

Incoterms Fundamentals

What does INCOTERM stand for ?

- Def : The word INCOTERM is an abbreviation for **International Commercial Terms** which provide a common set of rules used for defining the responsibilities of sellers and buyers in the delivery of goods under sales contracts.
- They are widely used in international commercial transactions.

Why are they important?

- Set international rules for commonly used terms in foreign trade
- Define obligations of both parties involved in the transaction
- Determine the distribution & transfer of risks regarding the goods delivered from seller to buyer
- State the clear sharing of expenses between the parties during transport

When and where did they appear ?

- First conceived by International Chamber of Commerce (ICC) in 1921 and implemented starting from 1936, since they have been updated 6 times in order to keep pace with the evolution of international trade.
- In 1923, a Trade Terms Committee developed the first 6 rules : FOB, FAS, FOT, FOR, Free Delivered CIF and C&F, as the precursor for what would later be known as INCOTERM rules.

Revising the INCOTERMS

- In order to keep up with the continuous evolution of commercial practices, types of goods and transport and international law, INCOTERMS need to be regularly updated by specialized experts.
- Some significant revisions :
- 1980 - FCA was introduced, for dealing with cases where the reception point was no longer the ship's rail, but a point on land where goods were stored in a container
- 1990 - the seller was permitted to provide the proof of delivery electronically by EDI-messages instead of paper documentation
- 2000 - export clearance and other formalities under FAS are placed on the seller (previously buyer) - in FCA, it became the seller's obligation to load the goods on the buyer's vehicle or the buyer's obligation to receive the seller's arriving vehicle unloaded

Revising the INCOTERMS

Updated every 10 years

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- 2010 –
- reduction from 13 to 11 terms by replacing 4 delivery terms : DEQ, DAF, DES, DDU with 2 new ones : DAT(Delivery at Terminal) and DAP(Delivery at Place)
- terms grouped in 2 categories, according to the means of transport used :
 - General all types of transport & Special sea & inland waterway

Incoterms (2 categories)

General all types of transport

EXW • FCA • CPT • CIP • DAT •
DAP • DDP

Special sea & inland waterway

FAS • FOB • CFR • CIF

General INCOTERMS

EXW (Ex Works)

Seller

- delivers goods at their own premises (factory/warehouse)
- minimal obligations, risks & costs

Buyer

- responsible for loading goods onto carrier and all other transport cost, duties and insurance
- clearance of goods for export
- bears the whole risk on their own

Minimal costs & risks for exporter

FCA (Free Carrier)

Seller

- completes and bears costs of export clearance and obtaining necessary documents
- delivers goods at agreed place to carrier
- liable for the load if delivery is made on his premises

Buyer

- import clearance formalities
- responsible for unload if delivery occurs in a facility or transport infrastructure

CPT (Carriage Paid To)

Seller

- contracts and pays transport to the buyer's country delivery place
- completes formalities and bears export customs clearance costs
- risk of transport is transferred when the goods are delivered to the first carrier in the seller's country

Buyer

- supports transport costs starting from the moment goods have reached the place of delivery in his country
- import clearance costs and formalities
- supports the transport risk since the goods have been delivered to 1st carrier and the insurance for international transport

CIP (Carriage and Insurance Paid To)

Seller

- bears the same costs and obligations as in case of CPT
- the obligation of hiring insurance to cover the buyer's risk during international transport
- contracts the insurance and pays the premium

Buyer

- beneficiary of the insurance paid by the seller
- must take into account that the buyer is obliged only to a minimum coverage insurance
- needs to agree with the seller to hire additional insurance if he wants a larger coverage

DAT (Delivery at Terminal)

Seller

- delivers goods unloaded at a port terminal or another place of destination in the buyer's country
- complete the formalities and bear costs of customs clearance for export
- transport risk passes to the buyer at the time of delivery to destination country

Buyer

- import customs clearance and tariffs paid
- clearly mention the specific point chosen for delivery

DAP (Delivery at Place)

Seller

- delivers goods ready for unloading in the country of destination, in a place other than a transport terminal, such as the buyer's premises or a place nearby
- risk is transferred to buyer in the same place where goods are delivered
- complete formalities and bear export clearance costs

Buyer

- pays the costs of import clearance customs
- useful for sales between countries of same economic area (EU) as there are no import customs

DDP (Delivery Duty Paid)

Seller

- delivers goods ready for unloading in the country of destination, usually at buyer's premises
- all costs and risks borne by seller
- customs clearance of export and import also covered by seller
- any import tax, including VAT are paid by the seller

Buyer

- only cost he assumes is the unloading of goods at delivery place
- if the parties agree in the contract of sale, the VAT or other taxes can be paid by the buyer, in what is known as a variant of DDP, called 'DDP VAT unpaid'

Sea INCOTERMS

FAS (Free Alongside Ship)

Seller

- delivers the goods placing them alongside the ship chosen by the buyer
- export clearance must be covered by the seller

Buyer

- responsible for loading the goods on the ship
- must have very good knowledge of the practices in the port of shipment

only used for certain commodities and materials that are not packed and cannot be individualized (grain, timber, minerals, etc.)

FOB (Free on Board)

Seller

- delivers goods by placing them on board of the ship named by the buyer
- covers the terminal costs and export clearance

Buyer

- assumes the transportation risk after the goods have been delivered on board of the ship

- oldest Incoterm and one of the most widely used
- preferably used with bulk, heavy loads and in case of complex goods (machinery) whose loading involves certain risks

CFR (Cost and Freight)

Seller

- delivers the goods on board of a ship but he also pays the cost of freight to the destination point
- covers terminal cost and export clearance
- the risk is transferred to the buyer after the goods had reached the board of the ship

Buyer

- must hire an insurance for transport from the port of shipment to the destination, as the seller is not obliged to do this

- used mainly for large volumes of general cargo

CIF (Cost, Insurance and Freight)

Seller

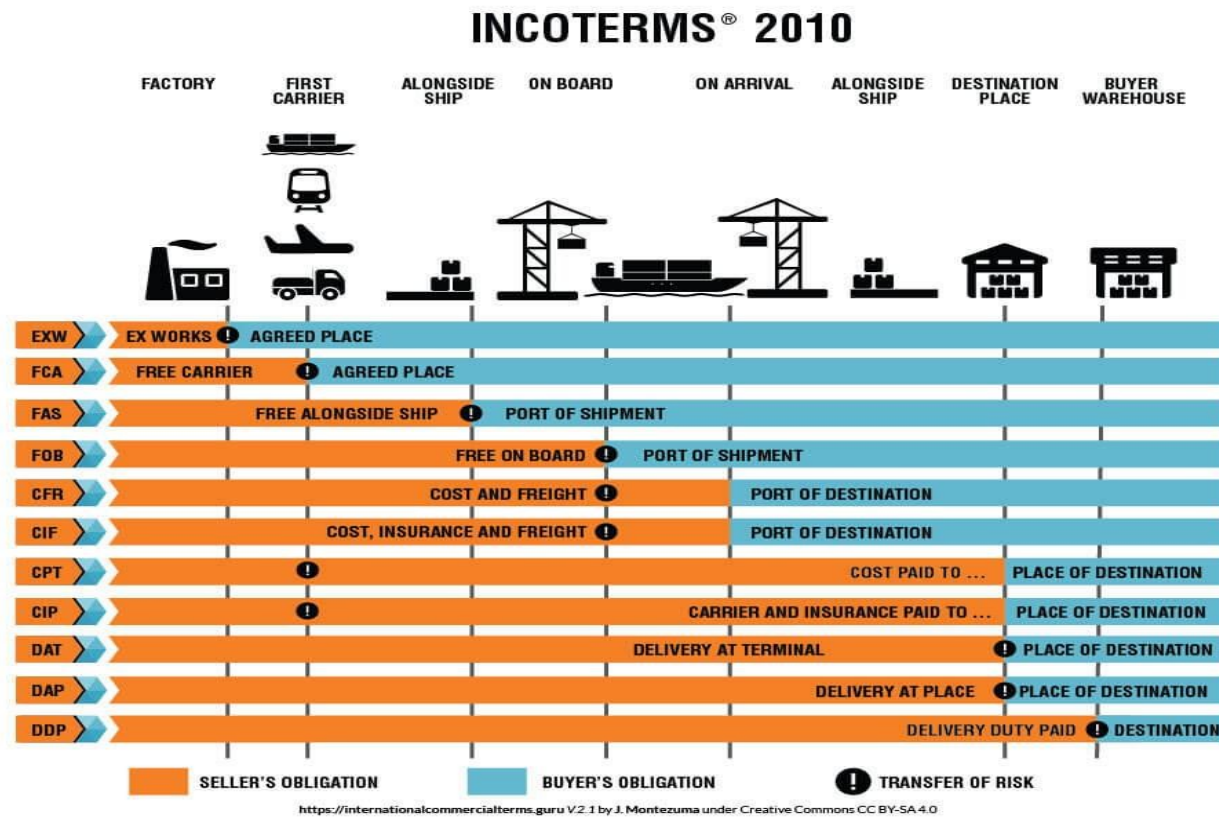
- same obligations that CFR implies
- seller is obliged to hire insurance for transport covering at least the way from the port of shipping to the port of destination
- insurance shall cover the price of the contract + 10%

Buyer

- might want to hire additional insurance, as the seller is only obliged to purchase a minimum coverage insurance

- used for general cargo of consumer or industrial products of high value CIF value is used in most of the customs to apply tariffs and import taxes, facilitating the clearance of goods for export

Graphic Representation of Incoterm Liability



Using INCOTERMS correctly

- Following the three letters of the appropriate chose term with the exact destination place to which the delivery of goods is to be made, and afterwards the expression 'Incoterms 2010'
- FCA Port of Savannah, USA, Incoterms 2010
- CIP Tianjin airport, China, Incoterms 2010