

Newsletter No. 55 (EN)

**Trade Terms in International Sale of Goods
and International Commercial Terms
(INCOTERMS)**

June 2010

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Trade Terms in International Sale of Goods and International Commercial Terms (INCOTERMS)

I. What are Trade Terms?

In a sale of goods contract, it is crucial, that the seller and the buyer discuss the issues regarding time, place and manner of transfer of such goods. Such issues are called “trade terms”. Thus simply defined, Trade terms are the sets of responsibilities of the buyer and seller in a sale relating to delivery of goods i.e. the method of delivery, the payment of costs of shipping, insurance and customs. Additionally, trade terms can also cover other parts of an agreement in the sale of goods, such as the purchase price, etc. Generally trade terms deal with 2 main issues:

- The allocation of the obligations such as loading and unloading fees, documentation charges, payment of import and export duties, insurance, handling charges, package for export etc.
- Delivery matters such as the place and time of delivery, etc.

II. Use of Trade Terms

The objective of trade terms is to help the seller and the buyer to settle the mentioned issues. Predefined trade terms have been developed in form of abbreviations which already allocate the obligations of the parties, so that they do not need to consume much time for negotiating the conditions of each issue.

During the past, various standard forms of trade terms in various countries have been developed. Although similar trade terms are used in international transactions, care must be taken as they may be interpreted differently in different countries, therefore, it is important that the parties have a common understanding of the applied terms. Despite the existence of various standard forms, the most commonly used standard form is ‘International Commercial Terms’ (INCOTERMS).

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III. What are International Commercial Terms (INCOTERMS)?

Introduced by the International Chamber of Commerce, INCOTERMS are a set of international rules for the interpretation of the most commonly used trade terms in international trade. The purpose of INCOTERMS is to standardise the usage of trade terms so that the uncertainties of different interpretations of trade terms in different countries can be avoided or at least reduced to a considerable degree. At present, there are three valid versions of INCOTERMS i.e. INCOTERMS 1980, 1990 and 2000.

IV. Validity

INCOTERMS are only valid if their appliance has been agreed upon explicitly in the contractual terms or has been mentioned in agreements, offers/quotations, general purchase and sales conditions, orders, order confirmations etc. or included in separate agreements. It needs to be clearly specified in agreements which version of the INCOTERMS shall apply, for instance “INCOTERMS 2000” (or another earlier version), so the parties know precisely what their rights and obligations are. A reference to INCOTERMS without further details, might cause problems, because the difference among the three valid versions can be significant.

Formulation proposal: e.g. CIF BANGKOK INCOTERMS 2000 etc.

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V. What areas do INCOTERMS cover?

Generally, INCOTERMS refer to the duties of the parties in certain aspects of an international sales contract. They define the rights and obligations of the parties with regard to:

- Delivery and transportation documentation (or equivalent electronic notifications)
- Allocation of costs for freight, taxes, duties, insurance, etc.
- Transfer of risk

INCOTERMS do not govern:

- The transfer of ownership and other rights arising from ownership
- Breaches of contract and the consequences thereof
- Description or quality of goods
- The timing and method of payment
- Choice of law
- Conditions with forwarders/carriers

VI. Description of commonly used trade terms in INCOTERMS

The definitions of INCOTERMS have broadly divided into four groups of terms as follows:

- The E-terms (EXW) whereby the seller only makes the goods available to the buyer at the seller's premises;
- The F-terms (FCA, FAS and FOB) whereby the seller needs to deliver the goods to a carrier appointed by the buyer;
- The C-terms (CFR, CIF, CPT and CIP) whereby the seller has to contract for carriage, but without assuming the risk of loss of or damage to the goods sold or additional costs due to events occurring after shipment and dispatch;

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- The D-terms (DAF, DES, DEQ, DDU and DDP) whereby the seller has to bear all costs and risks needed to bring the goods to the place of destination.

VII. Most commonly used

1 Ex Works (EXW)

Main obligations for the parties in this term are as follows:

a) Delivery

The seller must provide the goods in proper packaging, and placing at the disposal of the buyer at the seller's premises e.g. his factory, warehouse etc., not loaded on any collecting vehicle on the agreed time or, if no such time is agreed, at the usual time for delivery of such goods. If no specific point has been agreed within the named place, the seller may select the point at the place of delivery which best suits his purpose. The risk of loss or damage of the goods passes to the buyer as soon as the seller fulfils his delivery obligation i.e. placing the goods at the disposal of the buyer.

b) Contract of Carriage and Insurance

Since the seller is only obliged to place the goods as described above, he has no obligation to take care of the carriage and insurance. The buyer has to undertake these matters by himself.

c) Custom formalities for export and import of the goods

The buyer must obtain at his own expense any export and import document and carry out both export and import custom formalities.

This term represents the minimum obligations for the seller, and the buyer has to bear all costs and risks involved in taking the goods from the seller's premises.

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2 Free On Board (FOB)

The term 'FOB' applies particularly for maritime and inland waterway transportation. The main obligations for the parties are:

a) Delivery

This term obliges the seller to deliver the properly packaged goods on board the vessel in the manner customary at the port of shipment. The seller fulfils his obligations to deliver when the goods have passed over the ship's rail. As a result, he must bear all risks to the goods until the time the risk passes.

b) Contract of Carriage and Insurance

The vessel must be provided and contracted by the buyer at his own expense. Due to non-obligation in 'Insurance' for the seller, the buyer has to apply at his own expense if he wants the carriage to be covered by insurance.

c) Custom formalities for export and import of the goods

The seller must obtain at his own expense any necessary export document and carry out export custom formalities; meanwhile the buyer has to do the same in terms of import procedure.

3 Cost and Freight (CFR)

The term 'CFR' applies particularly for maritime and inland waterway transport as well. The main obligations for the parties are:

a) Delivery

The nature of delivery and passing of the risk is the same as that of FOB.

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b) Contract of Carriage and Insurance

The seller must contract at his own expense for the carriage of goods to the named port of destination. In other words, he has to bear the cost and freight in the contract of carriage. However he is not obliged to take out any insurance policy. It is the buyer's duty in case he wants insurance coverage.

c) Custom formalities for export and import of the goods

The character of this obligation is identical to that of FOB.

It should be noted that in practice, many traders worldwide frequently continue to use the traditional expression 'C&F'. If C&F INCOTERMS is used, the court will use INCOTERMS 1980's meaning which is different from INCOTERMS 2000's. Thus it is strongly suggested that the parties use the correct term i.e. CFR in order to avoid any unexpected dispute.

4 Cost, Insurance and Freight (CIF)

The main obligations for the parties in this term are:

a) Delivery

The nature of delivery and passing of risk for CIF is the same as that of FOB.

b) Contract of Carriage and Insurance

The seller is obligated at his expense to procure not only the contract for the carriage of the goods, but also 'minimum insurance cover of the Institute Cargo Clause' for the

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goods transported. In other words, he has to bear the cost, freight and marine insurance costs to the named port of destination.

c) Custom formalities for export and import of the goods

The character of this obligation is the same as that of CFR.

VIII. Conclusion

When negotiating an international sales contract, both parties need to pay attention to trade terms. Each party must be aware of the extent of his/her responsibilities because agreeing on certain trade terms might result in additional costs. INCOTERMS should be adopted in the light of the fact that they define exactly the responsibilities and risks of both the buyer and the seller. They also help to speed up the process of trade negotiations. Therefore, INCOTERMS are the most useful and common trade terms.

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	EXW	FOB	CFR	CIF
SERVICES	Ex Works	Free On Board	Cost and Freight	Cost, Insurance & Freight
Warehouse Storage	Seller	Seller	Seller	Seller
Export Packing	Seller	Seller	Seller	Seller
Loading Charges	Buyer	Seller	Seller	Seller
Inland Freight	Buyer	Seller	Seller	Seller
Terminal Charges	Buyer	Seller	Seller	Seller
Forwarder's Fees	Buyer	Buyer	Seller	Seller
Loading Onto Vessel	Buyer	Seller	Seller	Seller
Ocean/Air Freight	Buyer	Buyer	Seller	Seller
Duty, Taxes & Customs Clearance for Export	Buyer	Seller	Seller	Seller
Charges On Arrival at Destination	Buyer	Buyer	Buyer	Buyer
Duty, Taxes & Customs Clearance for Import	Buyer	Buyer	Buyer	Buyer

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We hope that the information provided in this brochure was helpful for you. If you have any further questions please do not hesitate to contact us.

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