

## Chapter 8

# Export Sales Contracts

### *HARMONIZATION OF CONTRACT LAW*

Export sales contracts are central to international commercial transactions and around it revolves a series of connected, but distinct, relationships, including cargo insurance, transportation, and payment arrangements. The rules and practices governing such contracts vary from one export transaction to another, based on the agreement of the parties as well as the legal system. National legal systems on contracts may differ, but the basic principles of contracts, such as good faith and consideration, are generally recognized and accepted in many countries. There is also a movement toward convergence among the world's different legal systems in the area of international commercial law (Lubman, 1988; DiMatteo, 1997). Today, it is almost difficult to identify any examples of substantial divergence that produce important and predictable differences in the outcome of commercial disputes (Rosett, 1982). Certain differences in theory or approach are often offset by the countervailing force of international usage or custom, which brings about a predictable and harmonious outcome in commercial dispute resolution. It is pertinent to identify the motives behind the move toward harmonization of international contract law:

- *Increase in trade and other economic relations between nations*
- *The growth of international customary law:* Commercial custom and usage have often been used in the drafting and interpretation of commercial law. Today, certain customs and practices, derived from merchants in Europe, regarding documentary drafts, letters of credit, and so forth, are universally accepted and form the basis for domestic and international commercial law.
- *The adoption of international conventions and rules:* There have been several attempts at unification of international contract law. The most

recent attempt at progressive harmonization of the law of international trade is one undertaken by the United Nations Commission on International Trade Law (UNCITRAL). The UNCITRAL produced a set of uniform rules (Convention on International Sale of Goods or CISG) on international trade that are a product of different national legal systems. The CISG, which came into force on January 1, 1988, governs the formation of international sales contracts and the rights and obligations of parties under these contracts. Many important trading nations, such as France, Germany, Italy, The Netherlands, Singapore, and the United States, have signed or ratified the convention (CISG, 1994). As of September 2004, sixty-three countries accounting for over two-thirds of world trade have adopted the convention. The CISG is largely identical to the provisions of the U.S. Uniform Commercial Code. However, there are several important distinctions (see Table 8.1). The CISG applies to contracts for the commercial sale of goods between parties whose “place of business” is in different nations that have agreed to abide by the convention. “Place of business” is often interpreted to mean the country that has the closest relationship to the contract and is closest to where it will be performed, for example, the place where the contract is to be signed or the goods delivered. Parties to a sales contract are at liberty to specify the application of a law of some third country that recognizes the convention in the event of a dispute. The CISG does not apply to certain types of contracts, such as sales of consumer goods, securities, labor services, electricity, ships, vessel, aircraft, or to the supply of goods for manufacture if the buyer provides a substantial part of the material needed for such manufacture or production (see International Perspective 8.1). The CISG is intended to supersede the two Hague conventions (UNIDROIT rules) on international sales.

### ***CISG: ESSENTIAL ELEMENTS***

#### ***Oral Contracts/Statements***

A contract need not be concluded in or evidenced in writing. Import companies that negotiate contracts by phone may be under the impression that the agreement will not be enforceable since it is not made in writing. However, they could be held liable under CISG if they either verbally accept an offer or their verbal offer is accepted by the other party. The CISG,

TABLE 8.1. The CISG versus the Uniform Commercial Code

	<b>CISG</b>	<b>Uniform Commercial Code</b>
Oral testimony	The provisions of a written contract can be modified by a prior or contemporaneous oral agreement.	A written sales contract between the parties cannot be modified by prior or contemporaneous written or oral agreement
Enforceability of oral contracts	CISG does not require that contracts for sale of goods be in writing to be enforceable. That is, agreements made on the phone, in a meeting are enforceable.	Oral contracts for the sale of goods worth \$500 or more are not enforceable unless the existence of contract is admitted or that there has been payment or delivery and acceptance
Perfect tender rule	A buyer may not reject the goods or cancel the contract unless the nonconformity constitutes a fundamental breach of the contract. Buyer can demand substitute goods in the event of a fundamental breach of contract by seller.	A buyer may reject the goods and cancel the contract even if the defects are not serious and the buyer would have received substantial performance
Specification of quantity/price	A contract is not sufficiently definite if it fails to indicate the goods and does not expressly or implicitly fix or make provisions for determining the quantity and price.	A contract is valid despite missing terms on provisions pertaining to performance and price in so far as the parties intend to be bound by the contract
Revocability of an offer/terms of acceptance	An offer to sell goods becomes irrevocable if it indicates a fixed time for acceptance or states that it is irrevocable or someone acts by relying on the statement. Acceptance of sale offer by buyer/seller occurs upon receipt by seller/buyer, respectively.	A firm offer to buy or sale goods made in writing, promising to keep the offer open for a period (no longer than 3 months) is valid and enforceable. Acceptance of sales offer by buyer/seller occurs when it is mailed or transmitted by seller/buyer, respectively
Additional terms	Expression of acceptance of the contract by buyer or seller that has additions, limitations, or other modifications is considered to be a rejection and a counteroffer.	Expression of acceptance by buyer or seller of contract terms is valid even if it contains additional terms to that expressed in the offer. In the absence of any objections, the additional terms that do not materially alter the offer (other than quantity, price, and warranty) become part of the contract

### **INTERNATIONAL PERSPECTIVE 8.1.**

#### **Chicago Prime Packers versus Northam Trading Co.**

Chicago Prime, a Colorado Corporation (seller), and Northam Trading, a partnership under the laws of Ontario, Canada (buyer), entered into an agreement for the sale of pork back ribs. In March 2001, Chicago Prime contracted to sell 40,500 pounds of pork back ribs to Northam for \$178,200 with payment due within seven days of the shipment. Chicago Prime purchased the ribs specified in the contract from Brookfield Farms (Brookfield) and Northam's carrier (Brown Trucking was hired by Northam) picked up the ribs from Brookfield and signed a bill of lading acknowledging that the goods were in apparent good order. The bill of lading also indicated that the "contents and condition of contents of packages were unknown." Brown Trucking delivered the goods to Northam's customer, Beacon Premium Meats, which also signed a second bill of lading indicating that they had received the shipment in "apparent good order."

As Beacon Premium Meats noticed some unusual conditions with the quality of the meat, it requested inspectors at the U.S. Department of Agriculture (USDA) to examine the product. The inspectors concluded that the inspected product was rotten (that it arrived to Beacon in rotten condition) and condemned the entire shipment. Even after Northam informed Chicago Prime of the results of the USDA's inspection, Chicago Prime continued to demand payment and later filed suit.

At trial, Northam submitted that it was relieved of its payment obligation because the product was spoiled when Brown Trucking received them for delivery to Beacon Prime Meats. The district court awarded Chicago Prime the contract price on grounds that the damage to the goods occurred after the risk had passed to the buyer. It also held that the contract was governed by CISG. Northam appealed stating that: (1) the court erred in placing the burden of proof on Northam to show that the ribs were spoiled at the time of transfer, and (2) the evidence did not support the court's finding.

The court of appeal affirmed the ruling of the district court. It agreed that the contract at issue was governed by CISG. Second, it stated that the CISG did not clearly provide as to which party bore the burden of proving that the product conformed to the contract. Given the similarity of the CISG with the provisions of the UCC, the court interpreted the CISG by comparing it with the general principles of the UCC. It stated that, as the buyer bears the burden of proving breach of implied warranty of fitness under the UCC, the buyer needs to prove nonconformity at the time of transfer to Brown Trucking. Also, Northam did not provide credible evidence to show that the ribs were spoiled at the time of delivery to the trucking company. (408 F.3d 894. 2005 U.S. App.)

however, allows members to opt out of this provision (in favor of domestic law that requires writing).

*Example.* ABC Inc., a cellular phone manufacturer in Florida, contacts various suppliers of semiconductors. The import manager negotiated an oral contract with suppliers in Italy and Germany. Both suppliers orally accepted the offer made by ABC Inc. (type, quality, quantity, price of semiconductors). A few days later, the import manager was advised that a Russian company makes similar goods at lower prices and that the price includes transportation costs to ABC Inc. in Florida. The import manager of ABC Inc. called the suppliers in Italy and Germany to cancel the contract. He thought that oral contracts were not valid and thus unenforceable.

Since each party is located in a different CISG country, CISG applies. The oral contracts with the German and Italian suppliers are enforceable. This means that ABC Inc. is obligated to buy the semiconductors or pay damages.

### ***Parole Evidence***

Prior oral statements (including witness testimony) are potentially enforceable and can be used to challenge the provisions of a written contract. Thus, exporters-importers have to be cautious about representations made during the negotiations which are not intended to be part of the written contract, since oral statements could be construed as part of the written contract (if used to prove intent). One solution is to include an integration clause which states that the written contract was the entire agreement and that no other agreements or evidence, which is contradictory, would be admissible.

*Example.* An Australian supplier of dairy products orally agreed to pay the cost of insurance during transportation of the goods to the buyer's warehouse in Portland, Oregon. However, the written terms of the contract explicitly provided for payment by the U.S. buyer.

The prior oral statement by the supplier is admissible and can be used to modify the terms of the written contract. The supplier would be obligated to pay the cost of insurance.

### ***Battle of the Forms***

A reply to a sales offer which purports to be an acceptance but contains additions or modifications is a rejection of the offer and constitutes a counteroffer. However, if the counteroffer does not materially alter the terms of the offer, it constitutes an acceptance unless objected and notified by the

offeror. Material terms include price, payment, quantity, and quality of goods; place and time of delivery; and liability.

*Example.* A manufacturer of leather shoes in Italy sends a purchase order for 500 pounds of polished leather from New Zealand at \$10 per pound and three year warranty. The supplier in New Zealand accepted the order but modified the terms: "\$12 per pound and two year warranty." The terms added by the supplier are material to the contract, and hence constitute rejections of the offer or are considered a counteroffer.

### ***Duty to Inspect and Proper Notice***

In the event that the buyer receives nonconforming goods, he or she must give timely (within as short a period as is practicable) and effective notice of nonconformity (specify the nature of nonconformity). The buyer's notice, such as "the goods are rancid" or "poor workmanship and improper fitting of the goods," were considered by courts as being insufficiently specific and regarded as no notice.

### ***Right to Remedy Deficiencies***

The CISG permits the seller to remedy the delivery of defective goods after the time of performance has expired unless such delivery would cause the buyer "unreasonable inconvenience and uncertainty." The buyer reserves the right to sue for damages caused by the delay or buy the initial delivery of nonconforming goods.

### ***Exemptions from Liability***

The CISG exempts a party from liability for failure to perform any of his or her obligations due to reasons beyond his or her control and not foreseeable at the time of the contract formation. Prompt notice of the impediment is required to avoid damages. The following circumstances do not give rise to exemptions from liability: financial difficulties of seller's supplier, buyer's inability to obtain foreign currency, increases in the cost of goods, and delivery problems due to production stoppages.

### ***Limitation Period***

There are no provisions in the CISG on limitation period (the time within which a buyer must bring a court action or seek arbitration). Another United Nations (UN convention), "Convention on the limitation period in the International Sale of Goods," provides rules on limitation period and has been

ratified by eighteen countries including the United States in 1994. The convention provides a four-year limitation period for most claims.

The International Chamber of Commerce (ICC) has also published several valuable documents on international trade. The Uniform Rules for Contract Guarantees (1978) deals with the issue of performance and bank guarantees supporting obligations arising in international contracts. The ICC also has rules on adaptation of long-term contracts to changing economic and political circumstances.

Standard contract forms are often used in certain types of international commercial transactions, such as trade in commodities or in capital goods. These contracts are prepared by trade associations, such as The Cocoa Association of London, The Refined Sugar Association, or certain agencies of the United Nations (model contracts for supply of plant, equipment, and machinery for export, or for the export of durable consumer goods and engineering articles).

### ***PERTINENT CLAUSES IN EXPORT CONTRACTS***

An export contract is an agreement between a seller and an overseas customer for the performance, financing, and other aspects of an export transaction. An export transaction is not just limited to the sale of final products in overseas markets but extends to supply contracts for manufacture or production of the product within a given time period. Parties should have a well-drafted and clear contract that properly defines their responsibilities and provides for any possible contingencies. This is critical in minimizing potential conflicts and allowing for a successful conclusion of the transaction.

Although many export contracts are concluded between the seller and an overseas buyer (the main contract), the buyer may also enter into a contract with an independent consultant for technical assistance and with a lender for financing in the case of complex projects. The exporter as prime contractor may enter into joint venture agreements with other firms, such as subcontractors or suppliers, to bid on and perform on a project. Parties could also establish a partnership, corporation, or a consortium in order to bid on and undertake different aspects of the transaction while assuming joint responsibility for the overall project. Such collaboration is common when one firm lacks the financial or technical resources to perform the contract.

It is relevant to state briefly how these joint venture arrangements differ from one another. Members may form a partnership for the purpose of undertaking the export contract. Each of the members remains responsible for the entire transaction even though the parties may be carrying out different

portions of the export transaction. Parties could also establish a new corporation to act as exporters or prime contractors. In the case of a consortium, each partner of the venture has a separate contract with the customer for performance of a portion of the work and, hence, is not responsible to the other members.

### ***Scope of Work Including Services***

The goods to be sold should be clearly spelled out in the contract. There is also a need to include the scope of work to be performed by the exporter, such as installation, training, and other services. The scope of work to be performed is usually contained in the technical specification, which should be incorporated into the main contract (by listing it with the other documents intended to form the contract). It is also important to specify whether the agreed price covers certain services, such as packaging, special handling, or insurance. Any contribution by the overseas customer should be explicitly stated as to the consequences of the failure to perform those services to enable the exporter to complete the transaction on time. Such contributions could include provision of office space and other support services, such as secretarial and translation, government licenses, permits, and personnel necessary for the performance of the contract.

### ***Price and Delivery Terms***

The total price could be stated at the time of the contract, with a price escalation clause that provides for increases in the price if certain events occur. Such provisions are commonly used with goods that are to be manufactured by the exporter over a certain period of time and when inflation is expected to affect material and labor costs. Such a clause also extends to increases in costs arising from delays caused by the overseas customer. It is important to draft the contract with a clear understanding between the parties as to whether such a clause applies when there is an excusable delay. In many contracts, the price escalation clause is in force in cases of excusable delay in performance by the exporter.

The contract should also specify the currency in which payment is to be made. Foreign exchange fluctuations could adversely affect a firm's profit. In addition, government exchange controls in the buyer's country may totally or partially prevent the exporter from receiving payment for goods and services. Hence, it is important to provide the necessary protection against such contingencies. The following contract provisions would be helpful to the exporter.

### *Shifting the Risk to the Overseas Customer*

An exporter may shift the risk by providing in the contract that payment is to be made in the exporter's country and currency. This ensures protection against currency fluctuations and exchange controls.

### *Payment in Importer's Currency*

Even though the seller will generally prefer payment in U.S. dollars, such a requirement may be difficult to comply with if U.S. dollars are not readily available in the buyer's country. The exporter may have to accept payment in the importer's currency. In such a situation, the exporter could fix the exchange rate in the invoice and would thus be compensated in the event of devaluation. Suppose Smith, Incorporated, of California, exports computers to Colombia; the price could be stated as follows: "300 million Colombian pesos at the exchange rate of \$1 5 1,000 pesos. The importer will compensate the exporter for any devaluation in the peso from the rate designated in the contract."

Another method of protection against fluctuations in the importer's currency is to add a risk premium on the price at the time of the contract. Yet another method is to establish an escrow account in a third country in an acceptable (more stable) currency from which payments would be made under the contract.

The contract should clearly indicate the delivery term (e.g., FOB, New York, or CIF, London) since there are different implications in terms of risk of loss, insurance, ownership, and tax liability. The seller would ideally prefer to be paid cash in advance (before delivery of goods or transfer of title) in its own currency or by using a confirmed irrevocable letter of credit. The buyer would often desire payment in its own currency on open account or consignment. Hence, the provision to be included in the contract has to accommodate the competing interests of both parties.

### *Delivery, Delay, and Penalties*

The most common type of clause included in export contracts is one that provides for a fixed or approximate delivery date and that stipulates the circumstances under which the seller will be excused for delay in performance and even for complete inability to perform. Most contracts state that either party has the right to cancel the contract for any delay or default in performance if it is caused by conditions beyond its control, including, but not limited to, acts of God and government restrictions, and that neither of the parties shall be liable for damages (force majeure clause). The force majeure

clause may also cover a number of specified events, including the inability of the exporter to obtain the necessary labor, material, information, or other support from the buyer to effect delivery. It should also include certain warranty obligations, such as delays in manufacture of replacement components. It is important to state that the force majeure (excusable delay) clause will apply even if any of the causes existed at the time of bidding, were present prior to signing the contract, or occurred after the seller's performance of its obligations was delayed for other causes. Some force majeure clauses provide for the temporary suspension of the contract until the causes for the nonperformance are removed; others state that the agreement will be terminated at the option of either of the parties if performance remains impossible for some stated period.

Contracts often provide for damages if the delay is caused by one of the parties. In the event that the delay is caused by the exporter (i.e., unexcused delay), some contracts specify that the importer will be entitled to recover liquidated damages (even in the absence of actual damages), whereas others provide that payment would be limited to damages actually incurred by the buyer (see International Perspective 8.2).

The converse of the seller's obligation to deliver is the buyer's obligation to accept delivery as stipulated in the contract. If delay in delivery is caused by the buyer, most contracts provide that the seller will be entitled to direct damages incurred during the delay, such as warehousing costs, salaries and wages for personnel kept idle, or loss of profit. Some contracts even provide for payment of indirect (consequential) damages, such as loss of productivity or loss of future profits due to delays caused by the buyer. Both parties can possibly eliminate or reduce potential risks of excusable delay by inserting (1) a best-efforts clause, without expressly providing for consequences in the event of delay, or (2) an overall limitation of liability clause. In cases in which the contract does not expressly impose the previous obligation on the customer, the customer remains responsible for delays caused personally or by someone for whom the customer is responsible. In most legal systems a party has an implied duty to cooperate in the performance of the work by the other party or to not interfere with the performance of the other party.

### ***Quality, Performance, and Liability Limitations***

Most contracts state that the seller warrants to the buyer that the goods manufactured by the seller will be free from defects in material, workmanship, and title and will be of the kind and quality described in the contract. It is not uncommon to find deficiencies in performance, even when the exporter

## **INTERNATIONAL PERSPECTIVE 8.2.**

### **Acceptance of Standard International Contracts**

In 1982, a buyer in Indonesia contracted to buy from a seller in England 400,000 metric tons of white sugar (C&F, Indonesian port for delivery in 1983/1984). The contract provided for payment under an irrevocable letter of credit against shipping documents in London. The contract was to be governed by English law and provided for arbitration of disputes in London under the Rules of the Refined Sugar Association. It was also expressly stated in the contract that the buyer was to be totally responsible for obtaining the necessary license and that failure to obtain the license was not to be considered sufficient ground for invoking force majeure.

As sugar prices collapsed during 1982/1983, the buyer declined to open a letter of credit in order to pay the seller in London. In June 1984, the seller commenced arbitration proceedings in London, as provided in the contract claiming damages for breach of contract. The buyer initiated two lawsuits against the seller in London, seeking the court to declare the contracts to be illegal since the Indonesian government declined to buy the sugar and it refused to provide an import license. The seller was awarded \$27 million in damages to be paid in three installments. The buyer paid the first installment and brought a lawsuit against the seller in Indonesia, seeking a court order declaring the contract illegal because it violated a decree stating that only the government agency could import sugar into Indonesia. The Indonesian court held that the contract violated the decree (local law) and was therefore illegal. The court ignored the following:

1. The contracts provided only for shipment to an Indonesian port, not importation into Indonesia, and the risk of not being able to import was expressly assumed in the contract by the buyer.
2. Under English law, delivery of shipping documents does not require that the goods be imported into the country of destination.

*Source:* Adapted from Hornick, 1990, pp. 8-10.

provides a product with state-of-the-art design, material, and workmanship. Hence, it is advisable to use certain approaches to limit risk exposure:

- Specify in the contract the performance standards that are to be met, and provide warranties for those which can be objectively tested, such as machine efficiency, for a specified period, usually a year.
- Stipulate the kinds of damages that may be suffered by the buyer, for which the seller is not responsible, such as loss of profit for machine

downtime, extra costs of acquiring substitute services, as well as other damages that are incidental or consequential.

- Limit the liability, especially in exports of machinery and equipment, to a specific amount expressed either in reference to the total contract price or as a certain sum of money. This limit should cover all liability or liabilities arising from product quality or performance.
- Carefully evaluate the cost implications of an extended warranty or an evergreen warranty provision before agreeing to include it in the contract. An evergreen warranty is automatically renewed each time a failure protected under the warranty provision is corrected.

### ***Taxes and Duties***

In the United States, Canada, and other developed countries, an exporter will not be subject to any taxes (i.e., when products are exported to these countries) if business is not performed through an agent, a branch, or a subsidiary. However, when the price includes a breakdown for installation and other services to be performed in the importing country, such income could be taxable as earnings from services. In some cases, it may be advisable to reserve the right to perform these services through a local affiliate to restrict exposure to foreign taxes. It is thus important to consider the tax and customs duty implications of one's pricing and other export decisions relating to shipment of components or assembly of (final) products. It is also helpful to evaluate the impact of tax treaties with importing countries.

### ***Guarantees and Bonds***

It is quite common for overseas importers to require some form of guarantee or bond against the exporter's default. Public agencies in many countries are often prohibited from entering into major contracts without some form of bank guarantee or bond. Guarantees are more commonly used than bonds in most international contracts. These are separate contracts and independent of the export agreement.

Bid guarantees or bonds are often provided at the first stage of the contract from all bidders (potential exporters) to provide security to the overseas customer. Then, performance guarantees or bonds are provided by the successful bidder(s) to protect the overseas customer against damages resulting from failure of the seller to comply with the export contract. Last, payment guarantees or bonds are provided so the importer can secure a refund of the advance payment in case of the exporter's default.

In the case of a bank guarantee, a standby letter of credit is issued by a bank, under which payment is made to the importer on demand upon failure of the exporter to perform its obligation under the export contract. Most importers favor a contract provision that allows them to obtain payment from the bank by simply submitting a letter that the exporter has defaulted and demanding payment. However, it may be advisable to stipulate in the standby credit that the amount of the credit becomes payable to the importer only upon the finding by a court or arbitration tribunal that the supplier of goods or services is in default of the contract.

A bank guarantee (standby credit) and a bond are similar in that both instruments are a form of security provided by a third party (a bank in the case of a guarantee; a surety company in the case of a bond) to the importer against the exporter's default. Both instruments are issued only if the exporter has a good credit standing, and they both specify the amount payable in the event of default, the period within which such claims can be made, as well as the fee charged for such services (see *International Perspective* 8.3).

In export trade, there is a tendency to make standby credits payable on the submission of a letter by the importer that simply alleges default by the exporter and demands payment. This is not usually the case with bonds, which are payable only when the importer has shown that the exporter is in default under the export contract. Bonds also usually require that the importer has met its obligations under the contract before realizing any benefits from the bond. In short, the surety company will conduct an investigation on the conduct of the parties before making a decision about payment. Second, the bank in the case of a standby letter of credit does not have the option of performing the contract (e.g., completing delivery of goods not made by exporter, paying losses incurred by exporter, etc.), as in the case of a surety company. The bank guarantor is required to pay the full amount of the standby credit without regard to the actual damages suffered. Under a bond, the surety is obliged to make good on only the actual damages suffered by the overseas buyer. In both cases, the exporter has to reimburse the bank or the surety company for any payments made under the guarantee or bond, respectively. In view of the widespread use of guarantees (standby credits) in international trade and the possibility of abuse, many countries provide their exporters an insurance program that protects them against wrongful drawing on the credit. In 1978, the International Chamber of Commerce adopted the "Uniform Rules for Contract Guarantees," which deals with guarantees, bonds, and other undertakings given on behalf of the seller and applies only if the guarantee or bond explicitly states the intentions of the parties to be governed by these rules. In view of the limited acceptance of the Uniform Rules for Contract Guarantees, the ICC adopted, in 1992, the "Uniform

### INTERNATIONAL PERSPECTIVE 8.3. Tendering for Export Contracts

In many countries, government purchases over a certain size are required to be awarded under tender. Purchase of goods under tender is common in cases involving goods and services purchased in large volumes and the likelihood of price competition. Tenders are also offered in the case of contracts for purchase or installation of complex projects that involve the purchase of goods and services. Tenders provide the purchaser the unique advantage of selecting the best supplier from among a large pool of bidders in terms of quality, price, and other factors, allowing the purchaser to avoid charges of patronage and favoritism.

The tendering process begins with a purchaser of goods and services inviting potential suppliers for submission of tenders (bids). However, with important projects, bidders are prequalified before submitting tenders to ensure that they satisfy the basic criteria that are critical for awarding the contract: necessary technical qualifications and compliance with local laws in submitting the bid. The invitation to submit bids (for prequalification or final selection) is usually announced in newspapers and this guarantees a fair, competitive, and transparent tendering process and affords some protection against corruption and nepotism by civil servants.

The invitation to submit tenders is announced in the newspapers to the public or to selected bidders who are prequalified. This stage in the tendering process is often called a request for proposal (RFP). At this stage, potential bidders are invited to submit tenders with certain conditions (e.g., technical specifications, commercial terms, etc.) that are to be included in the proposal. Suppliers may be requested to submit bid bonds to ensure that a supplier will not decline to sign the contract when the bid is accepted.

Once a proposal is accepted, the successful supplier is awarded the contract. In most cases, however, the award is just a first step prior to negotiation of the contract. In the event of failure to conclude the final contract, the customer would have to negotiate with the second bidder on the list.

Rules for Demand Guarantees,” which attempts to standardize existing guarantee practice. As in the case of contract guarantees, the parties have to state their intention to be subject to these rules.

#### *Applicable Law and Dispute Settlement*

The fundamental principle of international contract law is that of freedom of contract. This means that the parties are at liberty to agree between themselves as to what rules should govern their contract. Most contracts state the

applicable law to be that of the exporter's country. This indicates the strong bargaining position of exporters and their clear preference to be governed by laws about which they are well informed. It may be possible to arrange a split jurisdiction, whereby the portion of the contract to be performed in the customer's country will be interpreted under the importer's laws and the portion to be performed in the exporter's country will be governed by the laws of that country.

In cases where there is no express or implied choice of law, it may be the role of the courts to decide what law should govern the contract based on the terms and nature of the contract. The factors to be considered often include the place of negotiation of the contract, the place of performance, location of the subject matter, place of business, and other pertinent matters.

For several reasons, a large and growing number of parties to export contracts provide for arbitration to settle disputes arising under their contracts. Despite the wide use of arbitration clauses, the superiority of arbitration over judicial dispute resolution is not quite clear-cut, and parties considering arbitration should also be aware of the disadvantages in this choice, such as lack of mandatory enforcement mechanisms and difficulty obtaining recognition and enforcement of the award, which requires a separate action of law. It is also stated in some contracts that the parties agree to abide by the award and that the award is binding and final and enforceable in a court of competent jurisdiction.

## **CHAPTER SUMMARY**

### ***Export Contract***

An export contract is an agreement between a seller and an overseas customer for the performance, financing, and other aspects of an export transaction. It also includes supply contracts for the manufacture of a product within a given period.

### ***Factors Behind the Move Toward Harmonization of International Contract/Commercial Law***

1. Increases in global trade and economic relations between nations
2. The growth of international customary law
3. The adoption of international convention and rules
  - The Vienna Convention on international sale of goods
  - The ICC rules on contract agreements
  - Standard contracts developed by trade associations

**CISG: Essential elements:** (1) oral contracts, (2) parole evidence, (3) battle of the forms, (4) duty to inspect and proper notice, (5) right to remedy deficiencies, and (6) limitation period.

### *Major Clauses in Export Contracts*

- Scope of work
- Price and delivery terms
- Quality, performance, and liability
- Taxes and duties
- Guarantees and bonds
- Applicable law and dispute settlement

### **REVIEW QUESTIONS**

1. What are some of the factors that militate in favor of harmonization of international contract law?
2. State the major differences between the CISG and the Uniform Commercial Code.
3. In certain transactions involving transfer of technology, the contract provides for the sale of goods and services. Does the CISG apply to such contracts?
4. The CISG does not apply to certain types of contracts. Discuss.
5. An Italian seller agreed to produce and supply 250 pieces of leather furniture to a buyer in the United States. The contract included certain specifications and was signed by the parties. It further stated that any changes may only be made in writing and signed by both parties. A few days after the contract was signed, both parties agreed by phone to change the specifications. A couple of months later, when the seller delivered the furniture pieces, with the modified specifications, the buyer refused to accept them, stating that the latest agreement was not binding since it was not part of the written (original) contract. Does the CISG apply? If it does, is the buyer obligated to accept the furniture?
6. A manufacturer in California, United States, and distributor in British Columbia, Canada, agreed for the delivery of routers. The contract choice of law clause adopted “California Law.” In the event of a dispute, does it mean that the CISG will not apply?
7. What is the battle of the forms under CISG?
8. Discuss a typical tendering process for export contracts.

9. What are some of the provisions in a typical export contract?
10. How does an exporter protect against foreign exchange fluctuations?

### ***CASE 8.1. CISG***

Wombat, Inc., is a Florida corporation engaged in the rental and sale of tiles, while Pinochet, Inc., is an Italian corporation engaged in the manufacture of ceramic tiles. Representatives of Wombat negotiated an agreement with Pinochet to purchase tiles based on samples examined at a trade show in Bologna, Italy. After finalizing an oral agreement on important terms of the contract such as price, quality, delivery, and payment, the parties recorded these terms on one of Pinochet's preprinted order forms and the president of Wombat signed the contract. The agreement provided for the sale of high grade ceramic tiles at specific discounts as long as Wombat purchased sufficient quantities.

Wombat delayed payments for some of the shipments since it was not satisfied with the quality of the tiles. Pinochet stopped shipments and cancelled the contract with Wombat, claiming that the provisions on the printed form gave him the right to cancel or suspend the contract in the event that the buyer defaulted or delayed payment. Pinochet was not informed of the defects in writing, although the contract provided for notification of any defects in writing by means of certified letter within or no later than ten days after receipt of the merchandise. Wombat argued that the parties never intended the terms printed on the reverse of the order form to apply to the agreement. It also submitted affidavits from translators and Pinochet's representatives that the parties subjectively intended not to be bound by the terms on the reverse of the order form.

#### ***Questions***

1. Is the contract governed by CISG?
2. Are the parties bound by the terms on the reverse side of the print form?

### ***CASE 8.2. CHINA NATIONAL PRODUCTS VERSUS APEX DIGITAL INC.***

China National is a Beijing-based corporation organized under the laws of China with specific foreign trading rights. It facilitates the import and ex-

port of goods between Chinese and foreign companies. Apex is a company incorporated in Ontario, California, and engaged in the import and distribution of consumer electronic goods. In 2000, China National entered into a purchase agreement with Apex for the export of DVD players. The purchase agreement was formalized with the conclusion of several but substantially identical written contracts for the different types of players. Each contract contained two significant provisions: (1) in the event of nonconformity of the goods with the contract, Apex should claim for quality discrepancy within thirty days after arrival of the goods at the port of destination, and (2) all disputes arising from the contract shall be submitted to certain arbitration tribunal specified in the contract and the award is final and binding on both parties.

Apex imported and sold the products to major retailers such as Circuit City, Best Buy, and K-Mart. Soon after distribution of the imported goods, Apex began receiving reports from its retailers that consumers were dissatisfied with the quality of the DVD players: disk loaders did not open, the disk did not load after it was inserted, the player did not recognize certain music files, the front panel of the loader fell off, etc. Some were returned. In spite of these problems, Apex continued to place more orders with China National. It did, however, express its concerns to China National. Apex declined to pay China National, claiming “financial troubles” as well as China National’s refusal to correct the defects. In an effort to obtain payment, China National wrote several letters to Apex threatening legal action. It eventually filed suit in California.

The central issue to be decided by the court was whether Apex rejected the goods or if it did not, whether it later would be relieved of liability. The court stated that if buyers accept nonconforming goods and do nothing, the law deems them to have accepted those goods. Apex’s actions in continuing to order and sell known defective goods constituted an acceptance of those goods. Such conduct of ordering and selling of defective goods was inconsistent with the seller’s ownership and acceptance. It ordered Apex to pay for all unpaid invoices. (Source: 141 F. Supp. 2nd 1013. 2001 U.S. Dist.)

### *Questions*

1. Is the contract governed by CISG?
2. Do you agree with the decision of the court? Why/why not?