

# Incoterms®

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## International Commercial Terms or INCOTERMS®

International business brings along some additional complexity in terms of costs and risk. Who is responsible for the costs of handling and transport of goods, and who covers the risk? There are many possible combinations, and uncertainty may be the result. The correct terms have to be used in the contract between seller and buyer, where a small difference in wording can have a huge impact on the result of a transaction. To overcome this problem the International Chamber of Commerce (ICC) created a set of rules that define the **International Commercial Terms** or **INCOTERMS®** in 1936. ICC is the world business organization, helping businesses of all sizes and in all countries to operate both internationally and responsibly. Incoterms® are a set of predefined commercial terms and act as a uniform language to be used by businesses in order to define the agreements in international sales transactions. They are regularly updated. The eighth version – Incoterms® 2010 – has been published in 2011. Currently there are consultation rounds organised by International Chambers of Commerce in many countries for the revision of the INCOTERMS®, preparing for Incoterms® 2020.

The credit manager has to be aware of all the risks of the commercial transaction, allowing him to supervise risk management in the relations with the customers. This means that he has to know the existence of the INCOTERMS® and he must also know where to find the correct information in order to make sure that whatever the problem that may occur the consequences and responsibilities are identified, and no unexpected risks occur..

Incoterms® are widely used in International commercial transactions or procurement processes. A series of three-letter trade terms related to common contractual sales practices, the Incoterms® rules are intended primarily to clearly communicate the tasks, costs, and risks associated with the transportation and delivery of goods.

The Incoterms® rules are also accepted by governments, legal authorities, and practitioners worldwide for the interpretation of most commonly used terms in international trade.

The rules are identified by a 3 letter code. They basically identify who is responsible for the expenses involved in a shipment, the control and ownership of the goods and the liability for potential damages to the goods. They also deal with the documentation required for global trade, also specifying which party is responsible for which documents.

## Incoterms® 2010

Incoterms® 2010 has 11 pre-defined terms that can be subdivided into two categories based on the method of delivery.

The larger group of seven rules may be used regardless of the method of transport. The other four rules are applicable only to sales that solely involve transportation by water where the condition of the goods can be verified at the point of loading on board of the ship. They are therefore not to be used for containerized freight, other combined transport methods, or for transport by road, air or rail.

The definitions given below contain *the official short descriptions of INCOTERMS® 2010* available on the ICC website. These should be read in the context of the full official text of the rules which can be obtained from the [ICC Store](#).

INCOTERMS® are copyright protected. Information is based on the following source: [ICC website](#).

In the text the extracts of the official definition are shown in *italic*. The full text of the 2010 edition of the Incoterms rules is available at <http://store.iccwbo.org/>.

### Rules for any mode of transport

#### EXW – Ex Works (named place of delivery)

*“Ex Works” means that the seller delivers when it places the goods at the disposal of the buyer at the seller’s premises or at another named place (i.e., works, factory, warehouse, etc.). The seller does not need to load the goods on any collecting vehicle, nor does it need to clear the goods for export, where such clearance is applicable.*

Probably the most simple and basic shipment arrangement. It is usually followed by a named place of delivery, i.e. the seller’s premises, or any other named place. The seller makes the goods available for pickup at this named place. This term places the maximum obligation on the buyer and minimum responsibility on the seller. The Ex Works term can also be useful when making an initial quotation for the sale of goods without any costs included.

EXW means that the buyer has the responsibility and incurs the risks for bringing the goods to their final destination. The seller has no obligation to make a contract of carriage.

The buyer is also responsible for completing all the export documentation, although the seller does have an obligation to obtain information and documents at the buyer's request and cost.

These documentary requirements may result in issues with the export declaration in certain jurisdictions where the customs regulations require the declarant to be either an individual or corporation resident within the jurisdiction.

### **FCA – Free Carrier (named place of delivery)**

*“Free Carrier” means that the seller delivers the goods to the carrier or another person nominated by the buyer at the seller’s premises or another named place. The parties are well advised to specify as clearly as possible the point within the named place of delivery, as the risk passes to the buyer at that point.*

This INCOTERM® is followed by a named place.

The seller delivers the goods, cleared for export, at a named place (possibly his own premises). The goods can be delivered to a carrier or to another party nominated by the buyer.

In many respects this Incoterm® has replaced FOB in modern usage. The critical point at which the risk passes moves from loading aboard the vessel to the named place. The chosen place of delivery may also affect the obligations of loading and unloading the goods at that place. In the case that delivery is at a location that is under the seller's control (e.g. the seller’s premises), it is the seller who is in charge of loading the goods on to the buyer's carrier. If delivery occurs at any other place, the seller’s responsibility stops when the goods have arrived at the named place; it is now the buyer who is responsible for unloading the goods and loading them onto it’s own carrier.

### **CPT – Carriage Paid To (named place of destination)**

*“Carriage Paid To” means that the seller delivers the goods to the carrier or another person nominated by the seller at an agreed place (if any such place is agreed between parties) and that the seller must contract for and pay the costs of carriage necessary to bring the goods to the named place of destination.*

In this case it is the seller who pays for the carriage of the goods up to the named place of destination.

The delivery of the goods occurs when the goods have been handed over to the first or main carrier. This implies that the risk transfers to the buyer upon handing the goods over to that carrier at the place of shipment in the country of Export.

## **CIP – Carriage and Insurance Paid to (named place of destination)**

*“Carriage and Insurance Paid to” means that the seller delivers the goods to the carrier or another person nominated by the seller at an agreed place (if any such place is agreed between parties) and that the seller must contract for and pay the costs of carriage necessary to bring the goods to the named place of destination.*

*‘The seller also contracts for insurance cover against the buyer’s risk of loss of or damage to the goods during the carriage. The buyer should note that under CIP the seller is required to obtain insurance only on minimum cover. Should the buyer wish to have more insurance protection, it will need either to agree as much expressly with the seller or to make its own extra insurance arrangements.’*

This term is similar to the CPT term, but in this case the seller is required to obtain insurance for the goods while in transit.

## **DAT – Delivered At Terminal (named terminal at port or place of destination)**

*“Delivered at Terminal” means that the seller delivers when the goods, once unloaded from the arriving means of transport, are placed at the disposal of the buyer at a named terminal at the named port or place of destination. “Terminal” includes a place, whether covered or not, such as a quay, warehouse, container yard or road, rail or air cargo terminal. The seller bears all risks involved in bringing the goods to and unloading them at the terminal at the named port or place of destination.*

The seller delivers the goods, unloaded, at the named terminal. Since delivery occurs when the goods are unloaded, it is the seller who has to cover all the costs of transport (export fees, carriage, unloading from main carrier at destination port and destination port charges). The seller also carries all risk until delivery occurs.

## **DAP – Delivered At Place (named place of destination)**

*“Delivered at Place” means that the seller delivers when the goods are placed at the disposal of the buyer on the arriving means of transport ready for unloading at the named place of destination. The seller bears all risks involved in bringing the goods to the named place.*

The seller delivers the goods to the named place. Legal formalities in the exporting country are completed by the seller at his own cost and risk.

After arrival of the goods in the country of destination, the customs clearance in the importing country needs to be completed by the buyer at his own cost and risk, including all customs duties and taxes.

## **DDP – Delivered Duty Paid (named place of destination)**

*“Delivered Duty Paid” means that the seller delivers the goods when the goods are placed at the disposal of the buyer, cleared for import on the arriving means of transport ready for unloading at the named place of destination. The seller bears all the costs and risks involved in bringing the goods to the place of destination and has an obligation to clear the goods not only for export but also for import, to pay any duty for both export and import and to carry out all customs formalities.*

The seller is responsible for delivering the goods to the named place in the country of the buyer, and pays all costs in bringing the goods to the destination including import duties and taxes. The seller is not responsible for unloading.

## **Rules for sea and inland waterway transport**

To determine if a location qualifies for these four rules, please refer to 'United Nations Code for Trade and Transport Locations (UN/LOCODE)'.

These four rules defined by Incoterms® 2010 are applicable for international trade where transportation is entirely conducted by water. It is important to note that these terms are generally not suitable for shipments in shipping containers.

## **FAS – Free Alongside Ship (named port of shipment)**

*“Free Alongside Ship” means that the seller delivers when the goods are placed alongside the vessel (e.g., on a quay or a barge) nominated by the buyer at the named port of shipment. The risk of loss of or damage to the goods passes when the goods are alongside the ship, and the buyer bears all costs from that moment onwards.*

Unless parties have explicitly agreed differently the FAS term requires the seller to clear the goods for export.

## **FOB – Free on Board (named port of shipment)**

*“Free On Board” means that the seller delivers the goods on board the vessel nominated by the buyer at the named port of shipment or procures the goods already so delivered. The risk of loss of or damage to the goods passes when the goods are on board the vessel, and the buyer bears all costs from that moment onwards.*

The seller bears all costs and risks up to the point the goods are loaded on board the vessel. FOB should only be used for non-containerised sea freight and inland waterway transport. For other modes of transport the FCA term should be used.

## **CFR – Cost and Freight (named port of destination)**

*“Cost and Freight” means that the seller delivers the goods on board the vessel or procures the goods already so delivered. The risk of loss of or damage to the goods passes when the goods are on board the vessel. the seller must contract for and pay the costs and freight necessary to bring the goods to the named port of destination.*

CFR should only be used for non-containerized sea freight and inland waterway transport; for all other modes of transport the CPT term should be used.

## **CIF – Cost, Insurance & Freight (named port of destination)**

*“Cost, Insurance and Freight” means that the seller delivers the goods on board the vessel or procures the goods already so delivered. The risk of loss of or damage to the goods passes when the goods are on board the vessel. The seller must contract for and pay the costs and freight necessary to bring the goods to the named port of destination. ‘The seller also contracts for insurance cover against the buyer’s risk of loss of or damage to the goods during the carriage. The buyer should note that under CIF the seller is required to obtain insurance only on minimum cover. Should the buyer wish to have more insurance protection, it will need either to agree as much expressly with the seller or to make its own extra insurance arrangements.”*

## Using INCOTERMS®

The definition of the different INCOTERMS® makes clear that they are not only very important, but also that their application can be complicated.

When the buyer is not known to the seller, and there is no information on his reliability available one should be very careful. Also when the destination country does not have a strong and reliable judicial system extra care is necessary.

Incoterms® do not give a clear answer to :

- The many questions around transfer of title (ownership)
- In relation with the forwarder or transport company
- Relation with the insurance company
- Payment terms
- Applicable law

So it may be recommended to consult specialists in order to avoid unnecessary risks. The bank you are working with to handle your payments for import or export and your local Chamber of Commerce can certainly help you with more information.

As mentioned above Incoterms® 2010 is a trade mark registered by ICC.

“Source: [ICC website](#). The full text of the 2010 edition of the Incoterms rules is available at <http://store.iccwbo.org/>.