



Incoterms

International commercial terms of sale that assign costs and responsibilities between the buyer and seller.



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Incoterms 2020 explained

What are Incoterms?

Incoterms are international commercial terms of sale that assign costs and responsibilities between the buyer and seller when importing/exporting products. Incoterms are set by the International Chamber of Commerce (ICC) to provide a uniform interpretation of common contract clauses in international trade.

Incoterms define the role of both the buyer and seller as to who must undertake which part of the physical movement of inventory, who provides what documentation, and who is responsible for risk and the insurance to mitigate this risk. Incoterms use a three-letter trade term, e.g. FOB, followed by a place where the buyer and seller responsibilities transfer. More about this below.

The origin of Incoterms

Incoterms were first created in 1936. Since then, Incoterms have evolved into a codified worldwide contractual standard although it is not compulsory to use them. They are updated as international trade changes and evolves. Incoterms are updated every ten years. Incoterms® 2020 comprises the latest revisions including references to security, use of own transport and the seller/buyer relationship.



Differences in trading practices and legal interpretations between traders of different countries necessitate a need for a common set of rules. These rules need to be easy to understand by all of the participants in order to prevent conflict and litigation.

Why do we use Incoterms in contracts?

Buyers need to consider incoterms before the contract of sale is negotiated in order to reduce risk, avoid cost disputes and limit any potential for misunderstandings or delays. An incoterm gives a large amount of commercial information to the buyer and seller. Each incoterm is supported by a detailed legal definition. Companies trading internationally often use a freight forwarder who is an expert service provider that arranges shipments and provides advice on how to navigate incoterms.

The various incoterms refer to when the risk and responsibility of the goods being transported are transferred from seller to buyer, i.e. how far along the process will the supplier ensure that the goods are moved, and at what point does the buyer take over the shipment. Each Incoterm provides exporters and importers with clear rules that help them understand their responsibilities and clarify any grey areas in contracts. Free on Board (FOB) is one of the most frequently used terms.

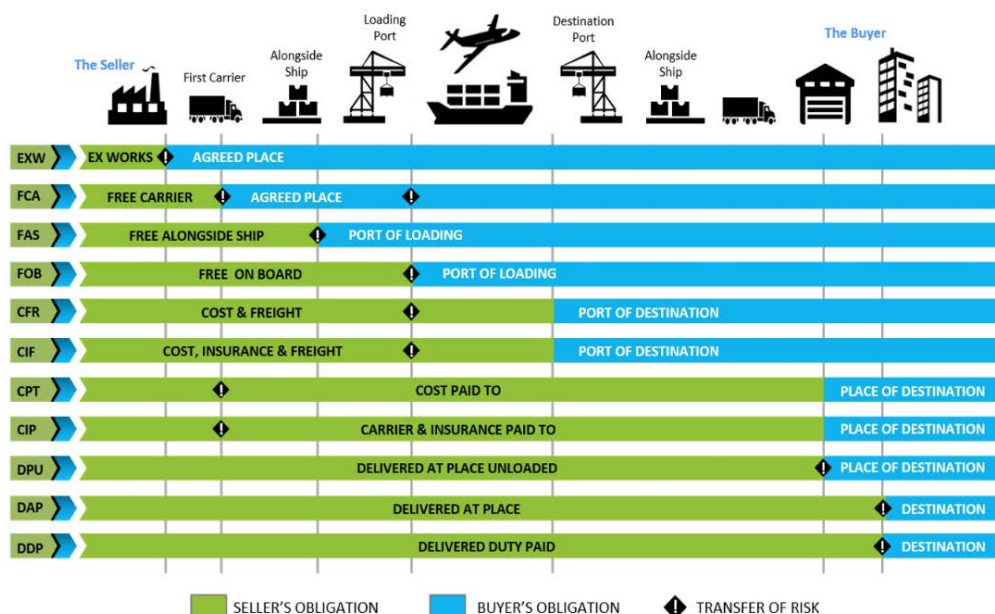
The risk of losses

Under FOB, the buyer is liable for any loss while the goods are in marine transit and should purchase insurance to protect the shipment. A company, using the term FOB, recently lost 13 containers off the back of a ship and several others were flattened when being unloaded. It could have been a very expensive mistake as the cargo was also underinsured. However, all items were recovered without incident but the buyer could have incurred a substantial financial loss.

The incorrect term was used in this case as the buyer did not want to take the risk of loss so early in the process. He really wanted the shipment to be the responsibility of the seller until it reached the destination port. It is important that staff are trained to understand the definition and use of each of the terms listed below.

INCOTERMS 2020

Point of Delivery and Transfer of Risk



Incoterms[®] source: Oceanair.net



INCOTERMS 2020®

Incoterms 2020®, effective January 1, 2020 consists of 12 incoterms inc Ex-works. The point where the responsibility moves from the seller to the buyer is defined by the first letter of the trade term:

- E - transfers the goods at the seller's location
- C - means the carriage is paid by the seller to move to another country
- F - means the seller has freight contract obligations in the country of the seller
- D - means the goods are delivered by the seller into another country

INCOTERMS 2020

Responsibility Matrix for Contract of Sale



INCOTERMS 2020	FREIGHT COLLECT TERMS					FREIGHT PREPAID TERMS						
	EXW	FCA	FCA	FAS	FOB	CFR	CIF	CPT	CIP	DPU	DAP	DDP
	Ex-Works	Free Carrier (Warehouse)	Free Carrier (Port/Airport)	Free Alongside Ship	Freight on Board	Cost & Freight	Cost Insurance & Freight	Carriage Paid To	Carriage & Insurance Paid	Delivered at Place Unloaded	Delivered at Place	Delivered Duty Paid
Mode of Transport	Any Mode	Any Mode	Any Mode	Ocean Only	Ocean Only	Ocean Only	Ocean Only	Any Mode	Any Mode	Any Mode	Any Mode	Any Mode
Obligations and Charges												
Export Packaging	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Export Formalities	Buyer	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Loading at Point of Origin	Buyer	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Origin Inland Freight	Buyer	Buyer	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Origin Port charges	Buyer	Buyer	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Forwarder Fees	Buyer	Buyer	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Ocean / Air Freight	Buyer	Buyer	Buyer	Buyer	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Destination Port Charges	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Seller	Seller	Seller
Customs Clearance	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Seller
Import Duties & Taxes	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Seller
Delivery Charges to Final Destination	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Seller	Seller

Incoterms ® source: [Oceanair.net](https://www.oceanair.net)

Other changes in INCOTERMS 2020®

- Incoterms 2020® rules recognizes sellers who may use their own transport to deliver the goods. The terms now expressly state that sellers can make a contract for carriage or simply arrange for the necessary transportation.
- Incoterms 2020® rules now specifically call out the import and export security requirements and identify whether the buyer or seller is responsible for meeting them.

- Sellers and buyers are now contractually obliged to assist each other with documents and information.

What incoterms don't cover

Incoterms will deal with many of the practical issues of delivery and risk, but they don't cover everything. For example, they do not define the description of the goods; price and payment; title/ownership of the goods; intellectual property; or the jurisdiction. Incoterms also do not cover possible force majeure situations and breach of contract.

Incoterms are quite complex and if incorrectly used they can cost time and money. It is important that the contract states that the new 2020 rules apply and that the destination is accurately defined, e.g. CIF, Port of Shanghai, Quay 4, Incoterms 2020® (or 2010). This will reduce the risk of delays or litigation. Used well, with knowledge and understanding, Incoterms can expedite logistics and enhance customer satisfaction.

More detail is available in the ICC publication Incoterms 2020®.



Incoterms 2020®

Author



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Elaine holds a Master's Degree in Management and a Bachelor of Commerce (Hons).

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LinkedIn

Reference

*At the time of publishing this knowledge paper all details are correct to the best of our abilities, to keep ahead of further developments with Incoterms 2020® please review the link below.

Reference

<https://iccwbo.org/resources-for-business/incoterms-rules/incoterms-2020/>

<https://oceanair.net/resources/incoterms-2020/>

