Drafting the International Commerce Agreement

Elizabeth F. R. Gingerich
Valparaiso University

Lee Schiffel
Valparaiso University

Crossing national borders necessitates considerations which do not usually characterize domestic decision-making. As pitfalls are inevitable, fundamental knowledge of terms constituting the international agreement may serve to prevent or mitigate loss of trust, compromised business relationships, and adverse financial investment. Due to inherent challenges posed by entering unchartered territories with new business initiatives, all parties negotiating trade agreements must be cognizant of the risks involved. This article provides insight into key provisions, terms, and considerations of which entities entering into an international agreement should be aware.

INTRODUCTION

The international marketplace has become the standard venue for not only multinational corporate transactions, but for long-term business planning for visionary and resourceful entrepreneurs. By definition, international commerce is the voluntary exchange of goods and/or services across national boundaries. Entering into a nongovernmental trade agreement may prove advantageous for all parties involved; however, crossing borders does necessitate considerations which do not usually characterize domestic decision-making. As pitfalls are inevitable, fundamental knowledge of terms constituting the international agreement may serve to prevent or mitigate loss of trust, compromised business relationships, and adverse financial investment.

The Parties

Knowing one's business partner is akin to knowing one's life partner. Whether the contract involves a collective labor group, business investors, or supply chain entities, or consists merely of a licensing or distribution agreement, accurate and thorough identification of the other party is a necessary first step. If a labor pool is involved, the determination must be made whether union representation exists and, if so, whether the anticipated contract may conflict with the terms of a collective bargaining agreement. If multiple businesses are involved, there must be an initial determination of the appropriate officer and/or other representative who has the necessary authority to participate in the negotiations.

Reputation

Conducting trade transactions with foreign suppliers, companies, or governments generates well-founded trepidation. A firm may have a positive national or even international, reputation for following a triple-bottom-line philosophy of doing business (i.e., people, planet, and profits) or, alternatively, carry a stigma of supporting, indirectly or directly, exploitative economic, social, and/or environmental conditions. Conversely, a more positive reputation can be ascribed to certain businesses that have been internationally recognized via particular metrics as producing or supporting superior products and/or services in an eco-friendly and socially-responsible manner. The *Rainforest Alliance* (a nonprofit organization that provides a certification process of goods, services, and other activities that work to preserve biodiversity, http://www.rainforest-alliance.org/); the *Kimberly Process* (a means of certifying that diamonds do not originate from countries where their sale is used to help finance rebel movements and their allies seeking to undermine legitimate governments, http://www.kimberleyprocess.com); the *Organic & Fairtrade Competence Center* (denotes a method of sustainable production of commodities, http://www.organicandfair.org/); and the *Energy Star* certification process (a voluntary program created by the U.S. Environmental Protection Agency that helps businesses and individuals produce products certified as superior energy-efficient consumables, http://www.energystar.gov/) all represent globally recognized sustainability metrics.

International Ratings

Before agreeing to conduct business with a foreign entity, checking the national security rating of that entity's home country may dictate if business can be transacted in a reasonably safe environment. There exists a plethora of resources which ascribe business risk ratings to countries. These ratings are typically based on criteria crime statistics, gender disparity, GDP, governmental stability, and quality of education, healthcare, and infrastructure. *Business Monitor International* (BMI), an independent company founded in 1984 in London, offers such security analyses, business data, and financial forecasts to businesses, banks, governments, and academia to aid in this process (http://www.businessmonitor.com/aboutus.html). For example, during the last quarter of 2011, BMI assigned Kuwait a favorable rating based on data related to these criteria (*Kuwait Defence & Security Report*, Q4 2011).Similarly helpful is the *Shipping Manifesto for Ocean Freight Imports*, or bill of lading (described in a broader context, *infra*). Such shipping documents are publicly accessible and commonly provide detailed activities and characteristics of particular businesses, countries, and governments as well as transaction specifics. Several private sector enterprises have digitalized this information (e.g., http://www.importgenius.com).

Bribery and Corruption

The reputation of a particular trade partner may also be influenced by its laws and common business practices. Implemented under the auspices of the *Organization for Economic Cooperation and Development* (OECD), the Convention Combating Bribery of Foreign Public Officials in International Business Transactions is the only legally-binding standard designed to criminalize acts of bribery of foreign public officials associated with international business transactions. Convention members must prosecute bribes made by their own nationals to foreign public officials – even those operating in countries which may not even be signatories. This uniform proscription thus attempts to eradicate unfair competition while supporting more robust development (Ehlermann-Cache, 2008). As of June 7, 2013, 34 countries (including the majority of the European Union countries and the United States) and six non-member countries (specifically, Argentina, Brazil, Bulgaria, Colombia, Russia, and South Africa) have adopted this OECD-sponsored Convention.

Global Financial Stability

A country's credit rating will inevitably affect a decision to enter into a commercial agreement with an overseas business. A country's banking system and general stability are key to fostering greater private sector investment. As revealed by Standard & Poor's (S&P), Moody's, and Fitch credit rating agencies, the best places to invest currently are rated "AAA." Examples of AAA-rated countries include the UK, Singapore, and Hong Kong.

Unions

Labor unions may be a considerable factor in the negotiating process. The United States is, ostensibly, the home country to many multinational companies. Thus, the participation of labor unions in any international business strategy appears critical for sustained success. Although weakened in recent decades in strength and numbers (particularly in the US), coordinated labor interests remain a viable force in contract talks. It has been alleged that American-based unions have interceded at US corporate headquarters on behalf of foreign unions experiencing labor relations problems with overseas subsidiaries of US companies (Leonard, 1974). The assumption that a potential overseas commercial partner has no unionized workforce to consider may be betrayed by the actual presence of a well-constructed network of union coalitions worldwide. Hence, it is imperative to research the potential demands of labor pools associated with multinational business partners in the course of bargaining.

Governments

Especially when dealing with a trading partner from an emerging market or a developing nation, the business entity must be leery of potential government interference vis-à-vis acts of *eminent domain*, *acts of state*, *repatriation of profits*, or any processes which facilitate a government takeover of a private company. This phenomenon is certainly not exclusive to non-industrialized countries, but may occur whenever economic instability could trigger government intervention. In the case of General Motors (GM), although the US government did not nationalize the company, it did step in after GM filed for reorganization in bankruptcy in 2009 to appoint a new CEO and temporarily acquire over 60% of its corporate stock to prevent anticipated financial ruin and the layoff of millions of workers (King & Terlep, 2009).

Eminent Domain

Eminent domain, as primarily used in the US, permits the governmental “taking” of private property owned by individuals and companies within its borders upon the showing of sufficient public need and upon giving reasonable compensation for the loss incurred. In many countries, such takings do not have to be predicated upon provable public need nor accompanied by reasonable remuneration to the prior owner; these acts simply serve as a means to achieve national financial stability– legitimate or pretextual. These *acts of state* have been used to gain control of utilities, transportation systems, banking operations, and mining operations in many countries (Jennings, 2012). Such shifts of power from private investor to government customer must be accounted for in international dealing (Orr, 2006).

Strategic Coalitions

Achieving a bargaining equilibrium is of utmost importance in international contracts, but not always possible. Contracting parties certainly do not want to be placed in a position of inferiority by accepting a standardized contract proposed by the more established enterprise, especially where there is a paucity of fairness and mutuality of governing terms. Power in size and numbers can influence this equation through the creation and interjection of strategic coalitions. Noria & Garcia-Pont (1991) propose a theoretical framework to better understand the nature of networks of strategic linkages and partnerships in global industries, and argue that membership in *strategic groups* (based upon similarities in capabilities) and *strategic blocks* (based upon similarities in linkages) must be assessed to determine the actual level of bargaining power.

Analysis of Financial Statements

Financial statement analysis can be effectively used to understand a partner’s business during an analysis of strengths, weaknesses, opportunities, and threats (SWOT) and in structuring the contract. A majority of countries have now adopted *International Financial Reporting Standards* (IFRS) or have set a date for complete adoption. Although many countries have adopted IFRS, due to cultural factors, there may be differences from country to country in the application of a given standard.

Since 2002, the United States Financial Accounting Standards Board (FASB) has been working closely with the International Accounting Standards Board (IASB) to converge U.S. Generally Accepted Accounting Standards (U.S. GAAP) with IFRS. (For more information regarding the convergence process, *see* http://www.ifrs.org/Use-around-the-world/Global-convergence/ Convergence-with-US-GAAP/Pages/Convergence-with-US-GAAP.aspx.) The United States has not yet determined if or when it will adopt IFRS. Regardless of the SEC's final decision regarding IFRS, the convergence process has led to significant changes. Hermann and Hague (2006) indicate that international accounting standards and U.S. GAAP increasingly influence each other, with differences narrowing and similarities becoming greater. However, the two boards are approaching the end of their convergence efforts and there are still key areas where differences remain. PriceWaterhouseCoopers (2012) notes, "Although US companies will not be permitted to use International Financial Reporting Standards (IFRS) for US public filings in the foreseeable future, IFRS has been affecting US companies for some time... ." Effects of these differences should be considered carefully when entering into an international contract where the partners are using different accounting standards.

Overall, U.S. GAAP is a highly rules-based system, including the provision of benchmarks (a/k/a, "bright-lines") for accounting treatment differences. Reliance on rules has led to a voluminous set of authoritative literature that the accountant must consider, including not just the standards themselves, but other guidance such as interpretations issued by the FASB. IFRS is more principles-based, establishing a broad set of rules as well as specifying specific numbers. Under IFRS, the accountant's judgment to interpret and apply the standards becomes more critical. This is not necessarily a simple accomplishment as individual judgment frequently differs due to prior experience and cultural differences.

This leads to another difference between IFRS and GAAP: the methodology used to assess an accounting treatment. Under GAAP, the research is more focused on searching through authoritative accounting literature to find the proper rule to apply. Under IFRS, a review of the fact patterns is more thorough, with the ultimate goal of meeting objectives specified by the IASB in its Conceptual Framework. The framework states that the objective of financial statements is to provide information about the fiscal position, performance, and changes of an entity. This is useful in making economic decisions and providing the current financial status of the entity to its shareholders and to the public in general.

In the interim, use of IFRS in the US is uncertain. However, it is clear that convergence has resulted and will continue to result in significant changes having an impact on financial reporting around the globe. For our purposes, parties entering into long-term contracts should be cognizant of how these changes affect the structure of both new and extant financial agreements. Users of financial statements should be aware of, and stay current on, specific differences between IFRS and US GAAP which include:

Inventories

Accounting for inventories is perhaps the largest difference between US GAAP and IFRS. For contracting purposes, it is important that both partners are aware of the inventory method used and the impact the method might have upon any debt covenants or other codicils which rely of financial statement measures. After the revision of IAS 2 Inventories in 2003, the *Last-In-First-Out* (LIFO) valuation method was explicitly prohibited for use by entities following International Accounting Standards to prepare and present financial statements, but is still allowed under other accounting standards, e. g., US GAAP. The main reason for excluding LIFO is because IFRSs shifted focus from the income statement to the *Statement of Financial Position*. The impact of this change in focus requires that *Statement of Financial Position* figures reflect present market conditions, providing the most relevant information with respect to time. Only if items are measured according to current information can the *Statement of Financial Position* be ascertained reliably.

One reason for selecting LIFO is that it yields a tax burden reduction under inflationary economies, i.e., in the times of rising prices. This happens because LIFO assumes that inventory bought most recently will be consumed first in the production process and thus higher value inventory will be included in cost of sales figure. Inventory on hand retains the oldest values. This results in higher costs and ultimately, in lesser profits and lower taxes. In order to use LIFO for tax purposes, a taxpayer must meet the LIFO conformity requirement under US Internal Revenue Code section 472. Specifically, under section 472(c), a taxpayer is prohibited from using a non-LIFO method of inventory to reflect inventory or compute income in a report other than the primary financial statements for the same taxable year.

Intangible Assets

IFRS categorizes costs associated with the creation of intangible assets as either *research phase costs* or *development phase costs*. Research phase costs are always expensed during the period in which they are incurred. Development phase costs are capitalized if they meet a set of six criteria. With limited exceptions, US GAAP requires that both research and development costs be expensed. Thus, recognition of internally-generated intangible assets is rare. The financial statement effect of this difference is that companies using US GAAP, on average, report higher expenses, which lower net income than do companies using IFRS.

However the reader should be aware that separate rules apply in certain conditions. For example, the development of software to be sold to third parties and the development of software for internal uses both have separate guidance.

Revenue Recognition

Due to the rules-based nature of US GAAP, guidance in this area tends to be industry specific, resulting in a large volume of material and neglecting to be relevant as new industries emerge. A recent effort to reorganize US GAAP− referred to as *codification* − has aggregated all revenue recognition literature into one location making it easier to find, but no less cumbersome. It is far beyond the scope of this article to discuss the specifics of US GAAP revenue recognition. A simple comparison should suffice to give the reader a feel for the difference in IFRS treatment. IFRS guidance consists of two primary revenue standards and four revenue-related interpretations. The IFRS literature is broad-based in nature rather than industry specific. Those broad principles are generally applied without further interpretation. Currently, the FASB and IASB are working on convergence on this topic, with a final decision scheduled for the third quarter of this year. Updates on the FASB and IASB project status can be found at http://www.fasb.org/jsp/FASB/Page/LandingPage&cid= 1175805317389.

Categorization of Preferred Stock

Under IFRS, if preferred stock has certain privileges attached that create a liability for the company, then that stock is considered a liability, whereas under US GAAP, all preferred stock is categorized as equity. This can cause a significant difference in the debt-to-equity ratio calculated using IFRS versus using US GAAP. It has been shown that where a company's debt-to-equity ratio could be impacted by IFRS standards, the company may choose to change its financing strategies.

A thorough understanding of the differences in IFRS and U.S. GAAP, or for that matter, any country-specific accounting treatment, should be carefully researched and the contract implications analyzed before trade agreement finalization. Existing contracts should also be reevaluated for any necessary changes as business partners switch from one set of accounting standards to another and consultation with an expert is advised.

THE CONTEXT OF NEGOTIATIONS

L.E.S.C.A.N.T. Factors

A thorough understanding of the contracting entity is largely influenced by the characteristics of the country in which it is based. L.E.S.C.A.N.T. factors (*Language, Environment and Technology, Social Organization, Contexting, Authority, Non-Verbal Behavior, and Time Concept*) delineate the universally-accepted, informal rules for international business transactions which help to provide insight into these intangible variables.

Language and Contexting

Language and contexting are inextricably interwoven. *Low*-context cultures are those that rely on the written word as the controlling factor in the relationship. Little weight is given to the context in which that agreement is reached. Low-context cultures include North America countries– including the United States – as well as Switzerland, Germany, and the Scandinavian countries, except Finland. With low-context cultures, the meaning of the text is explicit and self-contained (Palmer & Schoorman, 1998). Business practices in these countries often separate "the message from the messenger," allowing critique of ideas and behaviors (Elmer, 1993). *Mid*-level-context cultures include France, England, and Asian countries. Business conducted in *high*-level context cultures emphasize relationship-building as well as how and in what setting an agreement is reached (Jennings, 2012). Additionally, high-level context communication can be characterized as being reserved and purposefully ambiguous; conversely, low-level context communication is aptly defined as explicit, direct, and in alignment with the party's individual character (Gudykunst & Kim, 1997). However, while members of low-level context countries are more individualistic than their high-level, collective counterparts, it is important not to stereotype any group as characteristics may vary. Thus, research performed and communications made prior to entering into a commercial alliance may prevent disastrous consequences (Zweifel, 2003).

Environment and Technology

Although businesses have become accustomed to rapid communications systems geared to the exchange and verification of offers and acceptances, it is imperative to first research the type of communication and technology mutually available when considering contracting with a business entity in a developing country. However, as the World Bank (discussed more fully, *infra*) continues to control international lending practices, its loan agreements imbue a more sophisticated manner of contracting and impart a broader use of technological information (Neu, et al, 2006).

Social Organization, Authority, and Non-Verbal Behavior

These factors pertain to the social order of the country wherein the prospective business partner is situated. Before engaging in negotiations, it should be predetermined whether it is customarily appropriate to interject women, mid-level managers, attorneys, or other classifications of agents into the bargaining process. Specific rules of etiquette involving business meals, dress, position of hands, and the various meanings ascribed to non-verbal gestures, are also pertinent to this initial assessment.

Time Concept

Several countries, including the United States, Great Britain, Germany, Canada, New Zealand, Australia, the Netherlands, Norway, and Sweden are all considered *monochronic* nations where the immediate goal of businesspeople is to consummate the deal without delay. Conversely, countries that operate with greater flexibility in time and that consider the social setting, relationship-building, and networking implications of a business deal as important as completing the deal itself are termed *polychronic* nations. These regions include South America, the Middle East, sub-Sahara Africa, and Asian countries (*Cultural Differences*, 2011).

Cross-Cultural Appreciation

Understanding decision-making processes, core beliefs, negotiating roles, legal systems, and bargaining styles of cross-cultural businesspeople should not be underestimated and never ignored. Learning and respecting differences are critical in developing and maintaining sustained business relationships (Sebenius, 2002). Cross-cultural understanding can also mitigate the development of conflicts, or if serious disputes arise, help in the resolution process (Elmer, 1993). Thus, preservation of relationships in the business venture should be viewed as importantly as the business pursuit itself (Tindal, 2011).

Prohibited or Restricted Goods

Although potential business partners may desire that certain goods or services constitute the basis of their contemplated course of dealing, inquiries must be made to ensure that the laws and rulings (i.e., common law, code or statutory law, and judicial decisions) of the countries of exportation or importation will not be violated. Failure to do so could potentially nullify the contract and subject one or both parties to fines, penalties, and even imprisonment. For instance, Article R645-1 of the French Criminal Code prohibits, in relevant part, individuals and enterprises subject to French jurisdiction to "wear or exhibit" in public, uniforms, insignias, and emblems which "recall those used" by an organization declared illegal under the Nuremberg Statute. Others goods have either been similarly restricted or laws, rules, or regulations enacted that prohibit their transfer.

- In an attempt to bolster domestic economies, many countries invoke mandatory *repatriation* − or the return of profits and investments made by domestic companies abroad− back to the home country. Likewise, under *national procurement* policies, governments and tightly-regulated firms may be directed to purchase locally-produced goods even if there are less expensive counterparts available overseas.
- Nation states may also have *import quotas*, restricting the type or quantity of certain goods imported. With import quotas, licenses granted to businesses to import may be limited in scope and number. The license holder, then, is able to purchase these restricted goods and sell them at a higher price in their own home markets, generating *quota rents*.
- If a private party contracts with an overseas entity to import certain goods, the market potential for this merchandise and the importer's bargaining position may result in the creation of *Voluntary Export Restrains (VER)*, whereby the exporter agrees to forestall other trade restrictions associated with that category of merchandise (Keegan & Green, 2002). Similarly, individual nations may have *local content requirements* requiring that a certain portion of a good be produced domestically before public distribution. While this restriction does not necessarily impose an import quota, the end result is that if local businesspeople purchase more products from overseas markets, more capital will be required to be spent in the home country before those goods are sold (Keegan & Green, 2002).

INTERNATIONAL VENUES AND CONVENTIONS

Traditional barriers (language, legal systems, cultures, dispute resolution institutions, and mandatory procedures) to cross-border trade transactions have been greatly reduced in part due to uniformity of worldwide business practices, adoption of internationally-recognized standards and guidelines, passage of international business conventions, and the general proliferation of international trade agreements and treaties. Several documents, guides, tribunals, and venues, in addition to the OECD, which facilitate private international trade transactions include:

(1) The *International Institute for the Unification of Private Law (UNIDROIT),* headquartered in Rome, is an intergovernmental organization designed to harmonize private international law by drafting global conventions and model laws. In 2010, UNIDROIT drafted the *Principles of International Commercial Contracts (PICC)*, designed to provide increased uniformity in international commercial contracts law (DiMatteo, 2001).

(2) The *United Nations Commission on International Trade Law (UNCITRAL)* is the primary legal body of the United Nations, specializing in commercial trade law reform. The commission has worldwide membership and works toward the modernization and harmonization of international business rules by creating globally acceptable model laws, conventions, and procedures. This legal body also provides professional opinions, guides, and expert assistance in legal reform (http://www.uncitral.org/).

(3) The *Hague Conference on Private International Law (HCCH)*, formed in 1893, is universally regarded as the preeminent organization governing private international law. Its main charge is to

"work for the progressive unification of the rules of private international law" and has pursued this objective by creating and helping to implement various multilateral conventions and by promoting the synchronization of laws permeating global trade. Currently, seventy-two nations are members of the Hague Conference, including the US, the BRIC countries (Brazil, Russia, India, China), and all 27 member states of the EU (www.hcch.net).

(4) The *United Nations Convention on Contracts for the International Sale of Goods (CISG)* – also known as the *Vienna Convention* – is a treaty developed by UNCITRAL offering a uniform international sales law to avoid "choice of law" issues. As of August 2010, the CISG had been ratified by 76 "Contracting States" (including France, US, and China). The CISG governs a significant proportion of world trade and unless excluded by the express terms of the contract, the provisions of the CISG will be deemed to be incorporated into, or, where necessary, supplant, any otherwise applicable domestic law (http://www.cisg.law.pace.edu/).

(5) The *International Chamber of Commerce (ICC),* established in 1919 in Paris to serve global business by opening up new markets for trade and investment in goods and services, has advanced in its original mission by creating methods of resolving international trade disputes through its International Court of Arbitration. Additionally, the ICC provides Commercial Crime Services (London-headquartered) to the world business community equipped with a centralized commercial crime-fighting body designed to prevent, investigate, and prosecute maritime, counterfeiting, financial, and intellectual property criminal activities.

(6) Formed in the US following WW II, the primary objective of the *International Monetary Fund (IMF)* was initially to expand international trade through a lending system designed to stabilize currencies in emerging markets and developing countries. The IMF created the International Bank for Reconstruction and Development, more commonly referred to as the *World Bank*. While the IMF and the World Bank are essentially twin pillars of an intergovernmental financial institution, the fundamental purpose of the World Bank is to foster global development while the IMF is more of a cooperative institution which maintains an orderly system of international payments and receipts (Driscoll, 1996).

(7) *The General Agreement on Tariffs and Trade (GATT)* – replaced in 1995 by the *World Trade Organization (WTO)* – was a multilateral agreement regulating global commerce. Its core purpose was the reciprocal reduction of tariffs and other trade barriers throughout the world. While GATT constituted a set of rules agreed upon by member nations, the WTO is an institutional body which has broadened its purview to include trade in services and intellectual property (http://www.wto.org).

(8) As foreign trade in commodities and services has increasingly involved intellectual property components – i.e., copyrights, trademarks, trade secrets, trade dress, and patents – universal protections have been promulgated. The *World Intellectual Property Organization (WIPO*) (Geneva, Switzerland) administers twenty-five multilateral treaties.

THE AGREEMENT

Once the parties and goods or services have been identified, appropriate relationships initiated, risks assessed, and relevant laws and accounting standards researched, the terms of the international agreement should be memorialized in a carefully prepared document, addressing:

Risk of Loss

The international transfer of goods is inherently complex and fraught with perils and risks as the journey involves transport to the carrier, loading, main transport, unloading, and ultimate delivery to point of destination. The transfer of goods from the seller to the buyer presents an element of risk that implicates general economic and legal consequences. The parties must predetermine who will bear the responsibility for losses at every juncture of the journey.

Subject-Matter Description

While the contract will identify whether subject-matter of the agreement pertain to goods (tangible or intangible) or services, the subject-matter should also be expressly noted as either "exported" or "imported." Identifying the subject-matter for shipment necessitates a preliminary determination of export/import tariffs and other related costs. To simplify this process, the US Department of Commerce has provided a *Harmonized System (HS)* which assigns a 6-digit number to each good traded internationally and adds four additional numbers assigned from foreign countries that voluntarily participate in this coding framework. The US maintains a comprehensive register of products under its *Schedule B System* which indicates applicable tariff rates and import fees (http://www.census.gov/foreign-trade/schedules/b/).

Terms and Methods of Payment

There are several options of payment which may be used in overseas commercial transactions. For instance, when the manner of payment is stated as "cash," the parties could be agreeing to an exchange of currency in the form of hard money, electronic debits, bank notes, securities, bills of exchange, personal checks, letters of credit, promissory notes, or bonds. The phrase, "cash against warehouse receipts," indicates transferal of the agreed upon method of consideration only when documentation of ownership is produced by a holding facility to the buyer/importer. Payment can be additionally extended to give the buyer a sufficient opportunity to inspect the quality of the cargo (Keegan & Green, 2002). Other common terms of payment include:

(1) Bill of Lading. As discussed *infra*, a bill of lading is technically a document of title to the goods in question as well as evidence of the contractual relationship between the consignor of the merchandise and the shipping firm or carrier. It functions as a receipt from the carrier who, in turn, provides the details of a particular shipment. The buyer/importer often uses the bill of lading to secure the necessary loans from its bank to make payment for the imported goods even before the arrival of the shipment. These documents are the primary manner for the seller to prove that it has fulfilled the duty of delivery while providing the buyer with the confirmation to pay the purchase price (Keegan & Green, 2002).

(2) Letter of Credit. The primary instrument of payment for an international sales transaction is through a letter of credit. A letter of credit is a mechanism which allows the buyer/importer to offer a secure method of payment to the seller/exporter. Several banks may be involved in this process, allowing the buyer to shift the risk of loss to the financial institution. Thus, a letter of credit is a payment undertaking given by a bank that is issued on behalf of the applicant (usually, the buyer/importer or its agent) (Keegan & Green, 2002).

Choice of Currency

Recent austerity measures implemented across many member-states of the EU, as well as effects of the global credit and financial crisis of 2008 generally, have invariably affected the value and stability of foreign currencies. Unstable economies could easily trigger currency devaluations, leaving predictability of any given monetary unit in flux (Lee, 2013). The contracting parties must come to an agreement as to the form of currency to be used in business negotiations and financial forecasts. If either of the contracting parties has an edge in bargaining power, this term may well be dictated with little input from the aspiring, subordinate partner.

Choice of Language

There should always be a "choice of language" clause designating the official language to be used in interpreting and guiding the terms of the agreement. The choice should be agreed to without compromising or minimizing the culture of the other. Even with a mutually chosen language, it should be noted that various meanings could still be ascribed to the contractual verbiage used without the inclusion of a comprehensive definitional section. At present, an increasing number of multinational enterprises are requiring the use of English in their corporate chains of command to facilitate communication, geographical performance, and cultivate new endeavors and relationships (Neeley, 2012).

Choice of Law

Increasing competitive challenges and globalization and have resulted in the adoption and application of newly-developed, legally binding, voluntary standards, developed at both national and international levels to help improve trade and investment as well as to foster ethical dealings and maintain mutual integrity. Before particular laws are chosen under which the terms of the contract are to be interpreted, the parties should thoroughly assess their respective bargaining positions and the general economies of the countries of origin and destination. Implementation and enforcement of particular standards may have far-reaching consequences impacting investment opportunities, international ratings, and loan policies.

Application of Trade Agreements

Free trade agreements (FTAs) and Regional Trade Agreements (RTAs) collectively guide the flow of commerce in particular regions in the world. The primary objective of most FTAs and RTAs has been to encourage foreign investment between nation-members by reducing trade barriers and tariffs. An amalgamation of geo-political, security, and economic concerns are typically the main motivating factors supporting the creation of these alliances (Khatoon, 2010). The US and the EU are parties to a number of regional FTAs while the number of RTAs has dramatically increased from 250 in 2003 to 462 in 2010 (Khatoon, 2010).

Choice of Forum

In addition to pertinent treaties and laws, the parties should decide where disputes should be settled. *Forum clauses*, which specify a particular court, jurisdiction, or authority, are increasing in importance especially as over-the-border e-commerce proliferates. Arguments could be made that the relevant jurisdiction would be where the primary business activity occurs, e.g., the manufacture of goods. A more common practice today is to attempt to avoid judicial forums altogether in favor of alternate methods of dispute resolution (*Encyclopedia of Business*, 2009).

Dispute Resolution

As previously discussed, even the best crafted agreement will result in contentious conflict – over the meaning of certain contractual terms, the quality of goods or services proffered, or which party bears the risk of loss for a compromised shipment. Commercial contracts should set forth in great detail the method of alternate dispute resolution (ADR) preferred (assuming that judicial intervention is waived as the primary means of resolution). Alternate dispute resolution mechanisms include mediation and arbitration. Mediation is a process designed to quell more adversarial processes such as litigation and arbitration. A third party – often an individual or panel of individuals well-versed in the type of transaction involved – acts to promote more effective inter-party communication to help resolve the problem or issue at hand (Bowen, 2005). In the majority of cases, however, parties involved in international commerce have submitted to binding arbitration to rectify disputes (Bowen, 2005). This process allows the parties to present their arguments before a neutral arbiter whose ultimate decision cannot be contested unless in cases of provable fraud and collusion (Gingerich, 2007). Both forms of ADR offer ways to overcome impediments inherent in international commercial disputes and prevent the breakdown of the business relationship while offering flexibility, creativity, privacy, and less delay and cost.

There are certain unique characteristics of long-term, foreign-trade agreements whereby a strong system of international commercial arbitration is argued to be the most effective method of handling such issues (Holtzmann, 1969).

Tender

"Tender" is a trade term which means that the seller/exporter places goods that conform to their contractual description at the buyer's/importer's disposition. A valid tender indicates that the goods have met all import regulations and are ready for pickup, usually at an independently-owned warehouse, by the buyer. During the time of storage, goods usually can be kept without the incursion of tax liabilities until they are removed. In some instances, the seller is given a specific time period within which to deliver the goods as well a reasonable time thereafter to rectify any portion of the merchandise that fails to pass inspection.

Terms of Delivery

The global market mandates that delivery terms should be one of the essential clauses of a contract between international partners. There are trade terms uniquely associated with the entry of goods from one foreign country to another.

- *Advice of Arrival* is a phrase that mandates that the seller must inform the buyer (directly or through a pre-designated agent) when the goods have arrived at their destination. Such advice usually accompanies the warehouse name and location. If the notification is given verbally, it must be followed with written confirmation on the same day such as by express letter, printed message, or telegram (http://www.ace-group.net/Glossary.aspx).
- With a *Destination Contract*, the seller has the obligation to deliver the goods to the buyer's stated point of destination (e.g., the buyer's headquarters or a particular bonded public warehouse) – not simply deliver them into the hands of a carrier.

Additionally, there exist several sets of trading terminology that attempt to simplify the preparation of commercial contracts (Căruntu and Lăpădusi, 2010). Supplementing, or at times supplanting, the UCC or even CISG terminology is the ICC's set of International Commercial Terms more commonly referred to as *Incoterms* (Morrissey & Graves, 2008). Relevant Incoterms include:

(1) ***Delivered Duty Paid*** or "DDP" requires the seller to arrange shipment, obtain, and pay for import or export permits, and guide the goods through customs to a named destination.

(2) ***Cost, Insurance, and Freight*** or "CIF" – requires the seller to bear the risk of loss until the goods reach the buyer's destination port. Unless stated differently, the buyer must present proof of ownership documents to seller's selected carrier, pay for customs dues, inspections, and ultimately for port-to-door transportation.

(3) ***Ex Works*** or "EXW" obligates the buyer to bear all of the expenses and risks associated in moving the seller's goods from the seller's place of business (factory or warehouse) to the established destination arranged with the buyer.

(4) ***Delivered at Terminal*** or "DAT" is a relatively new Incoterm and refers to the delivery of goods by any means of transport. It obligates the seller to bear the risk of loss until the goods reach their designated terminal *and* are unloaded. From that point, the buyer assumes the risk. The seller typically bears the expense and risk associated with the activities inherent in export clearance procedures while the buyer must undertake importation customs clearance (http://www.free-logistics.com/incoterms/entregado-en-term inal-dat.html).

(5) ***Free on Board*** or "FOB" denotes the passage of the risk of loss to the buyer. With an FOB contract, the seller's obligations are fulfilled when the ordered goods are tendered to a vessel chosen by the buyer. Even though a stated price of particular good appears reasonable, costs of insurance, transportation, customs, and inspections must still be calculated by the buyer (http://www.wcscargo.com/wordpress/shipping-dictionary/incoterms/).

Quantity

Precise language delineating the quantity of the item to be imported or exported is one of the most important terms to include in an international commercial contract. Without it, a court may be precluded from enforcing the contract in its entirety. The parties must agree to a particular form of measurement, e.g., kilos, bags, bales, or drums.

Packaging and Weight

Packaging requirements can be used as a condition for acceptance of imported commodities and subsequent payment therefore. The contract should clarify the type of packaging to be used, including the exact materials to be used to construct the main container, the outer covering, and the inner lining; how such materials are to be assembled (e.g., stapled, adhered, or sewn – by hand or machine) and the exact size and condition (e.g., new, used, clean, or uniform). Bales may be the preferred type of packaging for bulk road transport, but with shipping freight, sturdier barrels of steel or other like materials may be required.

In some contracts, *delivered* and *shipped* weights should be distinguished. During shipping, some loss can be attributed to the type of goods transported (spoilage of fresh produce, for example) or the mode of transportation chosen. Weight clauses should also specify accepted standards of measurement (e.g., the metric system). Bulk shipments are typically only allowed if expressly agreed to by the parties. The precise weight per unit can be *exactly* stated or *approximately* stated. The parties' agreement that the subject goods may be delivered in *partial* shipments must be unambiguously stated.

Modes of Transport

Common acceptable means of transport include air, ship, railway, and parcel post. It must be determined not only who is responsible for the costs associated with the transportation of the goods, but the costs incurred from the seller's point of origin to the primary carrier, then from the port or tarmac to a holding facility, and ultimately to the buyer's final point of destination.

Force Majeure

All parties to trade agreements need to protect themselves from uncontrollable or unforeseen events which may render the performance of their respective obligations impracticable or impossible. A "force majeure" clause should include language stating that neither party should be liable to the other for damages if the performance of their duties is hindered by conditions beyond their control. These events could include natural disasters (earthquakes, hurricanes, floods), governmental actions (denial of customs processing), and manmade events (workers' strikes, insurrections, and/or acts of terrorism).

Noncompetitive Covenant

Either or both parties may strongly desire a restricted agreement – one which narrows where business activities are to be transacted and forbids engaging in similar practices with competitors. These "covenants not to compete" or "restricted covenants" concern geographical and time restrictions. Maintaining exclusivity of dealing with a certain supplier or importer for the transfer of particular goods and services for a set period of time and covering a demarcated region are typically upheld if reasonable in scope and duration.

Contract Defenses

Since many international contracts are prepared by the dominant, more established business enterprise, the other party possessing less bargaining power is not without defenses. If the terms are so one-sided, the subordinate party may interject the defense of "unconscionability" – which indicates the terms of the contract are excessively unfair to the weaker party. Good faith and fair dealing are expected of both actors when CISG tenets are invoked, regardless of the economic orientation or the political or ideological differences of the parties' home states. UNIDROIT's "Principles of International Commercial Contracts" furnish a supplementary set of principles used in conjunction with the CISG. Likewise, if liquidated damages provisions (discussed *infra*) transcend the assessment of fair damages in the event of a breach, the clause may be forfeited as a penalty and stricken from operation accordingly (DiMatteo, 2001).

Insurance and Tariffs

The parties must delegate who will be ensuring not only the safe passage of the goods, but for each step that the possession of the goods is transferred. The expiration of coverage must be unequivocally stated, e.g., seller's insurance duties terminate when the imported goods are delivered at a bonded public warehouse in the country of importation. As insurance coverage can be segregated to cover various segments of the journey, one option would be to purchase a *"W/W"* or warehouse (exporter/seller; point of origin) to warehouse (importer/buyer; point of destination) policy of coverage (Keegan & Green, 2002).

Exported and imported goods are subject to tariffs and other charges imposed by the governments of all countries involved. International contracts should precisely designate the entity that is responsible for these charges. Typically, the seller/exporter in an international trade agreement is responsible for all export taxes, duties, or other charges levied whereas similar fees assessed by the importing country are usually borne by the buyer/importer. There are different types of levies. A tax which produces government revenue – more commonly referred to as a *tariff* or a *duty* – can be assessed on both imported and exported items by the customs authorities of that country. This charge also helps to protect domestic industries from would-be predatory competitors overseas. Customs duties may consist of a charge based upon the value of the items or be premised upon the volume and/or weight of the cargo shipped (http://www.businessdictionary.com/definition/customs-duty.html#ixzz2W1wqmbgJ).

CONCLUSION

With increasing globalization and Internet-based trade transactions, the rapid proliferation of international business initiatives is unparalleled in history. Because of the inherent challenges posed by entering unchartered territories with new business initiatives, all parties negotiating trade agreements must be fully cognizant of the risks involved as well as the topics to be researched and addressed to create a situation of trust, sustained relationship-building, and responsible, long-lasting success.

REFERENCES

Bowen, A.A. (2005). The power of mediation to resolve international commercial disputes and repair business relationships. *Dispute Resolution Journal*, 60, (2), 58-65.

Căruntu, C. & Lăpădusi, M. (2010). Complex issues regarding the role and importance of internationally codified rules and incoterms. *Petroleum - Gas University of Ploiesti Bulletin, Economic Sciences Series*, 62, (1), 98-110.

Choice of Forum Clause. *Encyclopedia of business in today's world, volume 1*, C. Wankel (Ed) (2009). Thousand Oaks, CA: Sage Publishing.

Driscoll, D.D. (1996). The IMF and the world bank: How do they differ? *Retrieved 15 June 2013*: http://www.imf.org/external/pubs/ft/exrp/differ/differ.htm.

DiMatteo, L.A. (2001). A theory of efficient penalty: eliminating the law of liquidated damages. *American Business Law Journal*, 38, (4), 633-734.

Ehlermann-Cache, N. (2008). The impact of the OECD anti-bribery convention. *Retrieved 7 June 2013*: http://www.oecd.org/mena/investment/39997682.pdf.

Elmer, D. (1993). *Cross-cultural conflict: Building relationships for effective ministry*, Downers Grove, IL: Intervarsity.

Gingerich, E.F.R. (2007). Enforcing arbitration agreements in discrimination claims: Judicial reconsideration? *Employee Rights Law Journal*, Fall.

Gudykunst, W. & Kim, Y. (1997). *Communicating with strangers: An approach to intercultural communication* (3rd ed.), Boston, MA: McGraw-Hill.

Hermann, D. & Hague, I.P.N. (2006). Convergence: In search of the best. *Journal of Accountancy*, 201, (1), 69-73.

Holtzmann, H.M. (1969). Long term multinational disputes: A challenge to arbitration. *Arbitration Journal*, 24, (4), 234-238.

IFRS Foundation and the IASB. *Retrieved 6 June 2013*: http://www.ifrs.org/Use-around-the-world/Global-convergence/Convergence-with-US-GAAP/Pages/Convergence-with-US-GAAP.aspx

International Ratings. *Retrieved 11 June 2013*: http://www.businessmonitor.com/aboutus.html.

Jennings, M.M. (2012). *Business: its legal, ethical and global environment,* (9th Ed.), West-Thomson Learning/Cengage.

Keegan, W.J. & Green, M.C. (2002). *Global marketing management*, (7th Ed.) New Jersey: Prentice Hall, Inc.

Khatoon, S. (2010). Impact of US FTAS on the economies of Israel, Jordan and Bahrain. *International Journal of Business Insights & Transformation*, 3, (2), 21-32.

King, N. Jr. & Terlep, S. (2009). GM collapses into government's arms. *The Wall Street Journal*, 2 June.

Lee, D. (2013). G-20 moves to allay fears of 'currency war.' *Los Angeles Times*, 16 February 2013. *Retrieved 10 June 2013*: http://articles.latimes.com/2013/feb/16/business/la-fi-mo-g20-currency-war-20130216.

Leonard, A.S. (1974). Coordinated bargaining with multinational firms by american labor unions. *Labor Law Journal*, 25, (12), 746-759.

Morrissey, J.F. & Graves, J.M. (2008). *International sales law and arbitration*, New York: Aspen Publishers.

Neeley, T. (2012). Global business speaks english. *Harvard Business Review*. *Retrieved 9 June 2013*: http://hbr.org/2012/05/global-business-speaks-english.

Neu, D., Ocampo Gomez, E., Graham, C. & Heincke, M. (2006). "Informing" technologies and the world bank. *Accounting, Organizations & Society*, 31, (7), 635-662.

Nohria, N. & Garcia-Pont, C. (1991). Global strategic linkages and industry structure. *Strategic Management Journal*, 12, 105-124.

Orr, R.J. (2006). Living agreements for a risky world. *Harvard Business Review*, 84, (4), 20-21.

Palmer, D. & Schoorman, F. (1999). Unpackaging the multiple aspects of time in polychronicity. *Journal of Managerial Psychology,* 14, (3/4), 323-344.

PriceWaterhouseCoopers (2012). IFRS and US GAAP: similarities and differences. http://www.pwc.com/us/en/issues/ifrs-reporting/index.jhtml?gclid=CJLg782G7rgCFZFaMgodLksAxg

Sebenius, J.K. (2002). The hidden challenge of cross-border negotiations. *Harvard Business Review*, 80, (3), 76-85.

Security Risk Analysis. *Kuwait Defence & Security Report*, Q4 2011, (4), 43-47.

Tindal, L. S. (2011). Conflict resolution: Cultural understanding imperative. *Journal of Values-Based Leadership*, IV, (II), 20-25.

US Department of Commerce Harmonized System and Schedule B. *Retrieved 15 June 2013*: http://www.census.gov/foreign-trade/schedules/b/.

Zweifel, T.D. (2003). *Culture clash: Managing the global high-performance team*. New York: SelectBooks.