CONTROLLING THE TERMS OF SALE

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In attempting to understand who should control the terms of sale and what the parameters are in the decision-making process, several critical factors must be reviewed.

The Incoterms, published by the International Chamber of Commerce, advises on and provides definitions for terms of international trade. They include CIF, FOB FAS, all acronyms for potential terms of sale that the U.S. exporter needs to understand to conduct successful international trading. An exporter can obtain a copy of the Incoterms booklet, which should be part of every exporter's library, from any International Chamber of Commerce, or ICC Publishing Corporation, Inc. 1212 Avenue of the Americas, New York, NY 10036 or www.iccbooks.com.

OVERVIEW: SALES TERMS

The various terms of sale have significant consequences regarding responsibilities, liabilities, costs and profits or losses confronting both the importer and exporter. The Incoterms are European in foundation, reflecting a different mind-set. The terms combine documentary and transactional requirements for passage of title and payment terms. There are many hidden costs involved in international trade that the Incoterms help to define. The exporter should be aware that terms of sale directly affect costs and could affect an exporter's competitive advantage. The more responsibility assumed, the higher the price. For example, the price might be $4,500 from the plant dock, $4,800 to the U.S. port of export and $5,800 delivered to the customer's door in Oslo, Norway.

The Incoterms advise who is responsible for arranging transportation services, freight charges, insurance and other logistics. Freight forwarders, banks, carriers and experienced shippers are the best resource for figuring out what they are all about.

NAME THE TERMS AND THE POINT OF SHIPMENT

When using the terms, a point of destination or a site must be named. For example, if you were selling free on board or FOB, the question is "FOB at what point?" According to the definitions of the terms, once the goods are loaded on board the transportation conveyance, title passes to the buyer. But does this occur at the plant or at the port?

If you sell FOB plant, the title will pass once the freight has been loaded on board the inland conveyance. This means that the buyer will arrange to pay for the inland transportation. They will also assume responsibility for loss or damage to the freight during transit.

Choosing to sell FOB port of loading requires that the exporter arrange for the inland freight. The exporter will then assume all transit liabilities until the freight is transferred to the international carrier. If it is an ocean shipment, the risk transfers once the freight passes the rail of the vessel, illustrating the extent of the definition of the terms.

If you had an international transaction in France that called for a cost, insurance, freight or CIF sale with a named point, such as Paris and the shipment was by air, the exporter would be responsible for arranging the transportation. The shipper would assume all transit liabilities and provide marine insurance up to the point of pickup from the Paris airport. In such a case, the exporter has taken on a great deal of responsibility and with it an equal amount of risk. This is when the exporter needs to be a good traffic manager and/or have a quality freight forwarder. The marine insurance, the underwriter and the claims systems must all be in place to deal with the potential losses in an international transaction.

TERMS OF PAYMENT

At the time the export sale is being consummated, the terms of payment need to be decided, as this will have a great effect on the decision making for the terms of sale. Assume, for example, that you complete the transaction with all i's dotted and t's crossed, with the terms of sale as FOB/NY. The shipment is made with the terms of sale calling for a payment from your buyer in Paris in sixty days. The shipment arrives missing three of ten pieces. They represent approximately $12,000 of the total invoice value, for which your buyer discounts your bill. You argue that the "risk" passed in New York; therefore the insuring responsibility, with a clean bill of lading, was with the buyer from the time the freight was received on the international conveyance.

The buyer argues that the shipment showed up short and that under no circumstances — if the U.S. exporter is to keep the account — would he contribute to the loss, holding the exporter fully responsible. According to this scenario, while the terms of sale "appeared" to offer less exposure to the exporter, the terms of payment that allowed sixty days provided greater exposure. The position of the importer was both unreasonable and incorrect, but it is a common path when the buyer holds the advantage of not yet having paid for the freight.

Without contingency insurance of unpaid vendor protection, the exporter may have to sue to collect — at the cost of losing a customer, unnecessary aggravation and great expense.

ADDITIONAL CONSIDERATIONS

A very general conclusion that can be drawn is that in most export situations, the exporter should control the terms of sale as well as the terms of payment. Every factor must be considered in this evaluation, such as, but not limited to the following:

- Price and payment terms
- Competitive pressures
- Forwarder and carrier options
- Opportunities for loss and damage
- Previous experience with buyer
- City and country of destination
- Customs clearance in buyer's country
- Current economic and political situation in buyer's country

An additional consideration in controlling the terms of sale offers the exporter short- and long-term options for maintaining competitiveness. If you choose to sell on terms — where all the basic shipping, documentation, insurance and freight choices are in your control — then you have the ability to affect the CIF costs. You are not forced to accept a particular insurance company whose marine rates may be higher than you can obtain in the open market. If you are free to choose steamship lines, you have the option to look at possible non-conference carriers that might offer lower shipping costs. Each variable must be evaluated. Controlling the option to evaluate will afford the more competitive choices that will work to the exporter's advantage.

Another important consideration in determining the terms of sale is to look at the pitfalls of attempting a "door-to-door" sale, if required to do so, particularly in certain countries where customs law and practice work to the disadvantage of the exporter.

As "importer of record" in door-to-door sales, you assume certain liabilities in the import country that you might want to reconsider.

In certain countries, such as Mexico (though this situation is changing), U.S. exporters have found it preferable to sell FOB port of entry such as Laredo, in lieu of a CIF sale point of destination. Mexican customs (their trade and practice) have afforded the importer a better opportunity to arrange clearance than with the exporter's agent. This is also true in other countries such as, but not limited to Thailand and Algeria. Each situation must be carefully evaluated on its own merits. The exporter's freight forwarder's local relationship with foreign clearance agents plays a vital role in this regard.

The current political and economic situation in the buyer's country is critical. Take the situation in certain parts of the new Eastern Europe. While there is a big demand for U.S. products, payment is difficult at best. In order to make the sale, the U.S. exporter may not be able to sell completely on secured terms but may be willing to sell on a collect or sight draft basis. This arrangement might meet the need of the importer and reduce some of the exporter's exposure.

The key word is "reduce" not "eliminate." The exporter will need to make arrangements through the freight forwarder or the carrier not to release the freight until the payment is made to the local representation. Good communication and tight monetary controls will be critical to successful execution of this option.

Equally important is attention to the minutia of transactional detail for the passage of title and payment terms. Although title may transfer, responsibility, particularly fiscal responsibility, may not end.

Quality marine insurance affords protection to the exporter in all situations. The marine insurance contract should have features that protect the exporter regardless of who is responsible to insure and where title passes. "Unpaid vendor" or "contingency" insurance can be part of any successful export program. It will afford the exporter full transportation insurance in cases where they are not responsible for insurance, but may be exposed to payment or contract terms.

It is also critical when letters of credit are used for international transactions that the term of the sale conform to Inco practice as well as Uniform Customs and Practice (UCP) 500 for payment terms.

The bottom line is that the exporter must evaluate many issues in determining the best terms of sale for a particular export transaction. In any case, the exporter should negotiate a controlling advantage that will mitigate potential loss and maximize protection of profits.