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## **Analysis of Incoterms as Usage Under Article 9 of the CISG**

William P. Johnson

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## ANALYSIS OF INCOTERMS AS USAGE UNDER ARTICLE 9 OF THE CISG

WILLIAM P. JOHNSON\*

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## 1. INTRODUCTION

Imagine strolling along a pier in an exotic port of call located in some strange land. Massive, dark, ocean-going vessels are docked at the nearby quay to unload vast quantities of precious cargo. Seagulls and an occasional albatross swoop out over the sea in search of an elusive meal, while deceptively powerful waves pull urgently at the pier. Stevedores bark out instructions in foreign tongues, and sailors softly sing sea shanties audible only when the ocean breeze is just right. The subtle taste of brine is in the air; it's surprisingly pleasant and already invokes a feeling of nostalgia.

There is a mystery and an excitement to the port of call, in fiction and in life. It seems appropriate that, swirled into this seaside mélange of sights, sounds, and tastes, are mysterious customs and practices of merchants trading their wares – customs and practices that have evolved through the ages. The documents used in international trade contain terms of art that reflect those practices and are well-understood only by the initiated. In those documents, the merchant and his lawyer will employ cryptic delivery terms: “EXW supplier’s factory, Cape Town”; “FOB port of shipment, Shanghai”; “CIF port of destination, Rotterdam”; “DDP buyer’s plant, Chicago”; and numerous others.<sup>1</sup> Each is a trade term that consists of no more than a few words, often

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<sup>1</sup> EXW is an abbreviation for the trade term Ex Works; FOB is an abbreviation for Free on Board; CIF is an abbreviation for Cost, Insurance and Freight; and DDP is an abbreviation for Delivered Duty Paid. See INTERNATIONAL CHAMBER OF COMMERCE, INCOTERMS® 2010: ICC RULES FOR THE USE OF DOMESTIC AND INTERNATIONAL TRADE ITEMS (2010) [hereinafter INCOTERMS] (“The Incoterms® rules explain a set of three-letter trade terms reflecting business-to-business practice in contracts for the sale of goods.”).

accompanied only by a reference to some location. Yet in those few words there is contained a vast wealth of information regarding how the parties to the transaction intend to allocate significant risks and responsibilities between them in connection with shipment, transportation, and delivery of the goods. These transactions might include carriage of the goods through foreign countries, over the high seas, through the friendly – and sometimes not so friendly – skies, and across national borders. When the cargo, which might be worth millions of dollars, slips from the hoist into the depths of the cold harbor as it is unloaded following a long, hard voyage, which party has agreed to bear that loss?<sup>2</sup>

When the parties have the same subjective understanding of the delivery term, and that shared subjective understanding is consistent with an objective understanding of that term that can be ascertained by a third party, there is unlikely to be any cause for disagreement regarding how that delivery term allocates risk or responsibility. What if, on the other hand, the parties have different understandings of the meaning of the delivery term? What if that difference in understanding leads to a dispute regarding who has the responsibility to perform some task in connection with the transportation of the goods from point of manufacture to the ultimate destination, or how risk of loss has been allocated? In these cases, a court will be left to determine what set of default provisions the selected delivery term incorporates and how the default provisions apply to the facts of the case before the court. That can be “a costly and error-prone process.”<sup>3</sup>

This issue exists for any sale of goods transaction, including one that takes place entirely within a single country. But when the delivery term is used in a contract for the international sale of goods, when the buyer and seller have their places of business in different countries, the responsibilities allocated between the

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<sup>2</sup> Under the Incoterms definition of EXW and FOB, risk of loss would have passed from seller to buyer, and the buyer would therefore bear the risk of loss; under the Incoterms definition of the CIF term, the risk of loss would have similarly passed, but the seller would have the added obligation of purchasing marine insurance, and in this case that insurance would likely cover the loss; and under the Incoterms definition of DDP, the risk would still be with the seller, even though the incident might be thousands of miles from the seller’s place of business. *See id.*

<sup>3</sup> Clayton P. Gillette, *The Law Merchant in the Modern Age: Institutional Design and International Usages Under the CISG*, 5 CHI. J. INT’L L. 157, 158 (2004).

parties involve much more complex tasks. These tasks relate to exporting from the country of origin, importing into the country of destination, and navigating any space between the two. Perhaps even more important, the risk of loss attendant to the shipment, transportation, and delivery of the goods can be significantly more pronounced due to a longer journey. A longer journey likely involves more than one carrier and multiple modes of transport, added costs of pursuing remedies for breach when the target is located on the other side of the globe, and even the risk of piracy on the high seas. All of this makes use of delivery terms especially important in the international context.

The parties could simply write into their agreement how they came to agree to assign these tasks and to allocate these risks of loss between them. And sometimes parties do that. If the language is well-drafted and comprehensive, it will reduce the risk of misunderstanding between the parties regarding the terms of their bargain. In fact, however, businesspersons often do not include comprehensive, lengthy, written terms detailing how the parties have allocated risk and responsibility relating to delivery. Instead, they simply use delivery terms that provide default allocation of risk and responsibility.<sup>4</sup>

This practice is not a bad thing.<sup>5</sup> On the contrary, normatively, appropriate use of delivery terms is desirable because it is efficient and facilitates exchange, which is ultimately a fundamental purpose of contract. Using delivery terms is particularly valuable in the international context, where the parties will encounter additional barriers to trade due to language differences, logistical challenges, varying business practices, and different legal systems. The more comprehensive the default definition for the delivery term is, the more useful it is likely to be. As tasks need to be accomplished in order to move the goods from their point of origin to their point of destination, the buyer and seller know who – as

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<sup>4</sup> See INGBORG SCHWENZER, PASCAL HACHEM & CHRISTOPHER KEE, *GLOBAL SALES AND CONTRACT LAW* ¶ 29.27 (2012) [hereinafter SCHWENZER, HACHEM & KEE] (“Typically an agreement by the parties on the place of delivery occurs in conjunction with the agreement on other modalities of performance and is referred to in a shorthand manner by a trade term.”); see also JOSEPH LOOKOFSKY, *UNDERSTANDING THE CISG: A COMPACT GUIDE TO THE 1980 UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS* 101 (3d ed., 2008) [hereinafter LOOKOFSKY].

<sup>5</sup> Cf. Gillette, *supra* note 3, at 164-65 (describing administrative and error costs that can arise from use of incorporation strategy).

between the two of them – has the responsibility to see that each task is accomplished. And, as risks materialize during the loading or unloading of the cargo or during the voyage itself, the parties know who bears the risk of loss at each particular moment.

Despite the fact that delivery terms serve these important purposes, disagreements can and do occur regarding which party has assumed the risk of certain losses in connection with delivery of goods. These disputes arise even when the parties have included a delivery term in their written agreement.<sup>6</sup> Disagreement regarding who bears the risk of loss when an unanticipated calamity that leads to the total loss of an entire shipment of high-cost goods can result in a major dispute.

In fact, disputes happen. Sometimes businesspersons make decisions and enter into contracts under assumptions that prove to be false. Sometimes memories grow dim with the passage of time. Sometimes the individuals who negotiated the contract are replaced by new individuals who approach the relationship differently. In any of these circumstances, and a host of others, the corporate parties can reach a point where their human representatives do not see eye to eye on allocation of risk. Each might strongly believe the other to be responsible by contract for some loss. The loss has occurred; somebody will absorb that loss; what does the contract tell us about how the parties have agreed who that somebody is?

The simple inclusion of a delivery term in the parties' agreement should prove to be helpful when answering that question, at least when the source for defining the delivery term is clear. However, the source of the definition that the parties intended is not always evident. But when the applicable source of the definition is discernable, the delivery term is an objective means of determining and allocating risk and responsibility between the parties. Those delivery terms tell the parties, as well

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<sup>6</sup> See, e.g., *BP Oil Int'l, Ltd. v. Empresa Estatal Petroleos de Ecuador*, 332 F.3d 333, 335 (5th Cir. 2003), *as amended on denial of reh'g*; *Cedar Petrochems., Inc. v. Dongbu Hannong Chem. Co., Ltd.*, 769 F. Supp. 2d 269 (S.D.N.Y. 2011); *St. Paul Guardian Ins. Co. v. Neuromed Med. Sys. & Support, GmbH*, No. 00 CIV. 9344(SHS), 2002 WL 465312, at \*1 (S.D.N.Y. Mar. 26, 2002); *China N. Chem. Indus. Corp. v. Beston Chem. Corp.*, No. Civ.A. H-04-0912, 2006 WL 295395, at \*1, \*5 (S.D. Tex. Feb. 7, 2006); *Comptoir d'Achat et de Vente Du Boerenbond Belge S/A v. Luis de Ridder Limitada (The Julia)*, [1949] A.C. 293 (H.L.) [294] (appeal taken from Eng.) (U.K.); *Biddell Bros. v. E. Clemens Horst Co.*, [1911] 1 K.B. 934 [936] *rev'd* [1912] A.C. 18 (H.L.).

as third-party decision-makers, what the parties' respective rights and responsibilities are. This allocation of responsibility is true even though one of the parties might now regret the bargain that the parties have struck. The agreement is enforced nevertheless, because the parties *ex ante* want it to be enforced; it is the confidence of enforcement that facilitates entry into the contract in the first place and ultimately facilitates commercial exchange. As long as the delivery term is interpreted and applied correctly, which requires identifying the correct source of the definition of the delivery term, the expectations of the parties are protected and outcomes are predictable.

For many of these sales transactions, the applicable body of substantive law is the United Nations Convention on Contracts for the International Sale of Goods, or CISG.<sup>7</sup> The CISG facilitates commercial exchange in the international context in numerous ways, two of which are especially important for this analysis. First, the CISG invites the parties to define for themselves the terms of their agreement.<sup>8</sup> The CISG establishes a broad freedom of contract explicitly under Article 6, where the CISG provides that the parties to a CISG-governed contract may vary the effect of any of the CISG's provisions, subject only to limited exceptions not

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<sup>7</sup> United Nations Convention on Contracts for the International Sale of Goods, *opened for signature* Apr. 11, 1980, 1489 U.N.T.S. 3 (entered into force Jan. 1, 1988) [hereinafter CISG]. Subject to certain exclusions, the CISG governs contracts for the sale of goods between parties whose places of business are in different countries when the countries are "Contracting States" (or parties to the CISG). *Id.* at art. 1(1)(a). In the typical cross-border sale of goods transaction, when the parties know the goods are crossing a national border, the CISG will usually govern the transaction if the parties' places of business that are most directly involved with the transaction are in countries that have ratified the CISG. *See id.* at arts. 1(2) & 10(a). Because there are currently eighty parties to the CISG, including most of the major trading partners of the United States, the CISG is potentially relevant for a very large volume of international trade. *See* Dep't of State Pub. Notice 1004, 52 Fed. Reg. 6262 (Mar. 2, 1987) (noting those countries whose trade relations with the United States would be governed by the CISG as of its entry into force on January 1, 1988.); *see also* *Status of Chapter X(10): International Trade and Development, United Nations Convention on Contracts for the International Sale of Goods*, U.N. TREATY COLLECTION, [http://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsg\\_no=X-10&chapter=10&lang=en](http://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsg_no=X-10&chapter=10&lang=en) (last visited Nov. 11, 2013) [hereinafter CISG Status] (listing the current status of countries participating in the treaty).

<sup>8</sup> *See, e.g.,* CISG, *supra* note 7, at arts. 6, 11 & 29(1) (stating ways in which contracting parties may determine the extent to which the CISG applies to their contract, the way in which the existence of the contract is proven, and how the contract can be modified or terminated).

applicable here.<sup>9</sup> In fact, the CISG really allows for this variation throughout its text by deferring consistently to party agreement.<sup>10</sup>

The CISG allows for parties to shape their own agreements under Article 9 in a way that is specifically relevant for analysis of delivery terms. Under Article 9, the CISG provides for something called “usage” to become a binding term of the parties’ agreement, which can happen in either one of two different ways.<sup>11</sup> This mechanism for usage to become part of the parties’ agreement is important for the analysis of delivery terms because a certain prescribed allocation of risk and responsibility under a given delivery term can constitute usage, and courts can use Article 9 to determine whether a particular source of definition for the selected delivery term is part of the parties’ agreement. In international sales transactions, that source will often be Incoterms. Regardless, it is important for courts to understand how to use Article 9 to identify and apply the appropriate source of definition.

Unfortunately, however, U.S. courts have not analyzed or applied Article 9 correctly, and analysis by U.S. courts of delivery terms under Article 9 has been especially confused. This misinterpretation has led to poorly reasoned conclusions and gross misstatements of the application of Article 9, as courts have failed to see that Article 9(1) and Article 9(2), reflecting different policy considerations, establish completely different standards for usage to become a term of the parties’ agreement.

This improper analysis and misapplication of Article 9 of the CISG seriously undermines the CISG and its purposes. It undermines the CISG for the simple reason that the CISG, as a treaty made under the authority of the United States, is part of the

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<sup>9</sup> Article 6 provides: “The parties may exclude the application of this Convention or, subject to article 12, derogate from or vary the effect of any of its provisions.” *Id.* at art. 6.

<sup>10</sup> *See, e.g., id.* at art. 35(2) (listing conditions when the goods do not conform to the contract unless the parties agree otherwise).

<sup>11</sup> *See id.* at art. 9 (“(1) The parties are bound by any usage to which they have agreed and by any practices which they have established between themselves. (2) The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.”).



supreme law of the land under the Supremacy Clause.<sup>12</sup> As part of the supreme law of the land, the rule of law is best served by appropriate and uniform application of the CISG. More importantly for practical purposes, both within and outside the borders of the United States, when some courts interpret and apply the CISG properly and others do not, the stated purpose of the CISG to promote uniform rules for international sales transactions in order to “contribute to the removal of legal barriers in international trade and promote the development of international trade” is seriously undermined.<sup>13</sup> Similarly, when some courts interpret and apply the CISG properly and others do not, contracting parties are left guessing which approach they will face. This uncertainty can have the effect of upsetting the reasonable expectations of the parties that are otherwise derived from a good understanding of the proper application of the CISG.

We can do better.<sup>14</sup> While the mysteries shrouding the practices of foreign merchants – represented in arcane terms of art set forth in their contracts – might present an impenetrable fog for outsiders, a clear understanding of those practices and the corresponding delivery terms is nevertheless objectively attainable. Similarly, clear understanding of the relationship between Incoterms, as the dominant source of definitions for those delivery terms in international sales transactions, and the CISG, as the body of law that is likely to be applicable, is readily attainable. Ultimately, proper, uniform application of the CISG can provide a mooring for international trade and commerce, for the initiated and uninitiated alike.

This Article defines usage, as used in the CISG, in order to consider whether Incoterms should be characterized as usage for purposes of the CISG. This Article then describes the misguided approach that to date has been taken by U.S. courts when

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<sup>12</sup> U.S. CONST. art. VI. (providing in relevant part: “[A]ll Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land”).

<sup>13</sup> CISG, *supra* note 7, at pmbl.

<sup>14</sup> The U.S. Supreme Court has recognized the importance of faithful interpretation and enforcement of international commercial law to international trade. *See, e.g., Vimar Seguros y Reaseguros, S.A. v. M/V Sky Reefer*, 515 U.S. 528, 539 (1995) (“If the United States is to be able to gain the benefits of international accords and have a role as a trusted partner in multilateral endeavors, its courts should be most cautious before interpreting its domestic legislation in such manner as to violate international agreements.”).

analyzing the role of Incoterms as usage for contracts governed by the CISG. Finally, this Article proposes a method for proper analysis of Incoterms under the CISG, including the role that Article 9 should play in the analysis.

## 2. BACKGROUND ON DELIVERY TERMS

Delivery terms provide a shorthand method for assigning to each of the parties various responsibilities to complete specific tasks relating to shipment or transportation of the goods.<sup>15</sup> If export of the goods from the country of origin requires an export license, the delivery term might tell us who has the responsibility to obtain and pay for that license. If the contract does not include express terms dealing with packaging of the goods, the selected delivery term might address packaging requirements. The delivery term will be relevant for some of the logistics of actually getting the goods from the point of origin to the point of destination. For example, the term “Freight Prepaid & Add” generally means that the seller will pay the carrier for transportation of the goods and then will invoice the buyer for the cost of transportation.<sup>16</sup>

Similarly, the delivery term can indicate how payment is to be made. For example, in the absence of express agreement to the contrary, use of the CIF delivery term requires payment against presentation of documents, even before the goods have reached the buyer.<sup>17</sup> This payment obligation arises even though the contract says nothing about payment against presentation of documents.<sup>18</sup> This is also so even though the buyer would otherwise ordinarily have a right under applicable sales law to inspect the goods prior to tendering payment.<sup>19</sup>

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<sup>15</sup> These tasks might include proper storage of the goods until the carrier is ready to accept tender; satisfaction of customs formalities for export or import of the goods; obtaining marine insurance to cover 110% of the value of the goods; and so on. See INCOTERMS, *supra* note 1, at 108-17.

<sup>16</sup> MICHAEL HOLLOWAY & CHIKEZIE NWAHOA, *DICTIONARY OF INDUSTRIAL TERMS* 265 (2013).

<sup>17</sup> See, e.g., *E. Clemens Horst Co. v. Biddell Bros.*, [1912] A.C. 18, (H.L.) [22] (“[D]elivery of the bill of lading when the goods are at sea can be treated as delivery of the goods themselves . . .”).

<sup>18</sup> See *id.* at 23 (“[I]t is wrong to say that [the seller] must defer the tender of the bill of lading until the ship has arrived . . .”).

<sup>19</sup> See *id.* (“[I]t is still more wrong to say that [the seller] must defer the tender of the bill of lading until after the goods have been landed, inspected, and accepted.”). As a default matter, the UCC, for example, provides the buyer with a

Delivery terms also indicate where risk of loss passes from the seller to the buyer.<sup>20</sup> Risk of loss can pass from the seller to the buyer before the goods have even left the seller's loading dock under a properly worded Ex-Factory, Ex Works or similar term, for example,<sup>21</sup> or the risk of loss can remain with the seller until the goods have reached the buyer under a DDP term, for example.<sup>22</sup> And risk of loss can pass at numerous points along the way. The delivery term selected will automatically establish a default point for passage of the risk of loss.<sup>23</sup>

While delivery terms provide default allocation of risk and responsibility, the precise meanings of any of these delivery terms will ultimately depend on the applicable source of the definition for the delivery term.

### 2.1. Some Reasons Buyers and Sellers Use Delivery Terms

Use of delivery terms in sales contracts is customary and very common, and there are several reasons for that. For example, use of well-developed delivery terms contributes to certainty and predictability, at least to the extent the parties are or can become familiar with the objective understanding that a third party would give the delivery term. By selecting an appropriate delivery term, parties define each of their respective responsibilities relating to shipment of the goods and satisfaction of customs formalities for transportation of the goods. The parties also define the risk of loss while the goods are in transit. This process allows each party to

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right of inspection of the goods. See U.C.C. § 2-513(1) (2012) (stating the buyer's default right of inspection as recognized under the UCC). Inclusion of a CIF delivery term will not obviate the right of inspection, but it will require payment against documents in the ordinary case, even if inspection has not yet occurred.

<sup>20</sup> See JOHN W. HEAD, *GLOBAL BUSINESS LAW: PRINCIPLES AND PRACTICE OF INTERNATIONAL COMMERCE AND INVESTMENT* 151 (3d ed. 2012) [hereinafter HEAD] (noting that some trade terms delineate when a "transfer of risk" has occurred).

<sup>21</sup> See, e.g., INCOTERMS, *supra* note 1, at 15-21 (stating that where the term is EXW, delivery occurs when the seller places the goods "at the disposal of the buyer at the agreed . . . place of delivery, not loaded on any collecting vehicle" and that once delivery occurs, the risk of loss transfers to the buyer); *but see* U.C.C. § 2-319(1) (2012) (stating that where the term is F.O.B. the place of shipment, place of destination or vehicle, the seller bears the risk of placing goods in the possession of the carrier, transporting the goods for delivery, and loading the goods into the vehicle of delivery, respectively).

<sup>22</sup> See INCOTERMS, *supra* note 1, at 69-75.

<sup>23</sup> Note, however, that the delivery term does not establish at what point title passes.

properly allocate responsibility and risk in a way that is objectively determinable by each of them and, importantly, by third parties.

In the ordinary case, when the source of the definition for the selected delivery term is clear, there should be little or no doubt as to how the selected delivery term allocates risk or responsibility (even though there may be doubt as to its application to specific facts). Even if the parties are not actually aware of the allocation at the time they enter into the transaction, each of them can determine with specificity what it is, objectively, that they have agreed to. That makes the likely outcome of a misunderstanding or disagreement predictable. And predictability and certainty help to facilitate transactions and are especially important for international trade and commerce.<sup>24</sup>

Using delivery terms is also efficient.<sup>25</sup> In theory, the parties could attain predictability by taking the time to negotiate and write out detailed terms describing each step of the transportation of the goods and accounting for every conceivable contingency that could result in damage to or loss of the goods. In the fast-paced world of international trade and commerce, the parties often simply do not take the time to negotiate and finalize a comprehensive written agreement that sets out all of the terms of their bargain.<sup>26</sup> Having a set of tools will save time and cost. These tools are used by parties to dispense with the need to rehash and then memorialize their precise obligations relating to movement of the goods and

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<sup>24</sup> See, e.g., *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 629 (1985) (“[C]oncerns of international comity, respect for the capacities of foreign and transnational tribunals, and sensitivity to the need of the international commercial system for predictability in the resolution of disputes require that we enforce the parties’ agreement . . .”).

<sup>25</sup> See HEAD, *supra* note 20, at 151 (“The overall purpose of trade terms generally is to provide shorthand expressions for much more complicated and detailed arrangements between a buyer and a seller in an international transaction.”).

<sup>26</sup> See DANIEL C.K. CHOW & THOMAS J. SCHOENBAUM, *INTERNATIONAL BUSINESS TRANSACTIONS: PROBLEMS, CASES, AND MATERIALS* 213 (2d ed. 2010) [hereinafter CHOW & SCHOENBAUM] (“In contracts that are formed through casual contacts . . . it is not unusual for the parties to omit some or all of [the terms relating to place of delivery, insurance, and risk of loss].”); see also William P. Johnson, *The Hierarchy That Wasn’t There: Elevating “Usage” to its Rightful Position for Contracts Governed by the CISG*, 32 NW. J. INT’L L. & BUS. 263, 265 (2012) (“More often than one might imagine . . . commercial arrangements simply do not result in an executed written agreement that reflects the agreed-upon terms and allocation of risk and responsibility between the parties.”).

allocation of risk of loss of goods at various specific points in transit.

In some respects, these delivery terms also constitute jargon of international trade and commerce. Ordinary laypersons not involved in the international purchase, sale, or transportation of goods are unlikely to know what the term DDP means. And they certainly will not know how that term allocates risk or responsibility between the buyer and seller. Those who are facile at using delivery terms as shorthand for assignment of responsibility can be distinguished by that knowledge from those who are unfamiliar with the practice. Knowledge and use of commonly accepted delivery terms can contribute to a sense of being an insider in the world of international trade and commerce. This specialty knowledge can create a patina of credibility for those who can adroitly navigate and utilize the relevant jargon.

In fact, the attendant allocation of risk and responsibility under any given delivery term might be so regularly used and can become so well-known within certain international trade groups that it eventually rises to the level of trade custom. Once a trade custom, it will be understood and followed as a matter of course by insiders, even while mysterious and confounding to the uninitiated.

Despite the numerous good reasons for use of a delivery term, there are challenges as well. Part of the challenge has been that there are various iterations of delivery terms and their definitions that are used across jurisdictions and across industries. That's where Incoterms come into the picture.

## *2.2. Introducing Incoterms*

The term "Incoterms" refers to a set of rules, developed by the International Chamber of Commerce, that provide uniform definitions for delivery terms commonly used by buyers and sellers in their sales contracts.<sup>27</sup> Because delivery terms have long been used by merchants engaging in commercial transactions but delivery terms have been defined differently by various sources, the development of Incoterms was an attempt "to harmonize the countless variations among such [delivery] terms as they have

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<sup>27</sup> See INCOTERMS, *supra* note 1, at 5-11.

evolved differently in different countries and settings.”<sup>28</sup> In that regard, Incoterms have really been quite effective.

To be clear, Incoterms are not designed to replace the entire contract for sale; they merely supplement it.<sup>29</sup> Specifically, the applicable Incoterms definition establishes allocation of responsibility to complete certain tasks relating to delivery of the goods and allocation of certain costs incurred in connection with delivery of the goods.<sup>30</sup> Among other things, Incoterms address satisfaction of customs formalities, the obligation to obtain marine insurance, allocation of costs incurred in connection with delivery, and general obligations of the seller and the buyer, respectively.<sup>31</sup> Incoterms also govern allocation of risk of loss of and damage to goods during transportation of the goods from the point of origin to the point of destination.<sup>32</sup> With respect to those matters that are addressed by Incoterms, Incoterms offer a detailed, comprehensive set of determinable rules.

Incoterms have been around by now for more than seventy-five years.<sup>33</sup> The first set of Incoterms, Incoterms® 1936, was introduced in 1936.<sup>34</sup> Incoterms have been updated throughout the years to reflect evolving customary practices of merchants engaging in international trade, and the current version of Incoterms, Incoterms® 2010, entered into force in 2011.<sup>35</sup>

### 2.3. Other Common Sources of Definitions for Delivery Terms

Despite their growing relevance and importance, Incoterms are not the only source for definitions of delivery terms that are used in sales contracts today. For sales of goods governed by domestic U.S. law, Article 2 of the Uniform Commercial Code, or UCC,

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<sup>28</sup> HEAD, *supra* note 20, at 150.

<sup>29</sup> See INCOTERMS, *supra* note 1, at 6.

<sup>30</sup> See *id.* at 5-6.

<sup>31</sup> See *id.* at xx.

<sup>32</sup> See *id.*

<sup>33</sup> See HEAD, *supra* note 20, at 153 (explaining the change in Incoterms from its beginning in 1936 through subsequent revisions, in order to keep pace with commercial developments).

<sup>34</sup> INGEBOG SCHWENZER, CHRISTIANA FOUNTOLAKIS & MARIEL DIMSEY, INTERNATIONAL SALES LAW 81 n.41 (2d ed. 2012) [hereinafter SCHWENZER].

<sup>35</sup> See INCOTERMS, *supra* note 1, at 1.

provides default definitions for certain commonly-used delivery terms.<sup>36</sup>

There is some overlap between Incoterms and the UCC. For example, both Incoterms and the UCC define the commonly-used FOB, FAS, and CIF terms.<sup>37</sup> However, both the UCC and Incoterms define delivery terms that are not included in the other source.<sup>38</sup> The UCC defines C. & F., "Ex-Ship," and "No Arrival, No Sale," for example, none of which are specifically defined by Incoterms. On the other hand, the most recent iteration of Incoterms defines EXW, FCA, CPT, CIP, CFR, DAT, DAP, and DDP, and none of these delivery terms are specifically defined in the UCC.<sup>39</sup>

Of even greater importance, those terms that are common to the respective sources of definitions are sometimes defined in very different ways. For example, the FOB term is given different, and in some ways incompatible, meanings under the UCC and in Incoterms.<sup>40</sup> Under the UCC, the FOB term is a general delivery term that can be used with different modes of transport, whether transport occurs by air, road, rail, or water.<sup>41</sup> By contrast, FOB under Incoterms requires waterway transport.<sup>42</sup> While FOB under the UCC could allow risk of loss to pass to the buyer at virtually any named place, under Incoterms risk of loss passes to the buyer when the seller has delivered the goods at the port of shipment.<sup>43</sup>

And of course there are other sources of definitions for delivery terms. In the United States, for example, the American Foreign Trade Definitions held a place of importance for contracts for the

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<sup>36</sup> See U.C.C. §§ 2-319 – 2-324 (2012) (defining F.O.B., F.A.S, C.I.F., C&F, "net landed weight," "payment on arrival," "ex-ship," "overseas," and "no arrival, no sale").

<sup>37</sup> Cf. *id.* §§ 2-319 – 2-320, 2-323 (2012) and INCOTERMS, *supra* note 1, at 7.

<sup>38</sup> Cf. U.C.C. §§ 2-320 – 2-324 (2012) and INCOTERMS, *supra* note 1, at 7.

<sup>39</sup> Cf. U.C.C. §§ 2-319 – 2-322 (2012) and INCOTERMS, *supra* note 1, at 7.

<sup>40</sup> Cf. U.C.C. §§ 2-319, 2-323 (2012) and INCOTERMS, *supra* note 1, at 7 (explaining that there are two classes of Incoterms: the first class includes rules "that can be used irrespective of the mode of transport selected and irrespective of whether more than one mode of transport is employed. FOB belongs to the second class of terms, which is used only when the point of delivery and the place which the goods are carried to the buyer are both ports."). See also HEAD, *supra* note 20, 151–52 (explaining that FOB "is used differently in different countries and different settings"). See also SCHWENZER, HACHEM & KEE, *supra* note 4, ¶ 29.35.

<sup>41</sup> U.C.C. § 2-319 (2012).

<sup>42</sup> See INCOTERMS, *supra* note 1, at 87.

<sup>43</sup> Cf. U.C.C. § 2-319 (2012) and INCOTERMS, *supra* note 1, at 7.

international sale of goods prior to the 1980 revisions to Incoterms.<sup>44</sup> And delivery terms have long had meaning in the *lex mercatoria* and in the English common law tradition as well.<sup>45</sup>

This variety of definitions and sources makes clear identification of the selected delivery term and the applicable source of the definition for that delivery term critical. Otherwise the very purposes of predictability and certainty would be completely undermined.

### 3. DELIVERY TERM DEFINITIONS AS USAGE

Questions regarding party intent can arise even when parties use a delivery term. For example, if the parties' use of the delivery term is ambiguous in some way, then what have the parties, in fact, agreed to? Have the parties varied the default allocation of cost by agreement? Have the parties supplemented the default provisions by agreement? What is the applicable remedy if one of the parties breaches its obligations? When such questions arise, the court will turn to the applicable body of substantive law in order to interpret the parties' contract and to fill its gaps. For international sales of goods not involving consumer buyers, the applicable body of substantive law will often be the CISG.<sup>46</sup>

#### 3.1. Defining Usage for the CISG

The CISG provides two ways that usage can become part of the parties' agreement.<sup>47</sup> It is evident that Incoterms are important and that their use is widespread; does that mean that the Incoterms definitions of delivery terms constitute usage for purposes of the CISG? In order to determine whether Incoterms should be analyzed as possible usage for purposes of the CISG, it is

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<sup>44</sup> See generally, Peter Winship, *Introduction to Incoterms*, in 2 BASIC DOCUMENTS OF INTERNATIONAL ECONOMIC LAW 707, 707-10 (Stephen Zamora & Ronald A. Brand eds., 1990) (summarizing how Incoterms developed and attained widespread acceptance).

<sup>45</sup> See, e.g., *E. Clemens Horst Co. v. Biddell Bros.*, [1912] A.C. 18, 21 ("[D]elivery of the bill of lading when goods are at sea may be treated [under a c.i.f. term] as delivery of the goods themselves. That is so old and so well established that it is unnecessary to refer to authorities on the subject.").

<sup>46</sup> See CISG, *supra* note 7, at art. 1(1)(a) ("This Convention applies to contracts of sale of goods between parties whose places of business are in different States: (a) when the States are Contracting States.").

<sup>47</sup> See *id.* at art. 9 (establishing a means for usage to become part of the parties' agreement either by agreement of the parties or as an implied term).



important first to understand what is meant by the term “usage” as it is used in the CISG.

### 3.1.1. *The Text of the CISG*

The CISG is an international treaty. To determine the applicable definition of “usage” as it is used in the CISG, international law governing treaty interpretation prescribes that one should first look to the text of the treaty.<sup>48</sup> The CISG itself also calls for looking first to its text in order to determine its meaning.<sup>49</sup>

The term “usage” is not expressly defined in the CISG. The term is nevertheless used in five different sub-articles of the CISG.<sup>50</sup>

“Usage” appears in Article 8(3) of the CISG.<sup>51</sup> Under Article 8(3), courts are directed to give “due consideration” to usage (among other things).<sup>52</sup> They are to do this both under Article 8(1) when determining the actual intent of the parties and under Article 8(2) when determining a reasonable person’s understanding (*i.e.*,

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<sup>48</sup> See Vienna Convention on the Law of Treaties art. 31(1), May 23, 1969, 115 U.N.T.S. 331, 8 I.L.M. 679 [hereinafter Vienna Convention] (“A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.”). Though the United States is not a party to the Vienna Convention, the Vienna Convention is widely recognized as a codification of customary international law governing treaties. To the extent the Vienna Convention is a codification of customary international law, it is generally binding as a matter of international law even on those states that are not parties to the Vienna Convention. See, e.g., Statute of the International Court of Justice art. 38(1)(b), June 26, 1945, 59 Stat. 1055, 33 U.N.T.S. 993, 3 Bevens 1179 (“The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply . . . international custom, as evidence of a general practice accepted as law . . .”); *The Paquete Habana*, 175 U.S. 677, 686 (1900) (ruling on a maritime dispute based on an extensive discussion of applicable historical international norms in the absence of explicit statute or law governing both parties).

<sup>49</sup> See CISG, *supra* note 7, at art. 7(2) (stating that when issues are not expressly addressed in the CISG, they “are to be settled in conformity with the general principles” on which the CISG is based and when there are no such principles that are applicable, then in conformity with applicable law).

<sup>50</sup> See *id.* at arts. 4, 8(3), 9(1), 9(2), & 18(3) (citing to established usage between parties as an important factor in contract interpretation).

<sup>51</sup> See *id.* at art. 8(3) (“In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties.”).

<sup>52</sup> *Id.*

objective intent).<sup>53</sup> Notably, this requirement to consider usage in order to determine party intent is mandatory, not permissive.<sup>54</sup> That is, courts are not simply permitted to consider usage, they must do so when determining party intent – at least to the extent the usage constitutes a relevant circumstance of the case.<sup>55</sup>

Thus, usage is something that can impliedly demonstrate party intent. Moreover, there is no hierarchy established by Article 8(3) for usage relative to any other source a court is to consider when determining party intent, making usage of potentially significant importance for interpreting, and therefore establishing, the terms of the parties' agreement.<sup>56</sup>

Also significant for contract interpretation is Article 9(1), under which parties are bound by any usage to which they have agreed.<sup>57</sup> Any usage can qualify; as long as the parties have agreed to the usage, there are no additional requirements that must be satisfied. It is therefore clear that usage is an important means of establishing contract terms, both with respect to understanding the bargain that the parties intended to enter under Article 8(3), as well as with respect to supplementing under Article 9(1) any agreement that has been entered into by the parties.

Still, those provisions of the CISG are not particularly helpful with respect to defining clearly what is meant by the term usage. Article 9(1) suggests that usage is distinguished from, but nevertheless associated with, practices *established by the parties between themselves*. Although that does not define usage, it is a helpful means of understanding the scope of the meaning of usage. For example, under the maxim of *noscitur a sociis*, usage could refer to *practices established by third parties*, as a corollary to practices established by the contracting parties between themselves.

Next, Article 9(2) uses the term “usage” and sheds some light on the meaning of the term, as it is used in the CISG:

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<sup>53</sup> *Id.*

<sup>54</sup> *Id.*

<sup>55</sup> *Id.*

<sup>56</sup> See *id.*; see generally Johnson, *supra* note 26 (analyzing problems arising from U.S. courts misunderstanding the role usage plays in cases governed by the CISG).

<sup>57</sup> See CISG, *supra* note 7, at art. 9(1) (“The parties are bound by any usage to which they have agreed and by any practices they have established between themselves.”).

The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.<sup>58</sup>

Article 9(2) identifies the kind of usage courts are to determine binds the parties as an implied term.<sup>59</sup> It is clear from the plain language of Article 9(2) that usage is something that is capable of being “widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.”<sup>60</sup> At the same time, because that qualifying language does not appear in Article 9(1) (or Article 8(3)), usage, as used in Articles 9(1) and 8(3), need not actually be widely known to or regularly observed by parties to like contracts.<sup>61</sup>

The other two sub-articles of the CISG that use the term ‘usage,’ Articles 4 and 18(3), are not particularly helpful in defining usage.<sup>62</sup> Article 4 addresses principles of invalidity.<sup>63</sup> Article 4 provides that, except as otherwise expressly provided in the CISG, questions regarding the validity of any usage are outside the scope of the CISG.<sup>64</sup> Whether the issue of validity can even arise depends on whether the usage at issue is part of the parties’ agreement, because if it is not part of the parties’ agreement, then its validity or invalidity is not relevant for that contract. Whether the usage is part of the agreement, such that its validity could be at issue, depends on the application of the principles contained in Article 9.<sup>65</sup>

Article 18(3) describes what constitutes an acceptance in the formation of a contract under the CISG.<sup>66</sup> Specifically, mere

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<sup>58</sup> *Id.* at art. 9(2).

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

<sup>61</sup> *See id.* at arts. 9(1) & 8(3).

<sup>62</sup> *See id.* at arts. 4 & 18(3).

<sup>63</sup> *See id.* at art. 4 (“[E]xcept as otherwise expressly provided in this Convention, it is not concerned with . . . the validity of the contract or any of its provisions or of any usage.”).

<sup>64</sup> *Id.*

<sup>65</sup> *See id.* at art. 9.

<sup>66</sup> *See id.* at art. 18(3) (describing circumstances under which the offeree may indicate acceptance by performing an act that would constitute acceptance, without notice to the offeror).

performance of an act normally cannot constitute acceptance unless there is notice to the offeror.<sup>67</sup> But it is possible that applicable usage could allow acceptance to occur by performance of an act, even without notice.<sup>68</sup>

Knowing whether any such applicable usage is part of the contract between the parties, and therefore relevant for defining acceptable means of acceptance, also requires application of the principles contained in Article 9. Article 18(3) offers little independent insight regarding the meaning of the term usage.

Ultimately, the text of the CISG does not define the term usage, and it offers only limited insight regarding the definition of the term. We must therefore determine the definition of usage by some other means.

Article 7 of the CISG prescribes the method of analysis that is appropriate when the text of the CISG does not answer a question definitively.<sup>69</sup> Among other guidelines offered by Article 7, it requires considering first the general principles on which the CISG is based.<sup>70</sup>

### 3.1.2. General Principles

Whenever there is a question concerning a matter that is governed by the CISG, and the question is not expressly settled by the provisions of the CISG, the question is to be answered “in conformity with the general principles on which [the CISG] is based.”<sup>71</sup>

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<sup>67</sup> See *id.* at art. 18(2) (“An acceptance of an offer becomes effective at the moment the indication of assent reaches the offeror.”).

<sup>68</sup> See *id.* at art. 18(3) (“However, if, by virtue of the offer or as a result of practices which the parties have established between themselves or of usage, the offeree may indicate assent by performing an act, such as one relating to the dispatch of the goods or payment of the price, without notice to the offeror, the acceptance is effective at the moment the act is performed, provided that the act is performed within the period of time laid down in the preceding paragraph.”).

<sup>69</sup> See *id.* at art. 7(1) (stating that in interpreting the CISG, one must consider its “international character and to the need to promote uniformity in its application and the observance of good faith in international trade”).

<sup>70</sup> See *id.* at art. 7(2) (providing in relevant part that “[q]uestions concerning matters governed by [the CISG] which are not expressly settled in it are to be settled in conformity with the general principles on which it is based”).

<sup>71</sup> *Id.*

General principles on which the CISG is based can be derived from the text of the CISG itself.<sup>72</sup> One important principle that ripples throughout the text of the CISG is freedom of contract, or party autonomy.<sup>73</sup> The general principle of freedom of contract should inform and guide a court's approach to analyzing the CISG and applying its terms to a contract governed by the CISG, including when determining whether usage has become part of the parties' agreement. When the court can determine the parties' will, the parties' will should generally govern. That principle sheds no light on the precise meaning of usage, but it will be essential for the application of Article 9 when determining whether usage is part of the parties' agreement.

That leads to a second general principle on which the CISG is based - the principle of determining party intent, which should guide the court's analysis as to how best to determine the will of the parties under the CISG.<sup>74</sup> Under the CISG, actual intent of the parties, when it can be determined, prevails over any contrary objective intent.<sup>75</sup> And in order to determine party intent, courts are to consider all relevant circumstances.<sup>76</sup> This principle also sheds no particular light on the precise meaning of usage. Nevertheless, the principle should inform a court's analysis under Article 9, to the extent that determining party intent is relevant under Article 9 for the court's analysis.

A third general principle on which the CISG is based that is likely to be relevant for the court's analysis of Incoterms as usage is the principle of freedom from formalism.<sup>77</sup> That is, the CISG rejects

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<sup>72</sup> See SCHLECHTRIEM & SCHWENZER, COMMENTARY ON THE UN CONVENTION ON THE INTERNATIONAL SALE OF GOODS (CISG) 136-39 (Ingeborg Schwenzer ed., 3d ed. 2010) [hereinafter SCHLECHTRIEM] (discussing general principles that are derived from the CISG); see also SCHWENZER, *supra* note 34, at 52 (describing the primacy of general principles when filling gaps of the CISG).

<sup>73</sup> See CISG, *supra* note 7, at art. 6 ("The parties may exclude the application of this Convention or . . . derogate from or vary the effect of any of its provisions."); see also SCHLECHTRIEM, *supra* note 72, at 136 (describing the importance of party autonomy under the CISG's general principles).

<sup>74</sup> See CISG, *supra* note 7, at art. 8 (declaring that a party's conduct or statements "are to be interpreted according to his intent").

<sup>75</sup> *Id.*

<sup>76</sup> See *id.* at art. 8(3) ("In determining the intent of the party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case.").

<sup>77</sup> See *id.* at art. 11 ("A contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirement as to form. It may be

any formalistic requirements for demonstrating agreement, including modification of an agreement.<sup>78</sup> This principle will be relevant for analysis of whether and how the parties have manifested agreement to be bound, which is important for the application of Article 9.

General principles that can be derived from the text of the CISG will therefore be helpful for the court's analysis under Article 9. But those general principles do not define usage.

However, the CISG may also be based on general principles external to the CISG. Some commentators take the view that identifying general principles by reference to, for example, uniform laws external to the CISG is generally improper.<sup>79</sup> Other commentators take the view that various bodies of international commercial law essentially automatically provide ready sources for general principles that ought to be relevant for interpretation of the CISG.<sup>80</sup>

The key question is whether the identified principle, irrespective of its source, is a principle on which the CISG is actually based.<sup>81</sup> It is certainly plausible that the drafters had certain principles in mind when finalizing the CISG that can be found in other sources of international commercial law.

Additionally, given the CISG's missive to interpret the CISG with regard to its international character,<sup>82</sup> certain sources of international commercial law may be appropriate sources for shedding light on the meaning of CISG text. This is true especially

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proved by any means, including witnesses."); *see also* SCHLECHTRIEM, *supra* note 72, at 136 (advocating for the freedom of form).

<sup>78</sup> *See* CISG, *supra* note 7, at arts. 11 & 29(1) (rejecting requirements as to form).

<sup>79</sup> *See, e.g.,* SCHLECHTRIEM, *supra* note 72, at 139 (explaining that principles external to the CISG may not sufficiently reflect its international character, and thus may be unhelpful in interpreting ambiguity); *see also* SCHWENZER, HACHEM & KEE, *supra* note 4, ¶¶ 3.53-3.55 (explaining that the general principles of the CISG are certainly not based on the UNIDROIT Principles of International Commercial Contracts, which were adopted after the CISG was adopted).

<sup>80</sup> *See* SCHWENZER, HACHEM & KEE, *supra* note 4, ¶ 3.55 (explaining that UNIDROIT Principles of International Commercial Contracts have been used at times to discern general principles on which the CISG is based for purposes of Article 7(2)).

<sup>81</sup> *See* CISG, *supra* note 7, at art. 7(2) (prescribing that "questions concerning matters governed by this Convention . . . are to be settled in conformity with the general principles on which it is based").

<sup>82</sup> *See id.* at art. 7(1) ("In the interpretation of this Convention, regard is to be had to its international character.").

to the extent that the external source is a reflection of the *lex mercatoria* or otherwise sets forth general principles of international commercial law that would have been known to the drafters. However, the drafters' contemplation of these principles of international commercial law does not mean they are automatically relevant for the CISG. Reaching any conclusion that the principles are in fact principles on which the CISG is based requires careful analysis.

One potential source for determining general principles of international commercial law is the model law known as the UNIDROIT Principles of International Commercial Contracts.<sup>83</sup> It is true that the UNIDROIT Principles were adopted after the CISG came into effect. But, as a kind of restatement of principles of international commercial law, the UNIDROIT Principles nevertheless offer evidence of general principles applicable to international commercial contracts that the drafters of both the CISG and the UNIDROIT Principles might have had in mind.<sup>84</sup> In that regard, the UNIDROIT Principles can conceivably offer additional details concerning principles on which both the CISG and the UNIDROIT Principles are based.<sup>85</sup> And although hardly dispositive, some commentators believe that the UNIDROIT Principles are intended to be used "to interpret or supplement international uniform law instruments."<sup>86</sup>

The relevant text of the UNIDROIT Principles tracks the corresponding text of the CISG.<sup>87</sup> Article 1.9 of the UNIDROIT Principles provides that the "parties are bound by any usage to

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<sup>83</sup> UNIDROIT INT'L INST. FOR THE UNIFICATION OF PRIVATE L., UNIDROIT PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS (2010) [hereinafter UNIDROIT PRINCIPLES], available at <http://www.unidroit.org/english/principles/contracts/principles2010/integralversionprinciples2010-e.pdf>.

<sup>84</sup> See CHOW & SCHOENBAUM, *supra* note 26, at 181 (agreeing that the UNIDROIT Principles are a type of international restatement of contracts and, as such, are generally complementary to the CISG).

<sup>85</sup> See UNIDROIT PRINCIPLES, *supra* note 83, at pmbl. (asserting that one of the stated purposes of the UNIDROIT Principles is to "set forth general rules for international commercial contracts"). See also SCHWENZER, HACHEM & KEE, *supra* note 4, ¶ 3.55.

<sup>86</sup> *Id.* See also CHOW & SCHOENBAUM, *supra* note 26, at 181 (noting that the UNIDROIT Principles may have legal effect when international instruments need supplementation or interpretation).

<sup>87</sup> Cf. UNIDROIT PRINCIPLES, *supra* note 83, at art. 1.9 and CISG, *supra* note 7, at art. 9 (using the identical language: "the parties are bound by any usage to which they have agreed and by any practices which they have established between themselves").

which they have agreed and by any practices which they have established between themselves.”<sup>88</sup> Article 1.9 further provides that the parties are bound by any usage “that is widely known to and regularly observed in international trade by parties in the particular trade concerned except where the application of such a usage would be unreasonable.”<sup>89</sup> Thus, Article 1.9(1) of the UNIDROIT Principles is identical to Article 9(1) of the CISG, and Article 1.9(2) of the UNIDROIT Principles is very similar to Article 9(2) of the CISG.

The UNIDROIT Principles also do not define the term usage. However, the comments to Article 1.9 do show that usage reflects “established general lines of conduct.”<sup>90</sup>

When the UNIDROIT Principles are considered in light of Article 9(2) of the CISG, usage under the CISG appears to contemplate generally established conduct or practices of third parties.

### 3.1.3. *Law Applicable Under Principles of Private International Law*

Whenever there is a question concerning a matter that is governed by the CISG, the question is not expressly settled by the provisions of the CISG, and the question cannot be answered “in conformity with the general principles on which [the CISG] is based,”<sup>91</sup> the question is to be answered “in conformity with the law applicable by virtue of the rules of private international law.”<sup>92</sup> Any court adjudicating a conflict before it that is governed by the CISG will have its own rules of private international law, or conflicts of laws, and should apply those rules to determine the substantive body of law that would govern the dispute pursuant to those rules.<sup>93</sup> All the while, interpretation of the CISG is to be conducted with regard to its international character and with an eye toward uniform application across jurisdictions.<sup>94</sup>

When the transaction bears an appropriate relation to the state where the court is located, a court in the United States is likely to apply Article 2 of the UCC, as codified in the applicable state and

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<sup>88</sup> UNIDROIT PRINCIPLES, *supra* note 83, at art. 1.9(1).

<sup>89</sup> *Id.* at art. 1.9(2).

<sup>90</sup> *Id.* at art. 1.9 cmt. 3.

<sup>91</sup> CISG, *supra* note 7, at art. 7(2).

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> *Id.* at art. 7(1).



as supplemented by the common law of that state, unless the parties have effectively chosen some other body of law.<sup>95</sup> Usage is generally understood under the common law to refer to any practice that is habitual or customary.<sup>96</sup> Under the UCC, usage of trade is more narrowly defined as “any practice or method of dealing having such regularity of observance in a place, vocation, or trade as to justify an expectation that it will be observed with respect to the transaction in question.”<sup>97</sup> In both the common law and UCC definitions, usage constitutes practices of third parties that reach a sufficient point of regularity as to be appropriately characterized as habitual or customary. Under the UCC, if there is enough regularity of the practice to expect third parties to abide by the practice as a default matter, then it is usage of trade. The UCC is specific to the United States, of course, but according to one leading European commentary, various legal systems generally agree on the definition of trade usage, and the UCC definition is “[i]ndicative of this common ground.”<sup>98</sup>

Still, the CISG reflects more than the common law tradition, and it is important when applying the CISG not to assume that some domestic definition of a term used in the CISG controls. While considering various domestic understandings of the concept of usage may be helpful to glean a common definition, it is more important to consider the international character of the CISG.<sup>99</sup> As articulated in one of the leading European commentaries on the CISG, the concept of trade usage should “be interpreted without recourse to preconceived domestic notions.”<sup>100</sup> Instead, the focus should be on uniform application of the CISG in light of its

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<sup>95</sup> U.C.C. § 1-301(b) (2012). The exception is the State of Louisiana, which has not adopted Article 2 of the UCC.

<sup>96</sup> See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 219 (1981) (“Usage is habitual or customary practice.”).

<sup>97</sup> U.C.C. § 1-303(c) (2012).

<sup>98</sup> SCHWENZER, HACHEM & KEE, *supra* note 4, ¶ 27.31.

<sup>99</sup> See CISG, *supra* note 7, at art. 7(1) (“In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.”); see also *id.* at pmb1. (“Being of the opinion that the adoption of uniform rules which govern contracts for the international sale of goods and take into account the different social, economic and legal systems would contribute to the removal of legal barriers in international trade and promote the development of international trade.”).

<sup>100</sup> SCHLECHTRIEM, *supra* note 72, at 187.

international character.<sup>101</sup> And, according to that commentary, a usage is simply any rule of commerce that is “regularly observed by those involved in a particular industry or marketplace.”<sup>102</sup>

The term ‘usage’ is not specifically defined in the CISG. But it is a term that is well understood as a common term of various bodies of domestic sales law and as a concept that ripples throughout international commercial law. Based on its association with practices established between the parties under the CISG; its understanding under the common law as habitual or customary practices; and its understanding under international commercial law as generally established conduct, it is fair to say that usage refers to established conduct or established practices of third parties, including, for example, practices that are established enough to be characterized as habitual or customary. When that happens for a particular group—an industry group, a trade group, and the like—the practice constitutes usage of that group, and it can even become binding as an implied contract term under many legal traditions, including the CISG.

### 3.2. *Incoterms as Established Practice*

The key question, then, is whether the Incoterms definitions of delivery terms reflect practices that are so established that they can be said to have reached the point at which participants in the relevant industry simply expect to abide by them. Ultimately, this is a factual inquiry to be undertaken by the relevant finder of fact. But commentary suggests that Incoterms have reached that point.<sup>103</sup>

## 4. APPLICATION OF ARTICLE 9

Proceeding with the analysis under the assumption that Incoterms can constitute usage, it is important to consider what relevance that has for analysis and interpretation of a contract and its terms under the CISG.

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<sup>101</sup> CISG, *supra* note 7, at art. 7(1). *See also id.* at pmb1.

<sup>102</sup> SCHLECHTRIEM, *supra* note 72, at 187.

<sup>103</sup> *See, e.g.,* LOOKOFSKY, *supra* note 4, at 70 (describing Incoterms as “well-known and widely used”); INTERNATIONAL LAWYER’S DESKBOOK 30 (Lucinda A. Low, Patrick M. Norton & Daniel M. Drory eds., 2d ed. 2002) (describing Incoterms as “an internationally recognized set of trade terms”); SCHWENZER, *supra* note 34, at 81 n.41 (“The INCOTERMS® . . . are a universally recognised set of definitions of international trade terms.”).

#### 4.1. *The Text of Article 9*

Article 9 of the CISG distinguishes between usage that becomes part of the parties' agreement because the parties have agreed to the usage<sup>104</sup> and usage that becomes part of the parties' agreement as an implied term of the agreement without any express agreement by the parties regarding the usage in question.<sup>105</sup> Thus, two different standards exist under Article 9 for usage to become part of the parties' agreement. Under Article 9(1), any usage can become part of the parties' agreement simply because the parties have agreed that it should.<sup>106</sup> Stated differently, if the parties have agreed that some usage is part of their agreement, then it is, and no additional requirements or formalities must be satisfied.<sup>107</sup> That party agreement could be demonstrated in different ways;<sup>108</sup> it simply must be established that the parties have so agreed.

When the parties have not so agreed, usage might nevertheless become part of their agreement as an implied term.<sup>109</sup> By way of sharp contrast, however, usage may only become part of the parties' agreement as an implied term when certain specific conditions identified in Article 9(2) are satisfied.<sup>110</sup>

Article 9(2) provides as follows:

The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely

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<sup>104</sup> CISG, *supra* note 7, at art. 9(1) ("The parties are bound by any usage to which they have agreed . . .").

<sup>105</sup> *See id.* at art. 9(2) ("The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.").

<sup>106</sup> *Id.* at art. 9(1).

<sup>107</sup> *Id.*

<sup>108</sup> *See id.* at art. 6 ("The parties may exclude the application of this Convention or . . . derogate from or vary the effect of any of its provision."); *see also id.* at art. 11 ("A contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirement as to form. It may be proved by any means, including witnesses.").

<sup>109</sup> *Id.* at art. 9(2).

<sup>110</sup> *Id.*

known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.<sup>111</sup>

Thus, before concluding that a usage is an implied term of the parties' agreement under Article 9(2), the court must consider whether three distinct requirements are satisfied with respect to the usage in question: (i) whether the usage in question is a usage of which each party either actually knew or ought to have known, (ii) whether in international trade the usage is widely known to parties to like contracts, and (iii) whether in international trade the usage is regularly observed by such parties to like contracts.<sup>112</sup> Notably, these are questions that must be answered in the context of, and by reference to, the facts of the individual case before the court. Article 9(2)'s reference to "contracts of the type involved" shows that certain usages could satisfy the requirements of being widely known and regularly observed in some trades but not others. It is only usage that is widely known and regularly observed by parties to like contracts that can become part of the parties' agreement as an implied term under Article 9(2).

The party who argues for inclusion in the contract of some usage as a binding implied term under Article 9(2) bears the burden of showing that the usage in question satisfies each of these three requirements. If any of these three requirements cannot be established, then the usage is not made part of the agreement under Article 9(2).<sup>113</sup>

Even when the three requirements can be shown to have been satisfied, the analysis is not yet complete. The other party must have the opportunity to attempt to show that the usage is nevertheless not a part of the parties' agreement, because the parties have agreed that it isn't—that is, Article 9(2) would have made the usage an implied term, but the other party has successfully demonstrated that the parties have "otherwise agreed."<sup>114</sup>

When the requirements of Article 9(2) are satisfied, it is reasonable to conclude that the parties should be bound by the

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<sup>111</sup> *Id.*

<sup>112</sup> *Id.* See also Johnson, *supra* note 26, at 277-78 (describing the standards for establishing whether a usage is an implied term).

<sup>113</sup> CISG, *supra* note 7, at art. 9(2).

<sup>114</sup> *Id.*

usage as an implied term.<sup>115</sup> The reasoning that supports this conclusion is as follows:

Similarly situated third parties in international trade know about this usage, and those third parties abide by the usage.

The parties to this contract also either knew or ought to have known about this usage, and they did not manifest agreement not to be bound by it.

*Therefore, it is [fair and reasonable] to conclude that these parties intended to abide by the usage.*<sup>116</sup>

Because Article 9(2) provides a mechanism for usage to become a binding term of the parties' agreement without the parties' express consent, and potentially even without their actual knowledge of the existence of the usage, it is only a narrow category of usages that are reasonable to foist upon the parties. Courts should therefore analyze carefully whether each of the requirements has actually been shown to have been satisfied before concluding that the definition for some delivery term—or any other practice—constitutes a binding implied term under Article 9(2).

Unfortunately, however, U.S. courts have not carefully distinguished between usage that is actually agreed upon by the parties and usage that is implied because it satisfies the three requirements of Article 9(2) and has not otherwise been excluded by the parties' agreement.<sup>117</sup> Some U.S. courts have simply failed to recognize that Article 9 of the CISG treats these two categories of usage differently and uses different standards to determine

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<sup>115</sup> Johnson, *supra* note 26, at 278.

<sup>116</sup> *Id.* (emphasis in original).

<sup>117</sup> See, e.g., *BP Oil Int'l, Ltd. v. Empresa Estatal Petroleos de Ecuador*, 332 F.3d 333, 337-38 (5th Cir. 2003), *as amended on denial of reh'g* (holding without extensive elaboration that BP had satisfied its implied contractual obligations if the goods had met the qualitative specifications upon delivery); *Cedar Petrochems., Inc. v. Dongbu Hannong Chem. Co., Ltd.*, No. 06 Civ. 3972(LTS)(JCF), 2011 WL 4494602, at \*4 (S.D.N.Y. Sept. 28, 2011) (finding the incoterm "free on board" had been implicitly incorporated); *China N. Chem. Indus. Corp. v. Beston Chem. Corp.*, No. Civ. A. H-04-0912, 2006 WL 295395, at \*6 (S.D. Tex. Feb. 7, 2006) (applying Article 9(2) to shipping dispute); *St. Paul Guardian Ins. Co. v. Neuromed Med. Sys. & Support, GmbH*, No. 00 CIV. 9344 (SHS), 2002 WL 465312, at \*3-4 (S.D.N.Y. Mar. 26, 2002) (incorporating incoterms: "cost, insurance, and freight").

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whether the usage in question is part of the parties' agreement, if at all, as an agreed-upon term or an implied term.

#### 4.2. *Scant Attention Paid to the Text of Article 9*

While there are relatively few decisions of U.S. courts analyzing or applying Article 9 of the CISG, those U.S. courts that have applied Article 9 have engaged at times in only the barest of analysis, failing to consider carefully the text of Article 9 in light of the object and purpose of the CISG.<sup>118</sup>

The deep misunderstanding of U.S. courts regarding how commonly used delivery terms should be interpreted under the CISG and the proper role of Article 9 in that analysis is one specific example of this.

##### 4.2.1. *St. Paul Guardian Insurance Co. v. Neuromed Medical Systems & Support, GmbH*

In one case that arose out of the sale of a mobile magnetic resonance imaging system, or MRI, two insurance companies, St. Paul Guardian Insurance Company and Travelers Property Casualty Insurance Company, who issued policies to the buyer of the MRI, brought an action against the seller, Neuromed Medical Systems & Support GmbH ("Neuromed").<sup>119</sup> The insurance companies brought their action against Neuromed as subrogees of the buyer.<sup>120</sup>

Neuromed moved to dismiss on two grounds: first, on the basis of a forum selection clause in the parties' written agreement—which Neuromed argued required the action to proceed in Germany; and second, on the basis that the complaint failed to state a claim for relief.<sup>121</sup> The court had previously concluded that the forum selection clause did not require the action to proceed in Germany, and was considering Neuromed's

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<sup>118</sup> See, e.g., *Treibacher Industrie, A.G. v. Allegheny Techs., Inc.*, 464 F.3d 1235, 1238–39 (11th Cir. 2006) (discussing briefly the effect of "customary usage" on contract interpretation under the CISG); *Hanwha Corp. v. Cedar Petrochemicals, Inc.*, 760 F. Supp. 2d 426, 433 (S.D.N.Y. 2011) (stating, without discussing, that certain facts constituted a rejection and subsequent counter-offer within the meaning of Article 19(1)).

<sup>119</sup> *St. Paul Guardian Ins. Co. v. Neuromed Med. Sys. & Support, GmbH*, No. 00 CIV. 9344(SHS), 2002 WL 465312, at \*1 (S.D.N.Y. Mar. 26, 2002).

<sup>120</sup> *Id.*

<sup>121</sup> *Id.* at \*2.

second ground for dismissal.<sup>122</sup> The court granted Neuromed's motion on the second ground, and the complaint was dismissed.<sup>123</sup>

It was undisputed that the MRI was loaded "undamaged and in good working order" aboard the carrier and was therefore apparently damaged in transit.<sup>124</sup> Building on that undisputed fact, Neuromed's argument fundamentally was that "it had no further obligations regarding the risk of loss once it delivered the MRI to the vessel at the port of shipment due to a 'CIF' clause included in the underlying contract."<sup>125</sup>

The written agreement between the parties specifically included the following express clause: "CIF New York Seaport."<sup>126</sup> No reference was made to any source for the meaning of the CIF delivery term.<sup>127</sup> Neuromed argued that the applicable source for the definition of the CIF delivery term was the ICC's Incoterms 1990.<sup>128</sup> The insurance companies argued that Incoterms were inapplicable because the written contract failed specifically to incorporate them.<sup>129</sup>

The court applied German law and, accordingly, applied the CISG.<sup>130</sup> The court rejected the insurance companies' argument that Incoterms were inapplicable, conclusorily stating that Incoterms "are incorporated into the CISG through Article 9(2)" of the CISG.<sup>131</sup> That statement by the court reflects multiple layers of misunderstanding of the relationship between the CISG and Incoterms, as well as of the role of Article 9 in the analysis.

To be clear, the conclusion that Incoterms should provide the relevant definition of the delivery term used in the written agreement may very well be correct. It seems entirely possible that the parties intended to incorporate into their agreement the

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<sup>122</sup> *Id.* at \*1.

<sup>123</sup> *Id.* at \*2.

<sup>124</sup> *Id.* at \*1.

<sup>125</sup> *Id.*

<sup>126</sup> *Id.*

<sup>127</sup> *Id.*

<sup>128</sup> *See id.* at \*2 (arguing that "since the delivery terms were 'CIF New York Seaport,' [Neuromed's] contractual obligation, with regard to risk of loss or damage, ended when it delivered the MRI to the vessel at the port of shipment").

<sup>129</sup> *Id.* at \*4.

<sup>130</sup> *See id.* at \*3 (noting that Germany is a party to the CISG); *see also* CISG Status, *supra* note 7 (explaining that once Germany became a party to the CISG, the CISG became part of the law of Germany).

<sup>131</sup> *St. Paul Guardian Ins. Co.*, 2002 WL 465312 at \*3-4.

Incoterms 1990 definition of the CIF delivery term used in their agreement. Given that it is reasonable to assume that these sophisticated merchants were familiar with Incoterms, expressly including the CIF term in their written contract under the circumstances provides evidence that the parties intended to incorporate and be bound by the Incoterms definition. This is so, even though they included the delivery term without reference to any source for defining that delivery term.

The court's conclusion is nevertheless problematic for at least three reasons. First, at a fundamental level, the court sloppily concluded that Incoterms are part of *the CISG*, and not simply part of the parties' agreement as contemplated by Article 9.<sup>132</sup> In fact, Incoterms are not part of the CISG, nor is it necessary or appropriate to analyze whether they are. On the contrary, the CISG contains default delivery provisions in Articles 30 through 34, Article 60, and Articles 66 through 69.<sup>133</sup> These provisions provide default rules for the obligations of the seller in connection with delivery of the goods;<sup>134</sup> the buyer's obligation to take delivery;<sup>135</sup> and passing of the risk of loss.<sup>136</sup> The parties are free to agree on some other allocation of risk or responsibility that differs from the default provisions.<sup>137</sup> Adoption of an Incoterms definition as part of the parties' agreement is one way the parties could derogate from or add to the CISG's default provisions. But the conclusion that Incoterms are part of the CISG itself is simply not accurate and is not supported by the text of the CISG.

The court's conclusion that Incoterms have somehow become part of the CISG itself reflects a troubling disregard for the text of the CISG, which provides for usage to bind the parties pursuant to Article 9(1) or to be made impliedly applicable to the parties' contract or its formation under Article 9(2), but certainly not to

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<sup>132</sup> See *id.* ("INCOTERMS are incorporated into the CISG through Article 9(2) . . .").

<sup>133</sup> See CISG, *supra* note 7, at arts. 30-34, 60, & 66-69.

<sup>134</sup> See *id.* at arts. 30-34.

<sup>135</sup> See *id.* at art. 60 ("The buyer's obligation to take delivery consists: (a) in doing all the acts which could reasonably be expected of him in order to enable the seller to make delivery; and (b) in taking over the goods.").

<sup>136</sup> See *id.* at arts. 66-69 (detailing who assumes the risk depending on the context).

<sup>137</sup> See *id.* at art. 6 ("The parties may exclude the application of this Convention or, subject to article 12, derogate from or vary the effect of any of its provisions.").



become part of the CISG.<sup>138</sup> If we were to read and apply the court's statement literally, that is, if Incoterms had somehow become part of the CISG, then for future cases the other threshold requirements of Article 9—party agreement under Article 9(1) and the three requirements for usage as an implied term under Article 9(2)—would be rendered meaningless.

Of course, that must not be what the court meant. Still, the court should not have carelessly asserted that Incoterms are part of the CISG. They are not. Instead, the focus should be on whether the Incoterms definition of a delivery term has become part of the parties' agreement.

Second, the court referred to Article 9(2) as the operative section without considering Article 9(1).<sup>139</sup> If Incoterms did constitute usage that became a term of the parties' agreement under the CISG, this is likely to have been the result of party agreement and, therefore, by operation of Article 9(1). After all, the CIF term was an express term of the parties' written agreement.<sup>140</sup> Article 9(1) provides that the "parties are bound by any usage to which they have agreed."<sup>141</sup> Thus, the definition of the CIF term arguably became part of the parties' agreement under Article 9(1)—rather than Article 9(2) as asserted by the court—because the CIF term was expressly included in the written agreement and was therefore arguably a "usage to which [the parties] have agreed."<sup>142</sup> Ultimately, this is a factual question. Whether such agreement occurred here as a matter of fact does not seem to have been considered by the court.

Third, and most troubling, even if Article 9(2) were the appropriate section of the CISG to apply in order to determine whether the Incoterms definition of the CIF term was part of the

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<sup>138</sup> See *id.* at art. 9 ("(1) The parties are bound by any usage to which they have agreed and by any practices which they have established between themselves. (2) The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.").

<sup>139</sup> See *St. Paul Guardian Ins. Co. v. Neuromed Med. Sys. & Support*, No. 00 CIV. 9344 (SHS), 2002 WL 465312, at \*3 (S.D.N.Y. Mar. 26, 2002) ("Incoterms are incorporated into the CISG through Article 9(2) . . .").

<sup>140</sup> See *id.* at \*1 (discussing the existence of a CIF clause in the parties' underlying contract).

<sup>141</sup> CISG, *supra* note 7, at art. 9(1).

<sup>142</sup> *Id.* (emphasis added).

parties' agreement, the court failed to conduct any analysis of the requirements of Article 9(2) and its application to the facts of this case. Specifically, in no way did the court analyze whether the parties knew or ought to have known of Incoterms 1990; the court did not analyze whether Incoterms are, in international trade, widely known to parties to like contracts; and the court did not analyze whether Incoterms are, in international trade, regularly observed by parties to like contracts. That analysis is essential for any conclusion that usage became part of the parties' agreement pursuant to Article 9(2).<sup>143</sup> It is only usage that can satisfy the requirements of Article 9(2) that is impliedly made part of a contract under Article 9(2) of the CISG.

Were these three requirements satisfied here? We have no way to know because this analysis is entirely absent. It seems safe to assume that the court did not fail to engage in the requisite analysis due to any sort of willful impropriety. On the contrary, the court's other analysis of the CISG is generally sound, and its careful consideration of German law and German decisions is laudable. But by not engaging in the analysis specifically required by Article 9(2) in the context of the individual case before it, a court risks concluding that some obscure usage—actually unknown to the parties at the time of contract formation—nevertheless is part of the parties' bargain and is binding on a party who in no way agreed to be bound by it, and should not be deemed to have agreed to be bound by it, but will be nevertheless. That undermines the parties' expectations at the time of entry into the contract, and it undermines the CISG's principle of deferring to party intent. Because it will be difficult to know what usages the court might simply unilaterally incorporate into the parties' agreement, predictability will be undermined as well. This risk seems especially acute for parties in developing nations or otherwise in markets where prevailing trade usages may still be in nascent stages. And none of that is helpful to the removal of barriers to international trade, a core objective of the CISG.

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<sup>143</sup> See *id.* at art. 9(2).

4.2.2. *BP Oil International, Ltd. v. Empresa Estatal Petroleos de Ecuador*

In a subsequent decision by the Fifth Circuit, Incoterms were once again at issue.<sup>144</sup> In *BP Oil*, the dispute arose out of an agreement by which BP Oil International, Ltd. ("BP Oil") agreed to supply Empresa Estatal Petroleos de Ecuador ("PetroEcuador") 140,000 barrels of unleaded gasoline, to be delivered "CFR La Libertad – Ecuador."<sup>145</sup> The agreement stated that the gasoline was required to have a gum content of less than three milligrams per one hundred milliliters, which was to be established at the port of departure.<sup>146</sup> After a third party tested the gasoline, BP Oil shipped the gasoline, but, on arrival at the port of destination, the gum content exceeded the permitted limit.<sup>147</sup> PetroEcuador refused to accept delivery of the gasoline, and BP Oil sold it at a loss to a third party.<sup>148</sup> BP Oil then filed a claim in Texas against PetroEcuador.<sup>149</sup>

Applying Texas choice-of-law rules, the district court concluded that domestic Ecuadorian law was the appropriate substantive law to apply to the transaction, based on an apparent choice-of-law clause in the parties' contract, which provided as follows: "Jurisdiction: Laws of the Republic of Ecuador."<sup>150</sup> The district court held that under domestic Ecuadorian law, BP Oil was obligated to deliver conforming goods to Ecuador, the agreed-upon destination.<sup>151</sup> The district court granted summary judgment for PetroEcuador.<sup>152</sup>

BP Oil appealed, and the Fifth Circuit reversed the district court's judgment dismissing PetroEcuador.<sup>153</sup> Because the CISG is part of the law of Ecuador, the Fifth Circuit held the choice of law clause had the effect of choosing the CISG, and that the CISG

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<sup>144</sup> See generally *BP Oil Int'l, Ltd. v. Empresa Estatal Petroleos de Ecuador*, 332 F.3d 333 (5th Cir. 2003), as amended on denial of reh'g.

<sup>145</sup> *Id.* at 335.

<sup>146</sup> *Id.*

<sup>147</sup> *Id.*

<sup>148</sup> *Id.*

<sup>149</sup> *Id.*

<sup>150</sup> *Id.*

<sup>151</sup> *Id.*

<sup>152</sup> *Id.*

<sup>153</sup> *Id.* at 334–35, 339.

therefore governed the dispute.<sup>154</sup> In so holding, the court reasoned that an “affirmative opt-out requirement promotes uniformity and the observance of good faith in international trade, two principles that guide interpretation of the CISG.”<sup>155</sup> In that regard, the Fifth Circuit’s clear attempt to apply the CISG carefully and faithfully is commendable, and its focus on uniformity is refreshing and helpful. In addition, the court also engaged in careful and sound analysis of provisions of the CISG concerning latent defects.<sup>156</sup>

However, like the court in *St. Paul Guardian Insurance Co.*, the Fifth Circuit incorrectly asserted that “Incoterms are recognized through their incorporation into the [CISG].”<sup>157</sup> It further stated that the CISG “incorporates Incoterms through Article 9(2).”<sup>158</sup> The court in *BP Oil* engaged in at least some minimal analysis of Incoterms as possible usage for purposes of Article 9(2) by, for example, reproducing the text of Article 9(2) and reasoning that Incoterms are well known in international trade.<sup>159</sup> But when the court concluded that the fact that Incoterms “are well known in international trade means that they are incorporated through article 9(2)”<sup>160</sup> without actually analyzing the three discrete requirements under Article 9(2) in the specific context of the individual case before it, the court missed the subtlety of the provision and the actual standard set forth in Article 9(2) for making any given usage contractually binding on the contracting parties as an implied term of their agreement.

Moreover, because there was an express reference in the parties’ written agreement to the CFR delivery term,<sup>161</sup> Incoterms as usage arguably should have been analyzed under Article 9(1). The Fifth Circuit therefore ultimately committed the same three errors as the court in *St. Paul Guardian Insurance Co.*

The analysis of the Fifth Circuit is especially disappointing because the Fifth Circuit was not bound in any way by the *St. Paul Guardian Insurance Co.* decision, an unpublished opinion of a lower

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<sup>154</sup> *Id.* at 337.

<sup>155</sup> *Id.*

<sup>156</sup> *Id.* at 338.

<sup>157</sup> *Id.* at 335.

<sup>158</sup> *Id.* at 337.

<sup>159</sup> *See id.* at 337–38.

<sup>160</sup> *Id.*

<sup>161</sup> *Id.* at 335.

court. The Fifth Circuit should have recognized that the lower court did not perform any actual analysis in *St. Paul Guardian Insurance Co.* of the text of Article 9 before hastily adopting the reasoning. Given the Fifth Circuit's apparent care in other parts of the opinion, it seems likely that the court's method of analysis reflects a simple lack of understanding regarding how to navigate, analyze and apply Article 9 of the CISG. In order to promote the uniformity that the Fifth Circuit recognized should be promoted,<sup>162</sup> Article 9 must be interpreted and applied by U.S. and other courts in a uniform and proper manner.

4.2.3. *China North Chemical Industries Corp. v. Beston Chemical Corp.*

Following the Fifth Circuit's decision in *BP Oil*, a federal district court in Texas continued this trend of automatic incorporation of Incoterms under Article 9(2) without engaging in the requisite analysis prescribed by the CISG.<sup>163</sup> The case arose out of a contract between a Chinese seller, China North Chemical Industries Corporation ("Nocinco"), and a U.S. buyer, Beston Chemical Corporation ("Beston"), for the sale of 718 pallets of explosive boosters.<sup>164</sup> The parties entered into a written sales agreement for the supply of the explosive boosters, which indicated that the explosive boosters were to be delivered "'CIF' to Berwick, Louisiana."<sup>165</sup> The goods were damaged in transit on the ocean-going vessel that had been nominated as the carrier, apparently due to a combination of improper stowage of the cargo, inadequate securing of the cargo, and a strong storm that tossed the ship at sea.<sup>166</sup> Taking the position that Nocinco had undertaken additional obligations in connection with the loading and stowage of the cargo and had breached those obligations, Beston paid some—but would not agree to pay all—of the amounts that would otherwise have been due under the contract.<sup>167</sup>

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<sup>162</sup> See *id.* at 337.

<sup>163</sup> See generally *China N. Chem. Indus. Corp. v. Beston Chem. Corp.*, No. Civ.A. H-04-0912, 2006 WL 295395 (S.D. Tex. Feb. 7, 2006).

<sup>164</sup> *Id.* at \*1.

<sup>165</sup> *Id.*

<sup>166</sup> See *id.* at \*4-\*5 (describing conditions under which goods were damaged before reaching Berwick, Louisiana).

<sup>167</sup> See *id.* at \*5 ("Beston made payments to Nocinco in December 1999, April 2000, and May 2000, for a total of 15% of the Contract price. Beston refused to pay the remaining balance, however, due to the Cargo's damaged condition.").

The parties agreed that the CISG governed their contract and dispute.<sup>168</sup> Applying the CISG, the court concluded that inclusion in the parties' written contract of the CIF delivery term allocated to Beston the risk of loss of the goods after the goods passed the ship's rail in the port of departure.<sup>169</sup> The court used the definition of CIF that is set forth in Incoterms 1990 to reach that conclusion.<sup>170</sup> Unfortunately, this court also conducted its analysis under the stated assumption that Incoterms are incorporated into the CISG through Article 9(2).<sup>171</sup>

Not surprisingly, the court reached that incorrect conclusion with very little analysis, instead simply asserting that "Incoterms is the dominant source of definitions for the commercial delivery terms used by parties to international sales contracts," and citing to the *St. Paul Guardian Insurance Co.* and *BP Oil* decisions.<sup>172</sup> And thus, once again, the recurring problems with Article 9 analysis of Incoterms were repeated here: the court reached this strange and insupportable conclusion that somehow, despite the plain language of Article 9 and the illogic involved, Incoterms becomes part of the CISG itself, rather than simply a part of the parties' agreement; the court did not appear to consider whether Article 9(1) was the relevant mechanism for concluding that the parties intended to incorporate into their contract the default delivery term definitions provided by Incoterms; and the court engaged in no analysis of the three discrete requirements of Article 9(2).

This continuing careless application of Article 9 of the CISG is problematic in its own right. In this case, there was a related but distinct problem, insofar as the court failed to recognize the importance of considering "all relevant circumstances of the case" in determining the intent of the parties.<sup>173</sup> There was ample (and apparently undisputed) evidence of Beston's actual intent for the proper loading, stowage, and securing of the cargo.<sup>174</sup> The evidence consisted of substantial conduct by the parties, including actions taken by Nocinco vis-à-vis the loading and stowage of the

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<sup>168</sup> *Id.* at \*6.

<sup>169</sup> *See id.* at \*8.

<sup>170</sup> *See id.* at \*6.

<sup>171</sup> *Id.*

<sup>172</sup> *Id.*

<sup>173</sup> CISG, *supra* note 7, at art. 8(3).

<sup>174</sup> *See China N. Chem. Indus. Corp.*, 2006 WL 295395, at \*1-\*5 (chronicling Beston's intention regarding the loading, stowage, and securing of the cargo).

goods, as well as numerous communications between the parties, subsequent to the formation of their contract.<sup>175</sup> The evidence tended to show that Beston intended that Nocinco would assume responsibility for satisfaction of specific stowage requirements.<sup>176</sup>

The important factual question is whether Nocinco shared Beston's intent. Arguably, Nocinco's conduct suggested that it recognized an obligation under the parties' agreement that exceeded the default obligations otherwise binding on Nocinco under the Incoterms definition of the CIF delivery term. The court should have considered this factual possibility.<sup>177</sup> That conduct was relevant for determining the parties' actual intent regarding the scope of Nocinco's obligations.<sup>178</sup>

The court conclusorily stated that conduct could not trump the written delivery term: "[w]hatever Nocinco did at Beston's urging to accommodate its customer's requirements for correct stowage of the Cargo, including the exchanges of e-mails that reported those activities, did not alter the CIF term contained in the parties' written Contract."<sup>179</sup>

This statement by the court reflects the U.S. legal tradition of adhering rigidly to the court's understanding of a written contract even in the face of contrary extrinsic evidence. Under the U.S. parol evidence rule, it is generally difficult or impossible to introduce extrinsic evidence when the parties have entered into a written agreement, especially when that extrinsic evidence appears to contradict the express terms of the written agreement.<sup>180</sup> But the

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<sup>175</sup> See *id.* (recounting actions taken by Nocinco in the loading and stowage of goods).

<sup>176</sup> See *id.* at \*1 (describing Beston's September 3, 1999 fax to Nocinco including a list of stowage requirements).

<sup>177</sup> See CISG, *supra* note 7, at art. 8(3) ("In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties.").

<sup>178</sup> *Id.*

<sup>179</sup> *China N. Chem. Indus. Corp.*, 2006 WL 295395 at \*8.

<sup>180</sup> See U.C.C. § 2-202 (2012) ("Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in a writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be explained or supplemented (a) by course of performance, course of dealing, or usage of trade (Section 1-303) ; and (b) by evidence of consistent additional terms unless the court finds the writing to have been intended also as a complete and exclusive

CISG contains no parol evidence rule. And despite some U.S. jurists' yearning to cling to the parol evidence rule and the legal philosophy it represents, the CISG contemplates a different analysis—one that recognizes that written agreements sometimes fail to tell the whole truth.<sup>181</sup> Thus, under Article 8(3) of the CISG, courts are required to give due consideration to all relevant circumstances, including the parties' established practices, usages, and "any subsequent conduct of the parties" in determining party intent.<sup>182</sup>

In this case, it is plausible that the parties adopted the CIF delivery term but, at the time of contract, intended to vary the allocation of risk and responsibility established by the Incoterms definition of the CIF delivery term. The CISG gives the parties great freedom to establish for themselves the terms of their bargain.<sup>183</sup> This seems unlikely, because the parties could have simply used a different delivery term that more closely approximated their bargain in that case. Still, it is a factual possibility, and Incoterms do contemplate varying by agreement the default allocation of risk and responsibility.<sup>184</sup>

Based on the available facts, it seems more likely that the CIF term originally agreed upon was subsequently modified by the parties. The CISG provides that a contract may be modified "by

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statement of the terms of the agreement."); *see also* RESTATEMENT (SECOND) OF CONTRACTS §§ 215-216 (1981) ("Except as stated in the preceding Section, where there is a binding agreement, either completely or partially integrated, evidence of prior or contemporaneous agreements or negotiations is not admissible in evidence to contradict a term of the writing. . . . (1) Evidence of a consistent additional term is admissible to supplement an integrated agreement unless the court finds that the agreement was completely integrated. (2) An agreement is not completely integrated if the writing omits a consistent additional agreed term which is (a) agreed to for separate consideration, or (b) such a term as in the circumstances might naturally be omitted from the writing.").

<sup>181</sup> *See* William P. Johnson, *Understanding Exclusion of the CISG: A New Paradigm of Determining Party Intent*, 59 BUFF. L. REV. 213, 216, 266-69 (2011) (arguing that the "writing is not dispositive of the parties' intent.").

<sup>182</sup> CISG, *supra* note 7, at art. 8(3).

<sup>183</sup> *See id.* at art. 6 ("The parties may exclude the application of this Convention or, subject to article 12, derogate from or vary the effect of any of its provisions.").

<sup>184</sup> *See* INCOTERMS, *supra* note 1, at 9 (explaining that the Incoterms rules do not prohibit alterations to the rules, but warning that dangers may arise in altering Incoterms rules if parties do not make the alternations clear). *See also* SCHWENZER, HACHEM & KEE, *supra* note 4, ¶ 29.27 ("[P]arties usually enjoy the freedom of amending a trade term and as such it is always a question of contract interpretation.").



the mere agreement of the parties.”<sup>185</sup> And there was significant evidence available that might have been considered more carefully to take into account this possibility.

Of course it is important to acknowledge that the parties might have adopted the CIF delivery term and its allocation of risk and responsibility without variation, and that the parties in fact never intended to modify that delivery term. Such a factual finding would have been consistent with this court’s ultimate conclusion.<sup>186</sup> But to reach that conclusion requires due consideration of all of the evidence available, including the parties’ conduct, and a finding regarding the parties’ intent, and not simply an assumption that the court’s understanding of a term of the parties’ written agreement must prevail.<sup>187</sup>

A written contract itself of course offers important evidence of the parties’ intent. But it is not the only evidence of party intent, and the court is obligated to consider whether the actual intent of the parties is better understood by reference to other relevant circumstances.<sup>188</sup> Perhaps because it was unaware of its responsibility to do so, the court in this case does not appear to have engaged in that analysis.

4.2.4. *Cedar Petrochemicals, Inc. v. Dongbu Hannong Chemical Co., Ltd.*

Finally, a federal district court in New York recently took the improper analysis to a new level.<sup>189</sup> The *Cedar Petrochemicals*

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<sup>185</sup> CISG, *supra* note 7, at art. 29(1). Notably, China declared when it approved the CISG that any provision of Article 29 of the CISG that allowed modification of a contract by agreement to be made in any form other than in writing, would not apply. See CISG Status, *supra* note 7, Notes. But Nocinco did not appear to base its arguments on any Chinese statute of frauds, focusing instead on the inclusion of the CIF term in the written agreement. See *China N. Chem. Indus. Corp. v. Beston Chem. Corp.*, No. Civ.A. H-04-0912, 2006 WL 295395, at \*7 (S.D. Tex. Feb. 7, 2006) (“Nocinco . . . contends that under the Contract’s CIF term the risk of loss passed to Beston”). In addition, there were writings present here, including a faxed list of stowage requirements. See *id.* at \*1.

<sup>186</sup> See *id.* at \*8 (holding that “Nocinco is entitled to recover the Contract price, subject to any offsets based upon Beston’s claims that portions of the Cargo were defective and/or did not meet the Contract’s quality specifications, which issue remains to be tried”).

<sup>187</sup> See CISG, *supra* note 7, at art. 8(3) (stating that the intent of a party must be determined from all relevant circumstances).

<sup>188</sup> *Id.*

<sup>189</sup> See generally *Cedar Petrochemicals, Inc. v. Dongbu Hannong Chem. Co., Ltd.*, No. 06 Civ. 3972(LTS)(JCF), 2011 WL 4494602 (S.D.N.Y. Sept. 28, 2011).

decision arose out of a contract dispute between Cedar Petrochemicals, Inc., a New York-based buyer (“Cedar”), and Dongbu Hannong Chemical Co., Ltd., a South Korean supplier (“Dongbu”), by which Dongbu agreed to supply Cedar with a predetermined quantity of phenol.<sup>190</sup> The parties entered into a written agreement, and the contract provided for delivery of the phenol “FOB Ulsan Anchorage, Korea.”<sup>191</sup> The written agreement also included a clause by which the parties expressed their agreement that Incoterms 2000 would govern their use of the delivery term.<sup>192</sup>

The agreement specified certain requirements relating to the color of the phenol, which were satisfied at the time of loading in the port of shipment, but when the phenol reached its port of destination, the color had degenerated and was no longer within the agreed-upon specifications.<sup>193</sup> The parties disagreed as to whose risk the degeneration was, and Cedar brought a claim against Dongbu under Articles 35 and 36 of the CISG.<sup>194</sup> Dongbu moved for summary judgment on the basis that the express terms of the parties’ written agreement displaced the CISG provisions on which Cedar’s claim was based.<sup>195</sup>

In its analysis of Dongbu’s motion, the court stated, “[i]t is worth noting at the outset that the entire body of Incoterms—‘F.O.B.’ included—is incorporated into the CISG through Article 9(2) thereof.”<sup>196</sup> In this case, that misstatement of the relationship between Incoterms and CISG led to an even more troubling statement by the court: “Dongbu makes no attempt to explain how a term that is made part of the CISG could also derogate from it.”<sup>197</sup> Thus, the misunderstanding of the relationship between Incoterms and the CISG had a direct effect on the court’s analysis of the issue before it. This misunderstanding led to a confused analysis in

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<sup>190</sup> *Id.* at \*1.

<sup>191</sup> *Id.*

<sup>192</sup> *See id.* at \*3 (noting that “[a]s provided in the contract, the definition of ‘F.O.B.’ is furnished by Incoterms (International Commercial Terms) 2000 . . .”).

<sup>193</sup> *See id.* at \*1-2 (“The parties concur that the final agreement called for phenol that met a color specification of 10 Hazen units maximum . . . . When the phenol arrived in Rotterdam . . . tests revealed that its color had degenerated to over 500 Hazen units.”).

<sup>194</sup> *Id.* at \*2.

<sup>195</sup> *Id.*

<sup>196</sup> *Id.* at \*4.

<sup>197</sup> *Id.*

which the court then asserted, without drawing explicitly on the record in any way, that the parties' written agreement did not "explicitly displace any provision of the CISG."<sup>198</sup> But of course that is exactly what the parties did when they incorporated Incoterms 2000 and the definition of the FOB delivery term into their agreement by explicit reference. In doing so, they displaced any of the inconsistent default delivery provisions contained in Articles 30-34, 60, and 66-69 of the CISG.

Fortunately, the analysis here did not turn on any of those provisions and, instead, turned on the latent defect provisions of Article 36, together with the provisions of Article 35, which contain terms that create the approximate equivalent under the CISG of warranties, express and implied, under the UCC.<sup>199</sup> For that reason, the court's gross misstatements of the operation of the CISG and the relationship between the CISG and Incoterms probably did not affect the outcome.

#### 4.3. *Emerging Trend, Emerging Precedent?*

Taken together, these four cases highlight a recurring problem that arises with respect to CISG interpretation: a tendency to misunderstand, or to fail altogether to see, the plain language of the CISG. Here, that misunderstanding relates specifically to the relationship between Incoterms and the CISG.

The precedential weight of these four cases is dubious. Three are unpublished opinions of trial courts. The remaining case is a published opinion of the Fifth Circuit, but the issue of the

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<sup>198</sup> *Id.*

<sup>199</sup> See CISG, *supra* note 7, at art. 35 ("(1) The seller must deliver goods which are of the quantity, quality and description required by the contract and which are contained or packaged in the manner required by the contract. (2) Except where the parties have agreed otherwise, the goods do not conform with the contract unless they: (a) are fit for the purposes for which goods of the same description would ordinarily be used; (b) are fit for any particular purpose expressly or impliedly made known to the seller at the time of the conclusion of the contract, except where the circumstances show that the buyer did not rely, or that it was unreasonable for him to rely, on the seller's skill and judgment; (c) possess the qualities of goods which the seller has held out to the buyer as a sample or model; (d) are contained or packaged in the manner usual for such goods or, where there is no such manner, in a manner adequate to preserve and protect the goods. (3) The seller is not liable under subparagraphs (a) to (d) of the preceding paragraph for any lack of conformity of the goods if, at the time of the conclusion of the contract, the buyer knew or could not have been unaware of such lack of conformity.").

relationship between Incoterms and the CISG was not squarely before the court, nor was the court focused on discerning the appropriate analysis of Incoterms definitions of delivery terms as usage for purpose of incorporation into the parties' agreement of that definition. Thus, the decision should not be viewed as binding precedent as it relates specifically to those issues.

Any court confronted with a question relating to the proper analysis of Incoterms and the CISG should instead use the following framework.

#### *4.4. A Framework for Analyzing Incoterms Under Article 9*

In order to analyze whether Incoterms definitions have been incorporated into or have otherwise somehow become part of the parties' agreement and are therefore the appropriate source for determining how the parties have allocated between them risk of loss of goods in transit and the responsibility to satisfy customs formalities and the like, the court should engage in a careful, step-by-step analysis that is actually contemplated by the CISG. This might include analysis under Article 9, but it will not necessarily include Article 9.

Of course, this is only relevant when the parties disagree on whether some Incoterms definition has become part of their agreement. In other words, if one party has claimed that Incoterms is the appropriate source for allocation of risk and responsibility, and the other party has disputed that contention, the party claiming that the Incoterms definition is part of the parties' agreement bears the burden of proof. This burden of proof can be satisfied in one of three ways, as the following demonstrates.

##### *4.4.1. Incorporation by Reference*

When parties negotiate a written commercial contract, sometimes they agree that some ancillary document or resource that already exists in final form should be part of their agreement. This could be one of the party's standard terms and conditions; it could be a Quality Assurance Program; it could be a set of industry standards or manufacturing practices; and so on. The parties could copy the ancillary document or resource into their written commercial contract, word for word, line by line. However, that would be time-consuming and would carry risk of error.

Instead, parties simply incorporate the ancillary document or resource by reference. In other words, the parties will include in

their written commercial contract an express term that makes it clear that that other document or resource is deemed to be part of the agreement between the parties and is binding on the parties, as if it were written into the agreement itself.

Incoterms 2010 specifically contemplates and encourages incorporation by reference: “[i]f you want the Incoterms® 2010 rules to apply to your contract, you should make this clear in the contract, through such words as, ‘[the chosen Incoterms rule including the named place, followed by] Incoterms® 2010’.”<sup>200</sup> And of course the CISG also allows incorporation by reference. Article 6 allows the parties to derogate from the default provisions of the CISG, and Article 11 makes it clear that no particular form is necessary for this to be accomplished.<sup>201</sup>

Incorporation by reference is what the parties did in the *Cedar Petrochemicals* decision.<sup>202</sup> When the parties specifically incorporate Incoterms by reference, there is no need to engage in any analysis under Article 9. It is enough for the court to conclude that the parties have exercised their right under the CISG to choose for themselves the terms of their bargain by expressly incorporating Incoterms rules into their contract.

In short, the court should first consider whether the parties have incorporated Incoterms definitions into their agreement by selection of a delivery term accompanied by an express reference to a specified version of Incoterms. The party arguing for application of Incoterms bears the burden to show that Incoterms have been incorporated by reference into the parties’ agreement. This requires a factual inquiry. If the finder of fact finds that the parties have incorporated Incoterms into their agreement by express reference, then Article 9 is unnecessary for that part of the court’s analysis.

#### 4.4.2. Usage as an Agreed-Upon Term

Often the parties will include in their shipping documents or in their contract a delivery term and a named place, but will not

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<sup>200</sup> INCOTERMS, *supra* note 1, at 5.

<sup>201</sup> See CISG, *supra* note 7, at arts. 6 & 11.

<sup>202</sup> See *Cedar Petrochemicals, Inc. v. Dongbu Hannong Chem. Co., Ltd.*, No. 06 Civ. 3972(LTS)(JCF), 2011 WL 4494602, at \*1 (S.D.N.Y. Sept. 28, 2011) (outlining the basis of the Defendant’s motion for summary judgment “on the legal contention that the contract displaced the provisions of the CISG under which [Plaintiff] brings its action”).

include any express reference to Incoterms. When that happens, it is possible that the parties have agreed that the established practices prescribed by the applicable Incoterms definition for their selected delivery term are established practices that are part of their agreement. Article 9(1) provides a mechanism for the established practices prescribed by the applicable Incoterms definition to become part of the parties' contract by their simple agreement.<sup>203</sup>

For the Incoterms definition of the delivery term to become part of the parties' agreement under Article 9(1), two things must be shown.<sup>204</sup> First, the Incoterms definition must constitute usage,<sup>205</sup> although it is not necessary for that usage to be widely known or regularly observed.<sup>206</sup> Second, the parties must have agreed to the usage.<sup>207</sup> There is no real question regarding whether Incoterms definitions constitute usage. Because usage refers to any established practices of participants within a group, the Incoterms definitions—which reflect established practices of merchants in a variety of industries—readily satisfy that definition.

The salient question under Article 9(1), then, is whether the parties have agreed to the usage. Article 9(1) requires no particular manifestation of party agreement.<sup>208</sup> It is enough that the contracting parties have in some way agreed to be bound by the usage, have agreed to observe the usage, have agreed to make the usage applicable to their agreement, or have otherwise agreed to the usage. This analysis also requires a factual inquiry. If a party claims that an Incoterms definition of a delivery term is part of the parties' contract as usage under Article 9(1), then that party bears the burden of showing that the parties have so agreed. It is up to the finder of facts to determine whether, as a matter of fact, the parties have agreed to Incoterms definitions as the source intended to define their selected delivery term.<sup>209</sup> If the finder of facts finds that the parties have agreed that the Incoterms definitions are the

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<sup>203</sup> CISG, *supra* note 7, at art. 9(1).

<sup>204</sup> *Id.*

<sup>205</sup> *Id.*

<sup>206</sup> *See id.*

<sup>207</sup> *Id.*

<sup>208</sup> *See id.*; *see also id.* at arts. 6 & 11.

<sup>209</sup> Part of the analysis should focus on whether the parties *actually* intended to be bound by Incoterms, and that analysis should be grounded in the principles contained in Article 8. *See* CISG, *supra* note 7, at art. 8.

relevant source, then the applicable Incoterms definition is a term of the parties' agreement.

#### *4.4.3. Usage as an Implied Term*

When a court engages in the foregoing analysis and concludes that the party claiming that the Incoterms definitions are the relevant source of definitions for the contract has failed to bear its burden under Article 9(1), that conclusion does not necessarily end the analysis.

Next, the party claiming that Incoterms provide the relevant definition might argue that the applicable Incoterms definition has become part of the parties' agreement under Article 9(2), which does not require party agreement.<sup>210</sup> This inquiry requires a more involved, two-part analysis. The first part of the analysis focuses on whether Incoterms are the type of usage that falls within the scope of Article 9(2).

In order to determine whether Incoterms are within the scope of Article 9(2), and therefore potentially an implied term of the parties' agreement under Article 9(2), the court must consider whether three distinct requirements can be shown to have been satisfied:

- (i) Did each party know, or ought each party to have known, of Incoterms?
- (ii) Do Incoterms constitute a usage that in international trade is widely known to parties to contracts of the type involved in the particular trade concerned here?
- (iii) Do Incoterms constitute a usage that in international trade is regularly observed by parties to contracts of the type involved in the particular trade concerned here?<sup>211</sup>

The party arguing for application of the applicable Incoterms definition as an implied term bears the burden of showing that these three requirements have been satisfied. These questions must be analyzed and answered by reference to the particular trade that is relevant for the contract at issue.<sup>212</sup> If the answer to

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<sup>210</sup> *See id.* at art. 9(2).

<sup>211</sup> *See id.*

<sup>212</sup> *Id.*

any of these three questions is 'no,' then the usage is not part of the parties' agreement under Article 9(2).<sup>213</sup>

If the answer to each of the questions is 'yes' and Incoterms are therefore the type of usage that falls within the scope of Article 9(2) for these contracting parties, then the second part of the analysis asks whether the parties nevertheless opted out of the usage.<sup>214</sup> Specifically, did the parties agree not to have impliedly made the usage in question applicable to their contract?

It is important to note that the inquiry in the second part of the analysis is not whether the parties affirmatively agreed to make the usage applicable to their contract.<sup>215</sup> Such affirmative agreement is not required under Article 9(2).<sup>216</sup> In fact, if there is such affirmative agreement, then Article 9(1) is the appropriate section to apply. Rather, the inquiry is whether the parties have affirmatively agreed *not* to make the usage a part of their agreement.<sup>217</sup> Notably, however, Article 9(2) requires no particular means of manifesting that agreement.<sup>218</sup> Once again, it requires factual inquiry to determine whether the parties have manifested such agreement.

If the first part of the analysis shows that Incoterms are usage that is applicable under Article 9(2), then the burden shifts to the party who would like to evade application of the applicable Incoterms definition to show that the parties opted out of it.

If a party claims that Incoterms are part of a contract of sale of goods under Article 9(2), it is up to the finder of fact to determine whether Incoterms are the type of usage that is within the scope of Article 9(2), for these parties to this contract, by applying the first part of the two-part analysis. If the other party then claims that the parties have nevertheless opted out of Incoterms, then it is up to the finder of fact to determine whether that other party has met its burden to show that the parties have in fact opted out of Incoterms. If the finder of fact finds that the Incoterms definition is within the scope of Article 9(2) and does not find that the parties have opted out of Incoterms, then the applicable Incoterms definition is a term of the parties' agreement.

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<sup>213</sup> *See id.*

<sup>214</sup> *See id.*

<sup>215</sup> *See id.*

<sup>216</sup> *See id.*

<sup>217</sup> *Id.*

<sup>218</sup> *See id.*; *see also id.* at arts. 6 & 11.



The foregoing analysis could also apply even when the parties have included no delivery term in their contract documents. It will be much more difficult for the party who would like a particular Incoterms definition to be part of the agreement to carry its burden, but the analytical framework is the same.

## 5. CONSIDERING THE *TRAVAUX PRÉPARATOIRES* OF THE CISG

### 5.1. *Using the Travaux Préparatoires*

The *travaux préparatoires* of the CISG support the foregoing analysis of the role of Incoterms under the CISG. When the text of a treaty is insufficient to answer a question definitively, the treaty's *travaux préparatoires*, or drafting history, should be considered. Specifically, a treaty's drafting history is relevant to confirm the text, context, object, and purpose of the treaty, to resolve ambiguity, and to prevent a "manifestly absurd or unreasonable" result.<sup>219</sup> It is therefore important to consider what, if anything, the *travaux préparatoires* tell us about the role of Incoterms or other commonly used delivery terms under Article 9 of the CISG.

A draft of the CISG was prepared by the United Nations Commission on International Trade Law (UNCITRAL) and a diplomatic conference of plenipotentiaries consisting of representatives of sixty-two independent states, including the United States, was convened in 1980 to consider the draft.<sup>220</sup>

### 5.2. *Incoterms in the Travaux Préparatoires*

The First Committee of the Conference considered the draft Convention on Contracts for the International Sale of Goods

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<sup>219</sup> Vienna Convention, *supra* note 48, at arts. 31(2) & 32. U.S. courts, in particular, have shown willingness to use a treaty's *travaux préparatoires* to interpret the treaty. RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 325 Reporters' Note 1 (1987) ("United States courts, accustomed to analyzing legislative materials, have not been hesitant to resort to *travaux préparatoires*.").

<sup>220</sup> See U.N. Conf. on Contracts for the Int'l Sale of Goods, Vienna, Austria, Mar. 10–Apr. 11, 1980, *Final Act of the United Nations Conference on Contracts for the International Sale of Goods*, ¶¶ 1–3, U.N. Doc. A/CONF.97/18 (Apr. 11, 1980), reprinted in U.N. Conf. on Contracts for the Int'l Sale of Goods, *Official Records*, U.N. Doc. A/CONF.97/19, at 176–77 (1991) [hereinafter *Official Records*], available at <http://www.uncitral.org/pdf/english/texts/sales/cisg/a-conf-97-19-ocred-e.pdf>; see also CISG, *supra* note 7, Explanatory Note, available at <http://www.uncitral.org/pdf/english/texts/sales/cisg/V1056997-CISG-e-book.pdf>.

approved by UNCITRAL,<sup>221</sup> whereupon several amendments to Article 9 (numbered in the draft as Article 8) were proposed.<sup>222</sup> Specifically, the *travaux préparatoires* reveal that the drafters considered two proposals intended to make it more explicit that trade terms, including specifically Incoterms, would automatically be deemed to be part of the usage described in Article 9. However, the drafters rejected the proposals.<sup>223</sup>

The first proposal was an amendment to Article 9(2) that was proposed by Sweden.<sup>224</sup> The proposed Sweden amendment was to insert the words “or an interpretation of a trade term” between the words “a usage” and “of which the parties knew.”<sup>225</sup> Thus, Article 9(2) would have read as follows:

The parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage or an interpretation of a trade term of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.<sup>226</sup>

The second proposal was an amendment proposed by Egypt to add a third paragraph to Article 9, as follows: “[w]here expressions, provisions or forms of contract commonly used in

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<sup>221</sup> U.N. Conf. on Contracts for the Int’l Sale of Goods, Vienna, Austria, Mar. 10–Apr. 11, 1980, *Text of Draft Convention on Contracts for the International Sale of Goods Approved by the United Nations Commission on International Trade Law*, U.N. Doc. A/CONF.97/5 (Mar. 14, 1979), reprinted in *Official Records*, supra note 220, at 5–14.

<sup>222</sup> “Amendments were submitted to article 8 by China (A/CONF.97/C.1/L.24), Czechoslovakia (A/CONF.97/C.1/L.40), India (A/CONF.97/C.1/L.34), Sweden (A/CONF.97/C.1/L.19), Pakistan (A/CONF.97/C.1/L.64), United States of America (A/CONF.97/C.1/L.6), France (A/CONF.97/C.1/L.23) and Egypt (A/CONF.97/C.1/L.44).” U.N. Conf. on Contracts for the Int’l Sale of Goods, Vienna, Austria, Mar. 10–Apr. 11, 1980, *Report of the First Committee*, art. 8, ¶ 2, U.N. Doc. A/CONF.97/11 (Apr. 7, 1980) [hereinafter *Report of the First Committee*], reprinted in *Official Records*, supra note 220, at 89.

<sup>223</sup> U.N. Conf. on Contracts for the Int’l Sale of Goods, Vienna, Austria, Mar. 10–Apr. 11, 1980, *Summary Records of the Plenary Meetings, 7th Plenary Meeting*, ¶¶ 61, 63, [hereinafter *Summary Records – 7th Plenary*] reprinted in *Official Records*, supra note 220, at 269.

<sup>224</sup> *Report of the First Committee*, supra note 222, at art. 8, ¶ 3.

<sup>225</sup> *Id.*

<sup>226</sup> *Id.* (underlining denotes proposed additional language).

commercial practice are employed, they shall be interpreted according to the meaning usually given to them in the trade concerned."<sup>227</sup>

Both amendments were intended to account for commonly used delivery terms such as Incoterms.<sup>228</sup> Because their purpose was the same, the two proposals were discussed together at the seventh meeting of the First Committee.<sup>229</sup> Mr. Hjerner of Sweden explained that the aim of the sponsors of the two proposals was "to cover the question of the interpretation of trade terms, such as 'FOB', 'CIF', 'landed' and 'net weight'."<sup>230</sup> Mr. Shafik of Egypt confirmed that his purpose was the same "to reintroduce the reference to trade terms."<sup>231</sup>

There was some support for the idea.<sup>232</sup> Mr. Dabin of Belgium, for example, stated that he "saw no reason why the draft should make no reference to INCOTERMS."<sup>233</sup> However, there was also strong opposition grounded in the notion that Incoterms were not necessarily widely known or widely used, and that other sources of delivery terms, such as U.S. commercial law, provided different definitions for certain delivery terms.<sup>234</sup>

In fact, one of the unsuccessful predecessor conventions to the CISG, the Convention relating to a Uniform Law on the International Sale of Goods, adopted by the International Institute for the Unification of Private Law, or UNIDROIT, included a provision that appeared more squarely to incorporate definitions of commonly used trade terms into its provisions. That convention provided that "[w]here expressions, provisions or forms of contract commonly used in commercial practice are employed, they shall be interpreted according to the meaning usually given to them in the

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<sup>227</sup> *Id.*

<sup>228</sup> See *Summary Records – 7th Plenary, supra* note 223, ¶¶ 36-58, reprinted in *Official Records, supra* note 220, at 267-69 (noting that the delegation from Belgium suggested adding a specific reference to Incoterms to the Egypt amendment for clarity and noting that the delegations from Japan, France, and the USSR objected to the amendment on the grounds that "Incoterms were not well known everywhere").

<sup>229</sup> *Id.* ¶ 34.

<sup>230</sup> *Id.* ¶ 36.

<sup>231</sup> *Id.* ¶ 38.

<sup>232</sup> See *id.* ¶ 37 (noting the Belgium representative).

<sup>233</sup> *Id.*

<sup>234</sup> See *id.* ¶¶ 44, 52-53, 55 (noting the objections of Mr. Lebedev [Union of Soviet Socialist Republics] and Mr. Michida [Japan] to the Egyptian proposal, based primarily on the "unduly vague" language of the proposed provision).

trade concerned.”<sup>235</sup> When the CISG was drafted the drafters dropped that provision. Although there was some subsequent discussion regarding the value of reintroduction of that provision,<sup>236</sup> it was not reintroduced.

Ultimately, the proposed amendments were rejected by the First Committee.<sup>237</sup> Subsequently, at the sixth meeting of the Plenary Committee, the Swedish representative withdrew the Swedish amendment and the Egyptian amendment was rejected.<sup>238</sup>

Incoterms and other delivery terms therefore could become part of the parties’ agreement under Article 9, but Incoterms should not automatically become part of the parties’ agreement without the requisite analysis. Instead, Incoterms should be analyzed in the same way that other potentially applicable usages are analyzed, through the appropriate lens of Article 9.

## 6. CONCLUSION

A troubling trend has begun to emerge as U.S. courts have undertaken early analysis of the relationship between Incoterms and the CISG. U.S. courts have demonstrated misunderstanding of the relationship between Incoterms and the CISG and the role of Article 9 of the CISG in the analysis. Three related but distinct problems have recurred. These problems can be corrected by courts who look carefully at the language of Article 9 of the CISG.

Thus, courts should never conclude that Incoterms definitions are somehow incorporated into the CISG itself. That is illogical, insupportable, and improper.

Courts should also not conclude that Incoterms definitions constitute a binding term of the parties’ contract under Article 9(2) without first engaging in the analysis required by Article 9(1).

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<sup>235</sup> Convention Relating to a Uniform Law on the International Sale of Goods art. 9(3), July 1, 1964, 834 U.N.T.S. 107.

<sup>236</sup> See U.N. Conf. on Contracts for the Int’l Sale of Goods, Vienna, Austria, Mar. 10–Apr. 11, 1980, *Analysis of Comments and Proposals by Governments and International Organizations on the Draft Convention on Contracts for the International Sale of Goods, and on Draft Provisions Concerning Implementation, Reservations and Other Final Clauses, Prepared by the Secretary-General*, art. 8, ¶ 4, U.N. Doc. A/CONF.97/9 (Feb. 21, 1980), reprinted in *Official Records*, supra note 220, at 71-82.

<sup>237</sup> *Report of the First Committee*, supra note 222, art. 8, ¶ 3, reprinted in *Official Records*, supra note 220, at 90.

<sup>238</sup> U.N. Conf. on Contracts for the Int’l Sale of Goods, Vienna, Austria, Mar. 10–Apr. 11, 1980, *Summary Records of the Plenary Meetings, 6th Plenary Meeting*, ¶¶ 56, 59-60, U.N. Doc. A/CONF.97/SR.6 (Apr. 8, 1980), reprinted in *Official Records*, supra note 220, at 202-03.

When the parties have included in their written agreement an express delivery term but have simply failed to identify in their written agreement the source of law to be used to define that delivery term, it is entirely possible that the parties have in fact agreed that the Incoterms definition of the delivery term is the applicable definition. If the fact finder finds that that was the actual intent of the parties, after considering all relevant circumstances of the case, the Incoterms definition of the term is arguably part of the parties' agreement under Article 9(1), which allows for incorporation into the agreement of the usage in question by the mere agreement of the parties.

Finally, when analyzing usage under Article 9(2), which provides for usage to become a binding part of the parties' agreement without their express consent, the court must carefully consider each of the three discrete requirements created by Article 9(2) to identify usage that is appropriately binding on contracting parties as an implied term. It is only usage that can satisfy those requirements in the context of the particular case before the court that is reasonable to impose on the parties without their express consent.

Delivery terms serve highly important purposes for international trade and commerce; they increase efficiency, they contribute to a sense of association and group identity, and they aid in certainty and predictability—at least they should. Furthermore, delivery terms can and will contribute to certainty and predictability more regularly, once U.S. courts begin to look more carefully at the language of Article 9 of the CISG. It is essential that courts do so to facilitate, rather than hinder, international trade. It is essential because predictable, proper analysis and uniform application of Article 9 are necessary in order to avoid unfair surprise, to protect the reasonable expectations of the parties, and to contribute to certainty in the otherwise rough seas of international trade and commerce.