfaudler Inter-American Corp. v. Comm'r, 330 F.2d 471 (2d Cir. 1964). For a discussion of criticism of the test, see Surrey & Warren, The Income Tax Project of the American Law Institute, 66 Harv. L. Rev. 1161, 1197-98 (1953). In the absence of explicit intent of the parties, the courts will examine extrinsic evidence such as sales invoices and insurance policies to determine where title passed from seller to buyer. Dorn and Co. v. Comm'r, 12 B.T.A. 1102 (1928) (the location of the partnership office where payments were made); Barber-Greene Americas, Inc. v. Comm'r, 35 T.C. 365 (1960) (where the goods were sold); Kates Holding Co. v. Comm'r, 79 T.C. 700 (1982) (the place of payment i.e., upon delivery to ship). The courts have also looked to trade custom or usage. See, e.g., Amtnorg Trading Corp. v. Higgins, 150 F.2d 536 (2d Cir. 1945). The Tax Reform Bill of 1985, as passed by the House of Representatives in December, 1985, proposes to abolish the transfer of title test. H.R. 3838, 99th Cong., 1st Sess., § 611, 131 Cong. Rec. H12624 (daily ed. Dec. 17, 1985).
61. See, e.g., Balanovski, 236 F.2d at 305; Kates, 79 T.C. at 700; Miami Purchasing Service Corp., 76 T.C. at 830.
foreign tax credit should select shipping terms whose meanings coincide not
only with the parties’ expectations as to when title passes, but also with the
parties’ actual commercial and shipping practices. For example, under the
UCC, the terms “C.I.F.” or “C & F” carry the presumption that delivery to
the carrier is delivery to the buyer for purposes of risk and title. Thus, a
C.I.F. sale will be found to have occurred within the United States for U.S.
tax purposes, and that term should therefore be avoided by a U.S. seller wish-
ing to generate foreign source income.

International traders should consider potential U.S. tax consequences
before concluding an international sale, since it will be expensive, if not im-
possible, to correct an undesirable result after the deal has been consum-
mated. Of course tax considerations should not always dominate the business
decisions of an international transaction. For example, a particular U.S.
manufacturer may find it preferable to send a small shipment to France
“F.O.B. Minneapolis” rather than “F.O.B Paris”, given his limited resources
or his lack of expertise in international commercial practice. Although he
forgoes thereby the potential tax advantage of characterizing his transaction
as a foreign sale, he also avoids the complexity and expense of international
shipments. Moreover, tax benefits are always subject to the scrutiny of the
tax authorities, and a given seller should consider the costs of replying to, and
defending, a tax audit as well as the possibility of losing projected profits
should the audit result in an unfavorable decision.

B. International Tax Considerations

U.S. tax advantages resulting from the use of a shipping term that
designates title as passing outside the United States may also be outweighed
by foreign tax risks. For example, a U.S. seller who retains title to the goods
until they are delivered to the buyer in the country of destination may have to
carry out certain activities such as unloading and warehousing the goods in
that country. Regardless of whether these activities are carried out directly
or indirectly by the U.S. trader, they may, if substantial and conducted on a
regular basis, either constitute the “conduct of business” or create a “perma-
nent establishment” in that foreign country.

The creation of a “permanent establishment” in a foreign country ex-
poses an enterprise to income tax liability in that country. At the same time,
a U.S. corporation faces the worldwide jurisdiction of U.S. income tax laws.

63. The term “Permanent Establishment” is specifically defined in bilateral income tax
treaties and often means the creation of a fixed and permanent place of business. See e.g., U.S.-
Dutch Income Tax Treaty, Dec. 30, 1965, United States-Netherlands, art. II(1)(a),(b), 17
U.S.T. 896, 897–98, T.I.A.S. No. 6051. See also US Model Income Tax Treaty, art. 5, 1 TAX
TREATIES (CCH) ¶ 158 (1981).
Such an enterprise should consider the definition of "permanent establishment" under the applicable bilateral tax treaty, if any, to ascertain the potential double taxation effects of a "permanent establishment." In addition to the imposition of income tax, a domestic use or consumption tax may also apply to the business activities conducted in that foreign country. The resulting tax, which must be paid in local currency, may prove substantial.

The adverse consequences of the creation of a "permanent establishment" are not limited to those involving taxation. A U.S. seller may be required to secure temporary or permanent business licenses before conducting any further business activity in that country. Local labor laws, as well as other non-waivable local laws and regulations concerning public policy or public order, will also apply. Moreover, the U.S. persons or entities involved may have impliedly agreed to be subject to the personal jurisdiction of local courts.

To alleviate such problems, many countries have included provisions relating to "permanent establishments" in their bilateral tax or friendship, commerce and navigation treaties with the United States. Since these treaties usually prescribe the factors to be considered in determining whether or not a "permanent establishment" has been created, parties to an international sales transaction should review these treaties prior to entering into a binding agreement. For example, the France-United States tax treaty states that the term "permanent establishment" shall include, among other things, a warehouse. However, the treaty stipulates that the mere use of facilities for the purpose of storage, display, or delivery of goods or merchandise belonging to the resident or the maintenance of stock for the purpose of storage, display, or delivery does not constitute the establishment of a fixed place of business or "permanent establishment." If a foreign country has not ratified such a tax

65. The Value Added Tax (VAT), for example, is a general tax imposed on consumption that is levied for the rendering of services and at each stage of the manufacturing and distribution process. In France, the normal rate is 18.6%; certain items are taxable at a reduced rate of 7% or of 5.5%, while luxury items are taxed at a rate of 33.33%. It is not deductible against a taxpayer's income tax. Most countries also levy many other indirect taxes, including social security and other labor employment related taxes which are not deductible from taxable gross income. Why Washington Likes Consumption Taxes, Bus. Wk. June 13, 1983, at 80; J. BAL- LADUR AND A. COUTIERE, THE VALUE-ADDED TAX: LESSONS FROM EUROPE: FRANCE 20 (H. Aaron ed. 1981).

66. See generally Z. I. KAVASSK & A. SPRUDZS, A GUIDE TO THE UNITED STATES TREA- TyES IN FORCE (1983). However, the Treasury's interpretations of the definitions contained in U.S. income tax treaties may sometimes be surprisingly creative. For example, in a 1984 Private Letter Ruling (PLR 8424007) the Treasury ruled that a Dutch exploratory drilling vessel temporarily anchored to the seabed constitutes under the U.S.-Dutch Income Tax Treaty a fixed place of business for the "extraction of natural resources." It can be argued that this interpretation is incorrect, since an exploratory drilling is neither a mine nor a process of extraction but rather a means of finding natural resources. For an analysis and rebuttal, see Cooper, Exploratory Drilling Vessel Constitutes a Permanent Establishment, 13 TAX MGMT. INT'L J. 448 (1984).


68. Id. at art. 4(3)(a), (b).
treaty or a treaty of friendship, commerce and navigation 69 with the United States, the risk of undesirable tax consequences is greatly increased.

III
COMMERCIAL AND FINANCIAL CONSIDERATIONS

Since shipping terms determine both the legal burdens and the attendant expenses of transporting goods, they may disrupt the commercial and financial equilibrium of an international sales transaction. Although each set of shipping term definitions prescribes a different distribution of shipping costs, F.O.B. terms generally allocate shipping costs as follows:

(a) "F.O.B. Seller's warehouse": Packaging costs for inland transportation are paid by the seller. All other costs are paid by the buyer from that point on.

(b) "F.O.B. Port of Shipment": Same as (a) above, except that packaging for international shipment and freight costs are also paid by the seller. All other costs are paid by the buyer from that point on.

(c) "F.O.B. Vessel or Airport": Same as (a) above, except that freight forwarder's costs and consular fees, pier delivery costs, wharfage or air packaging costs, and loading costs (not applicable if "F.O.B. Airport") may or may not be included in the seller's expenses, depending upon the parties' agreement. In addition, the seller usually pays these costs, and the buyer pays all other costs.

(d) "F.O.B. Port of Destination": The seller pays all shipping costs, including air or ocean freight transportation, banker surcharge, port congestion, insurance and unloading (maritime only), while the buyer pays all costs from that point on, including unloading and inland shipping costs.

(e) "F.O.B. Buyer's Plant": All shipping costs are paid by the seller, including import duties, import brokers fees, cartage from pier (maritime only), inland freight and warehousing.

These definitions determine which party bears the costs of unforeseen loss, damage, or delay. For example, if a sale is made "F.O.B. Paris", the seller should be aware that, as the legal owner of the goods until their arrival in Paris, she will be responsible for any additional or unexpected shipping costs. If longshoremen in New York or in Le Havre go on strike, the seller must either arrange for the temporary safekeeping of the goods or seek an alternative means of shipping the goods to Paris. If insufficient insurance was secured, or if a force majeure clause was not negotiated to relieve the seller of liability, damage costs may considerably reduce a seller's profit margin.

69. See A GUIDE TO THE UNITED STATES TREATIES IN FORCE, supra note 66.
1. Insurance and Incidental Costs

Securing insurance for international sales transactions can be a costly endeavor in itself. International traders minimize costs by securing insurance only for those events they consider most likely to occur. Standard insurance policies often exclude from coverage perils such as strikes, riots, and wars. Although coverage for these risks can be obtained, such insurance policies require special limited endorsements that are usually expensive. Even the most common “all risks” insurance coverage, despite its name, covers only theft, pilferage, nondelivery, damage or loss during handling, stowage, weather and water damage. Risks of war, strikes and riots are not covered, nor are risks inherent in the goods, losses caused by delays, or loss due to improper packing.

An international shipper must also be familiar with the complexities of insurance coverages before agreeing to undertake an F.O.B. destination sale. Marine insurance policies, for example, contain terms not easily comprehensible to the layman or unsophisticated shipper. International shippers should familiarize themselves with words such as “barratry”, which refers to willful and wrongful acts of the master or crew of the ship, and the “inchmare clause”, which refers to damage caused to the cargo by faulty machinery or equipment of the boat.

Packaging, labelling, and other incidental costs can often prove burdensome. Air carriers, for example, impose special packaging requirements. Shipments by sea have packaging requirements and shipping rates which vary depending upon whether the goods are shipped “below deck” or “above deck”. If a seller undertakes to ship goods to the country of final destination, she should be aware that certain countries assess customs duties on the gross weight of the goods. If packaging weight can be maintained at the lowest weight-to-safety ratio possible, the buyer can economize on customs duties. The savings in cost thus may result in lower selling prices in that country, thereby giving the buyer a competitive edge in the market.

Translation costs pose another potential burden. France, for example, requires the use of the French language in all documents pertaining to import transactions into that country. French officials have not hesitated in the past to detain goods for weeks, subject to the receipt of French translations, when shippers have failed to comply with French labeling requirements.

Proper marking of the goods for export also requires the use of international symbols and cautionary marks which may not necessarily meet the labeling requirements of a receiving country. Failure to comply with such requirements may result in costly delays or damages to the goods, which may not be, under the circumstances, recoverable from the insurance company.

Certain goods are subject to local health inspections, special licensing requirements, and export controls. Determining what these requirements are

and how they are satisfied involves hidden costs in time and money. The U.S. Department of Commerce enforces regulations under the Export Administration Act of 1979, as amended, which lists those goods subject to special licensing and authorization requirements.\(^7\) Compliance with Commerce Department regulations, however, does not exempt a U.S. shipper from filing a U.S. Shipper's Export Declaration,\(^7\) nor from satisfying other U.S. statutory requirements, such as the Foreign Corrupt Practices Act\(^3\) and the U.S. Antiboycott Regulations.\(^4\) Filing the requisite registration and application forms is a complex process frequently requiring costly legal advice. Failure to comply with these statutes triggers civil penalties and sometimes criminal charges.

While not exhaustive, this discussion highlights some of the most common incidental costs of international shipping transactions. Parties to international transactions must examine such hidden and incidental costs and allocate the burdens accordingly.

2. Currency Considerations

The parties' choice of shipping terms may have a significant influence on the financial benefits of the transaction. A seller who agrees to make shipment "F.O.B. Country of Destination", may be forced to receive payment for the goods in the local currency of that country. As a result, the seller may find herself exposed to undesirable and perhaps unexpected foreign exchange risks. Or, if payment in the foreign country is to be made in U.S. dollars, the remittability of those funds may subject the seller to local exchange control rules. Such regulations impair the freedom of foreign currency transactions by requiring approval of a national or state bank before payments can be made or before any foreign currency can be exported.

The payment consequences triggered by the choice of shipping terms are particularly restrictive in countries with rigidly controlled economic systems. Most of these countries require that all local transactions be concluded in the local currency. This requirement has serious financial implications for the shipper for several reasons. First, the foreign exchange markets in these countries usually set artificially high exchange rates for the major western currencies. Consequently, the seller may not receive the profit anticipated on the transaction. Second, the controlled system currencies generally have little or no market value outside the respective countries. Finally, some of these countries, in an effort to foster their local economies, expressly prohibit the convertibility of local currency into foreign currencies. They thereby force foreign sellers to accept the local currency, which unfortunately must then be reinvested in the local economy.

\(^7\) Id. at pt. 386.
The choice of a shipping term should always follow a thorough analytical review of the particularities of the given transaction or business. Because modern international business transactions are constantly evolving and are increasingly subject to U.S. and foreign regulation, it is critical to review shipping policies regularly and to scrutinize their impact on business. Furthermore, factors such as the place of transfer of title, place of delivery, terms of payment, and responsibility for shipping costs can be controlled by the parties through the careful drafting of their shipping contracts with special attention given to specific shipping terms. Finally, optimal results can be achieved if the seller's resources permit the case-by-case review of all international sales contracts, so that shipping terms can accurately reflect the particular circumstances of each case.