

Introduction to Incoterms 2000

While the terms of sale in international business often sound similar to those commonly used in domestic contracts, they often have different meanings. Confusion over these terms can result in a lost sale or a financial loss on a sale. Thus, it is essential that you understand what terms you are agreeing to before you finalize a contract.

Incoterms 2000

By the 1920s, commercial traders had developed a set of trade terms to describe their rights and liabilities with regard to the sale and transport of goods. These trade terms consisted of short abbreviations for lengthy contract provisions. Unfortunately, there was no uniform interpretation of them in all countries, and therefore misunderstandings often arose in cross-border transactions.

To improve this aspect of international trade, the International Chamber of Commerce (ICC) in Paris developed INCOTERMS (International Commercial TERMS), a set of uniform rules for the interpretation of international commercial terms defining the costs, risks, and obligations of buyers and sellers in international transactions. First published in 1936, these rules have been periodically revised to account for changing modes of transport and document delivery. The current version is Incoterms 2000.

Use of Incoterms

Incoterms are not implied into contracts for the sale of goods. If you desire to use Incoterms, you must specifically include them in your contract. Further, your contract should expressly refer to the rules of interpretation as defined in the latest revision of Incoterms, for example, *Incoterms 2000*, and you should ensure the proper application of the terms by additional contract provisions. Also, Incoterms are not "laws." In case of a dispute, courts and arbitrators will look at: 1) the sales contract, 2) who has possession of the goods, and 3) what payment, if any, has been made. See *International Contracts*, also by World Trade Press.

Illustrated Guide to Incoterms

This guide was designed to give a graphic representation of the buyer's and seller's risks and costs under each Incoterm. The material on each facing page gives a summary of seller and buyer responsibilities.

Incoterms Do . . .

Incoterms 2000 may be included in a sales contract if the parties desire the following:

1. To complete a sale of goods.
2. To indicate each contracting party's costs, risks, and obligations with regard to delivery of the goods as follows:
 - a. When is the delivery completed?
 - b. How does a party ensure that the other party has met that standard of conduct?
 - c. Which party must comply with requisite licenses and government-imposed formalities?
 - d. What are the mode and terms of carriage?
 - e. What are the delivery terms and what is required as proof of delivery?
 - f. When is the risk of loss transferred from the seller to the buyer?
 - g. How will transport costs be divided between the parties?
 - h. What notices are the parties required to give to each other regarding the transport and transfer of the goods?
3. To establish basic terms of transport and delivery in a short format.

Incoterms Do Not . . .

Incoterms 2000 are not sufficient on their own to express the full intent of the parties. They will not:

1. Apply to contracts for services.
2. Define contractual rights and obligations other than for delivery.
3. Specify details of the transfer, transport, and delivery of the goods.
4. Determine how title to the goods will be transferred.
5. Protect a party from his/her own risk of loss.
6. Cover the goods before or after delivery.
7. Define the remedies for breach of contract.

Tip: Incoterms can be quite useful, but their use has limitations. If you use them incorrectly, your contract may be ambiguous, if not impossible to perform. It is therefore important to understand the scope and purpose of Incoterms—when and why you might use them—before you rely on them to define such important terms as mode of delivery, customs clearance, passage of title, and transfer of risk.

Organization of Incoterms

Incoterms are grouped into four categories:

1. The "E" term (EXW)-The only term where the seller/exporter makes the goods available at his or her own premises to the buyer/importer.
2. The "F" terms (FCA, FAS and FOB)-Terms where the seller/exporter is responsible to deliver the goods to a carrier named by the buyer.
3. The "C" terms (CFR, CIF, CPT and CIP)-Terms where the seller/exporter/manufacturer is responsible for contracting and paying for carriage of the goods, but not responsible for additional costs or risk of loss or damage to the goods once they have been shipped. C terms evidence "shipment" (as opposed to "arrival") contracts.
4. The "D" terms (DAF, DES, DEQ, DDU and DDP)-Terms where the seller/exporter/manufacturer is responsible for all costs and risks associated with bringing the goods to the place of destination. D terms evidence "arrival" contracts.

The following table sets out these categories.

<u>Incoterms 2000</u>		
Group E Departure	EXW	Ex Works (...named place)
Group F Main Carriage Unpaid	FCA	Free Carrier (...named place)
	FAS	Free Alongside Ship (...named port of shipment)

	FOB	Free On Board (...named port of shipment)
Group C Main Carriage Paid	CFR	Cost and Freight (...named port of destination)
	CIF	Cost, Insurance and Freight (...named port of destination)
	CPT	Carriage Paid To (...named port of destination)
	CIP	Carriage and Insurance Paid To (...named port of destination)
	DAF	Delivered at Frontier (a named place)
Group D Arrival	DES	Delivered Ex Ship (...named port of destination)
	DEQ	Delivered Ex Quay (...named port of destination)
	DDU	Delivered Duty Unpaid (...named port of destination)
	DDP	Delivered Duty Paid (...named port of destination)

Mode of Transport

Not all Incoterms are appropriate for all modes of transport. Some terms were designed with sea vessels in mind while others were designed to be applicable to all modes. The following table sets out which terms are appropriate for each mode of transport.

<u>Incoterms 2000</u>		
All modes of transport including multimodal	EXW	Ex Works (...named place)
	FCA	Free Carrier (...named place)
	CPT	Carriage Paid To (...named port of destination)
	CIP	Carriage and Insurance Paid To (...named port of destination)
	DAF	Delivered at Frontier (...named place)
	DDU	Delivered Duty Unpaid
	DDP	Delivered Duty Paid
Sea and inland waterway transport	FAS	Free Alongside Ship (...named port of shipment)
	FOB	Free On Board

	(...named port of shipment)
CFR	Cost and Freight (...named port of destination)
CIF	Cost, Insurance and Freight (...named port of destination)
DES	Delivered Ex Ship (...named port of destination)
DEQ	Delivered Ex Quay (...named port of destination)

Helpful Definitions

Pre-carriage—The initial transport of goods from the seller's premises to the main port of shipment. Usually by truck, rail or on inland waterways.

Main carriage—The primary transport of goods, generally for the longest part of the journey and generally from one country to another. Usually by sea vessel or by airplane, but can be by truck or rail as well.

On-carriage—Transport from the port of arrival in the country of destination to the buyer's premises. Usually by truck, rail or on inland waterways.

[return to top](#)

Notes on Incoterms

1. **Underlying Contract**—Incoterms were designed to be used within the context of a written contract for the sale of goods. Incoterms, therefore, refer to the contract of sale, rather than the contract of carriage of the goods. Buyers and sellers should specify that their contract be governed by Incoterms 2000.
2. **EXW and FCA**—If you buy Ex Works or Free Carrier you will need to arrange for the contract of carriage. Also, since the shipper will not receive a bill of lading, using a letter of credit requiring a bill of lading will not be possible.
3. **EDI: Electronic Data Interchange**—It is increasingly common for sellers to prepare and transmit documents electronically. Incoterms provides for EDI so long as buyers and sellers agree on their use in the sales contract.
4. **Insurable Interest**—Note that in many cases either the buyer or the seller is not *obligated* to provide insurance. In a number of cases neither party is obligated to provide insurance. However, both the seller and buyer should be aware that they may have insurable interest in the goods and prudence dictates purchase of insurance coverage.
5. **Customs of the Port or Trade**—Incoterms are an attempt to standardize trade terms for all nations and all trades. However, different ports and different trades have their own customs and practices. It is best if specific customs and practices are specified in the sales contract.
6. **Precise Point of Delivery**—In some cases it may not be possible for the buyer to name the precise point of delivery at contract. However, if the buyer does not do so in a timely manner, it may give the seller the option to make delivery within a range of places that is within the terms of the contract. For example, the original terms of sale may state CFR Port of Rotterdam. The Port of Rotterdam is huge and the buyer may find that a particular point within the port is best and should so state in the sales contract and in the trade term. Also, since the buyer becomes liable for the goods once they arrive, he or she may be responsible for unloading, storage and other charges once the goods have been made available at the place named.
7. **Export and Import Customs Clearance**—It is usually desirable that export customs

- formalities be handled by the seller and import customs formalities be handled by the buyer. However, some trade terms require that the buyer handle export formalities and others require that the seller handle import formalities. In each case the buyer and seller will have to assume risk from export and import restrictions and prohibitions. In some cases foreign exporters may not be able to obtain import licenses in the country of import. This should be researched before accepting final terms.
8. **Added Wording**—It is possible, and in many cases desirable, that the seller and buyer agree to additional wording to an Incoterm. For example, if the seller agrees to DDP terms, agreeing to pay for customs formalities and import duties, but not for VAT (Value Added Taxes) the term “DDP VAT Unpaid” may be used.
 9. **Packing**—It is the responsibility of the seller to provide packaging unless the goods shipped are customarily shipped in bulk (usually commodities such as oil or grain). In most situations it is best if the buyer and seller agree in the sales contract on the type and extent of packing required. However, it may not be possible to know beforehand the type or duration of transport. As a result, it is the responsibility of the seller to provide for safe and appropriate packaging, but only to the extent that the buyer has made the circumstances of the transport known to the seller beforehand.
If the seller is responsible for packing goods in an ocean or air freight container it is also his responsibility to pack the container properly to withstand shipment.
 10. **Inspection**—These are several issues related to inspections: a) the seller is responsible for costs of inspection to make certain the quantity and quality of the shipment is in conformity with the sales contract, b) pre-shipment inspections as required by the export authority are the responsibility of the party responsible for export formalities, c) import inspections as required by the import authority are the responsibility of the party responsible for import formalities, and d) third-party inspections for independent verification of quality and quantity (if required) are generally the responsibility of the buyer. The buyer may require such an inspection and inspection document as a condition of payment.
 11. **Passing of Risks and Costs**—The general rule is that risks and costs pass from the seller to the buyer once the buyer has delivered the goods to the point and place named in the trade term.