

International Trade & Title: Security & Tax Concerns—Part 1

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INTERNATIONAL TRADE BRINGS WITH IT SUBTLE

complexities that now can have major consequences in areas not usually considered problematic for exporters and importers. One of those complexities is the concept of ownership or title and the relationship of title to liability and security. We will examine the significance of the passing of title in international sales and its resulting impact on taxation and homeland security liability.

Ownership and Title

In general, a sale is defined as the exchange of ownership for a price. If there's no transfer of ownership, there's no sale. Given the greater distances and the options available to buyers and sellers in international business, the problems with the transfer of ownership involve the locus of exchange. For instance, does a U.S. importer take ownership of the goods in the foreign nation, aboard the vessel en route, when they are discharged from the vessel, or when the goods reach his or her warehouse in the United States? If the merchandise belongs to someone else until it reaches the U.S. destination, who has the security risk and liability? Where does the merchandise become the inventory of the buyer? Are assets determined on the sale or on custody? Two legal sources are used in the U.S. to explain the legality of transferring title: the *Uniform Commercial Code* (UCC) and the *United Nations Convention on Contracts for the International Sale of Goods* (CISG). Both relegate the passing of title as a component of contract law.

The Uniform Commercial Code

In general, title is passed as intended by the buyer and seller. Under the UCC, however, there are four accepted rules to use in determining when title changes from the seller to the buyer, as described in Part 4, Title, Creditors, and Good Faith Purchasers, Paragraph 2-401:

1. No title can transfer unless both the buyer and seller first identify the goods in the contract, providing an insurable interest in them. Title transfers upon the agreement of the seller and buyer.
2. Unless otherwise explicitly agreed to, title passes at the time and location where the seller physically delivers the goods to the buyer. In this case, the time and place of the transfer of an actual document of title is preempted by physical delivery of the identified goods. Also, if the seller is required by contract to send the goods to the buyer but not to destination, the title passes at the actual time and place of shipment. Finally, if the contract requires delivery at a specific destination, title passes at arrival to that destination.
3. If delivery is made without moving the goods, the transfer of ownership occurs when the document of title is delivered; if the goods are already identified at the time of contract and no documents are to be delivered, title passes at the establishment of the contract.
4. A refusal to accept or keep the goods reinvests the title to the seller.

Title of contractually identified goods, therefore, passes from seller to buyer at a time and place specifically agreed

Table 1: Incoterms 2000

INCOTERM	DELIVERY	DOCUMENTS
1. EXW (Ex works, named place)	Seller's premises unloaded	Buyer's receipt or acceptable document
2. FCA (Free Carrier)	Carrier nominated or buyer	Evidence of delivery
3. FAS (Free Alongside Ship)	Alongside vessel	Alongside Receipt
4. FOB (Free On Board)	Over rail of vessel port of export	Clean on-board receipt
5. CFR (Cost and Freight)	Over rail of vessel port of export	Clean Bill of Lading
6. CIF (Cost, Insurance, Freight)	Over rail of vessel port of export	Clean Bill of Lading
7. CPT (Carriage Paid To)	First Carrier	Transport Document
8. CIP (Carriage, Insurance, Paid To)	First Carrier	Transport Document
9. DAF (Delivered at Frontier)	Place at disposal	Transport Document of buyer at frontier or warehouse warrant
10. DES (Delivered ex Ship)	Port of Destination aboard ship	Bill of Lading or delivery order
11. DEQ (Delivered ex Quay)	Port of Destination on dock	Bill of Lading or delivery order
12. DDU (Delivered Duty Unpaid)	Named Place of Destination	Delivery Document
13. DDP (Delivered Duty Paid)	Named Place of Destination	Delivery Document

From Jan Ramberg, *ICC Guide to Incoterms 2000, Understanding and Practical Use*, International Chamber of Commerce, 1999, pp. 39-171. It should be noted that in addition to the specific transport-related documents cited, the commercial invoice is a required document for each of the 13 terms.

upon by both parties, at the time of physical delivery of the goods at shipment or destination, at the time of physical delivery of the documents of title (normally a warehouse receipt or bill of lading), or at time of contracting. If the goods are rejected, title returns to the seller.

UN Convention on Contracts for the International Sale of Goods

The CISG treats the transactional aspect of a contract instead of the property aspects. There are no articles within the CISG that specifically treat the passing of title. Instead, it treats the elements of title transfer contained in the UCC and more—specif-

ically, the delivery of goods and handing over documents (Articles, 31, 53, 57, 60), payment and possession (Articles 59, 85), the right to reject the goods (Articles 39, 58, 86), and even the passing of risk (Article 67, 68, 69).

Of all the treatment of contractual components within the CISG, it appears that title relates directly to the international terms of sale used in the contract. The current international commercial terms are called incoterms. The current incoterms in use are found in the publication *Incoterms 2000*. Each of these terms defines the place of delivery and the obligations of the buyer with respect to costs and risks. *Incoterms 2000* clearly cautions the buyer and seller

that incoterms do *not* specifically deal with title, but with delivery, risks, and costs.

Incoterms and Title

While incoterms don't specifically treat title transfer, their focus on the delivery obligations of the seller also addresses components used in determining title transfer. Each of the 13 incoterms indicates specific delivery components and which documents are required, all of which can be used when determining title transfer, e.g., bills of lading, warehouse receipt, delivery receipts, etc. Table 1 shows a simple summary of the incoterms, where delivery takes place, and the documents required.

Assuming that the seller's obligation is completed at the delivery points included in the incoterms and/or the appropriate document of title is provided, title is likely to have transferred from the seller to the buyer at the point of delivery. At least, all risks and costs transfer at the point of delivery. Therefore, unless otherwise agreed to by the buyer and seller in the contract of sale, title passes at the point of delivery and/or the furnishing of documents. Unless otherwise stipulated, in a CIF sale connected to a documentary credit payment, for example, title would pass from the seller to the buyer when the seller presents to the bank an "order bill of lading" along with other documents stipulated in the credit. An "order bill of lading," like a bill of exchange, can be made out to the bearer of the bill of lading or to a particular person. So when the exporter presents documents required by the documentary credit to the bank for payment, the exporter is essentially turning over the goods by virtue of turning over the order bill, which is a negotiable bill of lading. The order bill demonstrates that the seller performed his/her obligation to deliver to the buyer by virtue of the goods crossing over the rail of the vessel at the port of shipment and so evidenced through the issuance of a clean bill of lading by the carrier.

Liability and Ownership

Since September 11, 2001, the U.S. has become more concerned about the potential link of terrorism and trade. The Patriot Act, the Trade Act of 2002, the Maritime Port Security Act of 2002, and the creation of the Department of Homeland Security and its Bureau of Customs and Border Protection, now called Customs and Border Protection (CBP),

demonstrate the concern for the potential threat imposed by inbound traffic to U.S. seaports and land ports. As a result, two major CBP programs, CIS (Container Security Initiative) and C-TPAT (Customs Trade Partnership Against Terrorism), were launched to control inbound shipments better and fix liability should they be linked to terrorism.

Importers clearly must ask themselves where they should take responsibility for and ownership of imported products. If the importer buys a container load of goods CIF, the importer is likely to become the owner of the goods as they cross the ship's rail in the foreign port. The U.S. importer is then accepting any risk that container may pose (by having illicit contents) along with its legal contents. Should the U.S. importer instead buy the goods on a DDU or DDP incoterm, where the foreign seller takes responsibility and ownership of the contents of the container all the way through the U.S. port to the point of destination within the States? Or is it better for the

U.S. importer to buy EXW? If so, possession of the goods is taken as they sit unloaded in the foreign nation, and the importer accepts the responsibility to load them into the container and clear outbound foreign Customs and inbound U.S. Customs.

Each incoterm may pose a new dilemma for the U.S. importer. Each term also offers U.S. importers the role they want to assume in the international transaction, what risk and responsibility they want with respect to the control of the container, and their obligations under U.S. law and CBP programs. ■

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