



Using Incoterms to Make Your Products More Competitive Overseas

by Chris Johnston, President, WTCBN

When entering into an agreement to sell products to a company in another country, it is important that both parties have a common understanding of each party's costs, risks and obligations on the delivery of the goods. The International Chamber of Commerce (ICC) has devised, published and copyrighted the widely accepted Incoterms (International Commercial Terms). The most recent version is referred to as Incoterms 2000. There are 13 Incoterms in all.

WHAT ARE INCOTERMS AND WHEN ARE THEY USED?

Incoterms is an abbreviation of International Commercial Terms, which were first published in 1936 by the International Chamber of Commerce. Since that time there have been six different revisions and updates to the Incoterms. The Incoterms provide a common set of rules for the most often used international terms of trade. The goal of the Incoterms is to alleviate or reduce confusion over interpretations of shipping terms by outlining who is obligated to take control of and/or insure goods at a particular point in the shipping process. Furthermore, the terms outline the obligations for the clearance of the goods for export or import and packing requirements. The Incoterms are used quite frequently in international contracts and an official version of the Incoterms should be referenced in the text of the contract. Although the Incoterms are widely used and exceedingly handy, they are not appropriate for every type of contract. The terms used in a contract state exactly when the shipper unloads and relinquishes obligation and when the buyer takes responsibility for carriage and insurance. The Incoterms are not meant to replace statements in a contract of sale that outline transfers of ownership or title to goods. Therefore, the Incoterms may not be of use when looking to resolve disputes that may arise regarding payment or ownership of goods.

WHAT ARE SOME EXAMPLES OF INCOTERMS?

Incoterms fall into four different groups: Departure (E), Main Carriage Unpaid (F), Main Carriage Paid (C) and Arrival (D). The point at which liability and carriage transfer from the seller to the buyer distinguishes the groups and each group's letter corresponds to the first letter of an INCO Term. For example, if your agreement with a buyer calls for the seller to release goods at the seller's location (Departure group), the INCO Term Ex Works (EXW) would be used.

Ex Works states principally that the buyer takes over carriage and insurance responsibilities at the seller's dock. Alternatively, if the seller were to deliver goods to the buyer's dock, including all carriage and insurance, a term from the arrival group such as DDP (Delivered Duty Paid) would be appropriate.

DDP requires that the seller deliver goods to the buyer's dock with all carriage, insurance and duties paid. In the range of Incoterms, DDP entails the most obligations for the seller, whereas EXW represents the least. Caution must be exercised when using Incoterms because they relate to particular modes of transportation.

For example, Incoterms such as FOB (Free on Board) and CIF (Cost, Insurance and Freight) are only applicable to sea transport. FOB indicates that the shipper (seller) has upheld his/her part of the agreement when the goods pass the ship's rails at the port of exit. The receiving party (buyer) assumes risk and costs associated with the goods once they pass the ship's rail in the seller's homeport. Due to the specific mention of the ship's rails, an aircraft or other mode of transport should not be used with FOB. For a shipment scheduled for delivery by air, rail, or some other form of transport with the same agreement as FOB one would need to use the Incoterm FCA, or Free Carrier.

FCA can include other modes of transportation such as road, rail, inland waterway and air. Whereas transfer under FOB takes place when the cargo passes the ship's rails, transfer with FCA occurs when delivery of goods has been made at a destination previously outlined by the buying party.

These examples are not an exhaustive or definitive guide, but serve to highlight common Incoterms used in exporting.

WHAT IS THE MOST COMMON INCOTERM USED IN OUR REGION AND WHY?

EXW (Ex Works at a named place), for example, "EXW Silver Creek, NY," is a typical Incoterm used in our region. This places minimum delivery responsibility on the seller. Under EXW, the buyer is responsible for filing export documentation. However, the U.S. government continues to hold the seller responsible for export control compliance and for filing of Shipper's Export Declaration information. Because of this conflict, EXW is rarely the appropriate Incoterm. In its place the shipper should consider FCA (Free Carrier at a named place), for example, "FCA Silver Creek, NY". The reason EXW and FCA are used is primarily a matter of convenience. They are after all, the easiest method to use and this explains their popularity.

WHAT INCOTERM WILL MAKE MY COMPANY'S PRODUCT MORE COMPETITIVE OVERSEAS?

It is important to understand the way business is done in the export market and conduct your business similarly by offering the same value proposal as local suppliers. Payment terms, delivery and after-sale servicing are important considerations. In an increasingly competitive world, quoting and delivering your product EXW or FCA can severely limit your competitiveness versus another competitor. At WTCBN, we recommend exploring the option of quoting your product CIF (Cost, Insurance and Freight) or CIP (Carriage & Insurance Paid to [named place of destination]), as it shows the foreign buyer the cost of getting the product to or near the desired country. If your product is in great demand, quoting FCA is more palatable, but as competition increases, CIF or CIP, will allow you a greater degree of flexibility in your buyers' mind and make your product more competitive internationally.