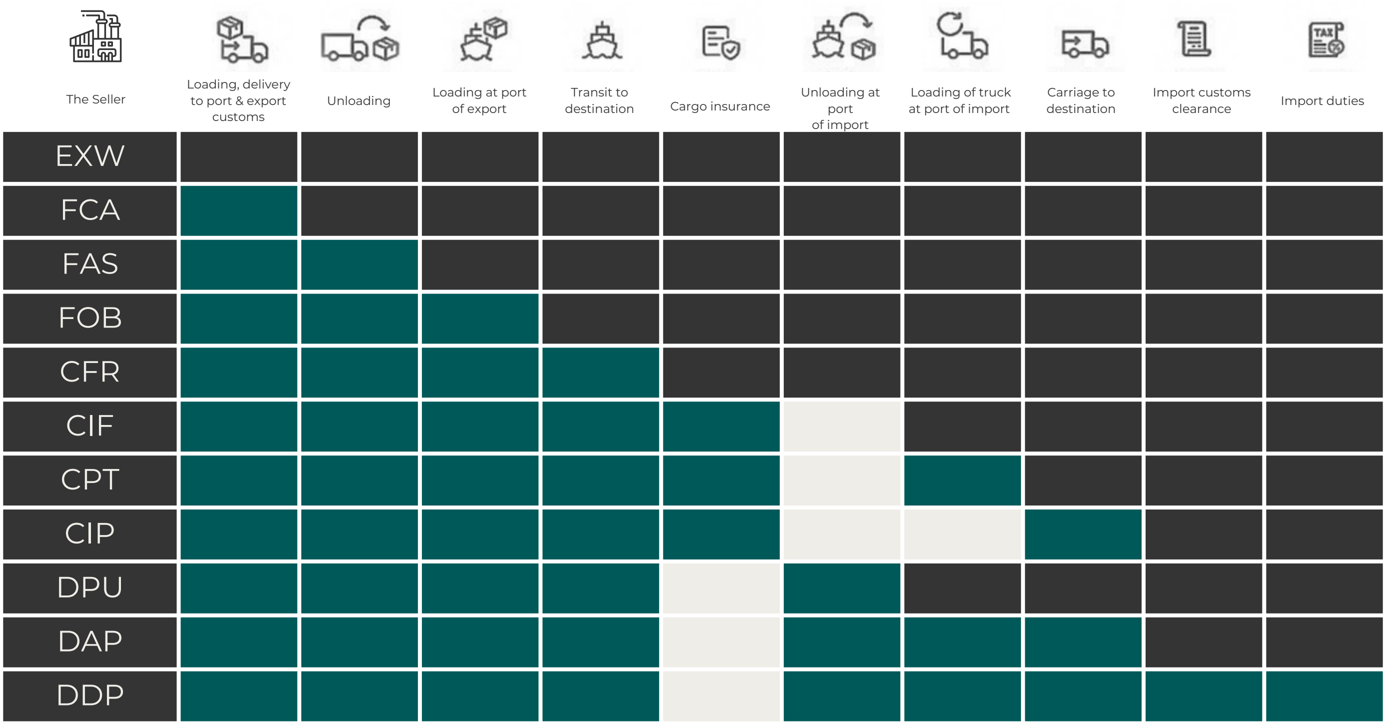
INCOTERMS

Incoterms (International Commercial Terms) are universally recognised rules that guide buyers and sellers to fulfil a contract for the shipment of goods.

The International Chamber of Commerce (ICC) introduced the new rules in effect from 1 January 2020.

A careful study of INCOTERMS 2020 will repay the effort by enabling more favourable trade terms for effective trade finance.



Seller's Obligation

Buyer's Obligation

Negotiable

Group E: Most costs and risks are the responsibility of the buyer.

Group F: The costs and the risks of the main transport are the responsibility of the buyer.

Group C: The seller is responsible for all the risks and costs of the main transport.

Group D: The seller is responsible for all costs and risks until the arrival of the goods at the final destination.

ESW	Ex Works
FCA	Free Carrier
FAS	Free Alongside Ship
FOB	Free On Board
CFR	Cost And Freight
CIF	Cost, Insurance and Freight
CPT	Carriage Paid To
CIP	Carriage Insurance Paid To
DAT	Delivered at Terminal
DAP	Delivered At Place
DDP	Delivered Duty Paid

OVERVIEW

An Incoterm (International Commercial Term) is a set of rules that helps buyers and sellers determine who will be responsible for expenses such as transportation, insurance, and import/export fees when buying or selling something internationally. This standard helps to avoid misunderstandings and disputes between buyers and sellers.

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Incoterms are a widely-used set of 11 internationally recognized rules that define the responsibilities of sellers and buyers in international trade. These rules specify who is responsible for paying and managing the shipment, insurance, documentation, customs clearance, and other logistical activities.

RULE BREAKDOWN

The latest Incoterms 2020 has 11 different rules. Seven of them can be applied for any type of transport, while the remaining four are reserved for shipment by boat, whether on rivers or sea. Here are they, starting with the universal ones:

EXW – Ex Works

The seller only needs to have the goods ready for pickup. It is the buyer's job to load them onto the vehicle and take care of the rest of the transport. Once the goods are out of the seller's premises, they are no longer his concern.

FCA – Free Carrier

In the case of export, the seller will deliver the goods to the port (for sea transport) or the cargo terminal (in case of air freight), and do the export clearance. From there it is the buyer's job to take care of international transport and import into the destination country.

If it is domestic transport the seller only needs to load the goods on the buyer's vehicle. The buyer needs to organize transport.

CPT – Carriage Paid to

Here it is the seller who arranges transport. The seller as well takes care of the paperwork needed for export. But the risk of loss, theft or damage is with the buyer during the transportation. While in domestic transport this may not be an issue, it is not the best choice for shipping.

CIP – Carriage and Insurance Paid To

The significant difference between CPT and CIP is that the seller now bears also insurance costs for the cargo until the final destination of the goods.

DAP – Delivered at Place

If this Incoterm is agreed upon, the responsibilities of the buyer are to pay for the customs clearance and duties in the country of import. Furthermore, he needs to arrange to unload goods at the point of destination. Everything else is done by the seller.

DPU – Delivered at Place Unloaded

All customs formalities at destination would be the buyer's responsibility. Here the seller is responsible for unloading of the goods at the place specified by the buyer. The logistics of the goods movement is completely run by the seller.

DDP – Delivered Duty Paid

The seller takes care of everything. Import/export documentation and fees, transportation, unloading. The buyer has no obligations whatsoever until the goods are on his premises. In some countries it is not legally possible that the seller does the import, so check it out before signing the contract. As you may pay for the customs clearance twice, to the seller and then the customs office.

GAP Merchant Recycling

Marine transport is a bit more complicated compared to land or air transport. Therefore, we have a couple more specific Incoterms for this kind of transport. Also, all Incoterms for marine transport talk in more detail about export and import duties. As it is by default international transport.

THE INCOTERMS RELATED TO MARINE TRANSPORT

FAS – Free Alongside Ship
The seller should clear the export documentation and deliver the goods to the port, ready to be loaded onto the ship. From there the buyer takes over. The buyer will hire the shipment, arrange to load and import the goods. This term is used mostly for non-containerized shipments, like sand, oil etc.
FOB – Free on Board
Here the seller must assure the goods are loaded onto the ship nominated by the buyer. So, besides the export clearance, he still bears the risk of damage while the goods are in the port. Once the goods are safely stored on the ship, the buyer is the one responsible for all risk.
CFR – Cost and Freight
Moving forward, now the seller takes care of sea transport. Once the ship reaches the final destination, it becomes the responsibility of the buyer. The buyer needs to arrange to unload at the port, pay customs fees and arrange documents and transport to the final destination.
CIF – Cost Insurance and Freight
This is quite similar to CFR. The main difference is that the seller must arrange insurance for the goods to cover all risks until the final port of destination.

MAIN DIFFERENCES SPECIFIC TO A COUNTRY

The above advice covers most countries in most circumstances. But there are some factors to keep in mind when choosing an incoterm with your supplier:

- Customs procedures are much more relaxed at porous borders, like within the EU
- Different countries require different procedures and paperwork for shipments: the US requires
- Customs Bond, importing into the UK requires a Deferment Account, and exporting from India includes a withholding tax.

WHEN TO CHALLENGE ADVICE

Some freight forwarders prefer only using a favored set of incoterms because they “seem to work.” Therefore don’t be surprised if some forwarders push back on your selection of incoterm, despite it being the most appropriate incoterm for your shipment.

WHAT SHIPPING INCOTERMS DON’T COVER

Incoterms do not cover property rights, possible force majeure situations and breach of contract. Include of these within the contract of sale. Similarly, all incoterms except the C terms do not assign responsibility for arranging insurance. Cargo insurance is, therefore, a separate cost for buyers.

DEFINE NAMED PLACE IN THE SALES CONTRACT

When the incoterm is written in the sales contract, the named place should immediately follow the three letter incoterm abbreviation, e.g. “FCA Shenzen Yantian CFS.” Be precise when defining the location, especially with larger cities that may have several terminals, and with larger terminals that may have several drop-off points. You can use this global port finder to find specific port codes.

HOW LETTERS OF CREDIT LIMIT CHOICE OF INCOTERM

If the sale is being completed with a letter of credit or documentary credit, the chain that releases funds begins with the seller providing several documents to the bank, including the bill of lading/air waybill. Letters of credit are used where there is limited trust between the seller and the buyer. That rules out EXW, because the supplier will be paid before pickup. F terms require trust because if the buyer cancels the international transit, the supplier won’t have a bill of lading to present to the bank. D terms require trust because the seller is bearing all of the transport costs. That leaves the four C terms as the best options to use with a letter of credit.