
**Small businesses selling internationally tend to rely on large logistics companies for their shipping needs. Their orders generally are delivered at the right place at right time. But by settling for the "one size, fits all" solutions typically offered, small businesses miss out on customer service options that could help differentiate their products.**

Just as a French buyer might select the supplier that accepts payment in euros or a Mexican distributor might favor open account terms, an arrangement in which the seller pays for insurance or delivers to a preferred port could turn one-off shipments into repeat customers.

According to the U.S. Commercial Service, "The most common Incoterms are EXW (Ex Works); FOB (Free On Board); CIF (Cost, Insurance, and Freight); CPT (Carriage Paid To); DDU (Delivered Duty Unpaid); and DDP (Delivered Duty Paid)."[1] This causes concern as the term DDU was replaced in the latest revision of these internationally recognized terms. Other Incoterms,[2] or International Commercial Terms, frequently are misused. More than learning to use them correctly, small businesses can benefit from applying all the options Incoterms present. Certain Incoterms could represent arrangements that satisfy the needs of a small business but better respond to its international customers.

This paper will define the terms and describe the conditions under which each is most appropriate.

Incoterms have been developed through the International Chamber of Commerce (ICC).[3] Although Incoterms do not dictate trade practice, they have been endorsed by the United Nations Commission on International Trade Law[4] and have been designed to work with the United Nations Convention on Contracts for International Sale of Goods (CISG).[5]

Meant for business-to-business trade, Incoterms define the responsibilities of the buyer and seller in the delivery of goods. Incoterms also convey risk, which party should pay what charges, and where physical delivery occurs. That said, they communicate neither payment terms nor title of goods. Incoterms also do not address prices to be paid, methods of payment, or consequences for non-compliance. Note that with Incoterms, "delivery" means where responsibility for the goods transfers, not necessarily where title to the goods changes hands.

Although laws and regulations take precedence,[6] Incoterms can help to minimize trade disputes.

1 https://www.export.gov/article?id=Incoterms-ecommerce
2 such as EXW and FOB.
3 The ICC also administers the guidelines regarding letters of credit.
4 http://www.unidroit.org/english/news/principles2010-un-en.pdf
5 http://www.cisg.law.pace.edu/cisg/text/passage.html#cisg
6 if a situation goes to court, for example.

The following table summarizes each of the 11 current Incoterms.[7]

| Prefix[8] | How it appears on documents[9] | Meaning |
|---|---|---|
| EXW | EXW (place in seller's country) | Ex Works – goods made available at seller's facility, or at another named place in seller's country; places maximum obligation on buyer |
| FCA | FCA (place in seller's country) | Free Carrier – goods delivered when seller releases them to the first carrier designated by buyer at a named place in seller's country |
| FOB | FOB (port of shipment) | Free On Board – goods delivered when seller loads them on board the vessel in seller's country; seller arranges export clearance |
| FAS | FAS (vessel named by buyer at port of shipment) | Free Alongside Ship – goods delivered when seller places them alongside buyer's vessel at the named port of shipment in seller's country |
| CFR | CFR (port of destination) | Cost and Freight – goods delivered after seller loads them on board the ship in seller's country, but seller pays transport to named port in buyer's country |
| CIF | CIF (port of destination) | Cost, Insurance, and Freight – similar to CFR, but seller required to obtain insurance for goods in transit for 110% of value[3] |
| DAT | DAT (terminal at port or place in buyer's country) | Delivered At Terminal – goods delivered once unloaded by seller at named terminal in buyer's country |
| CPT | CPT (place in buyer's country) | Carriage Paid To – goods delivered when seller releases them to the first carrier, but seller pays transport to named place of destination in buyer's country |
| CIP | CIP (place in buyer's country) | Carriage and Insurance Paid To – similar to CPT, but seller required to obtain insurance for goods in transit for 110% of contract value[10] |
| DAP | DAP (place in buyer's country) | Delivered At Place – goods delivered when ready for unloading from arriving means of transport at named place of destination in buyer's country |
| DDP | DDP (place in buyer's country) | Delivered Duty Paid – goods delivered by seller to buyer's facility or another named place in buyer's country, paying all costs; places maximum obligation on seller |

## LEGEND

- Terms appropriate for any mode or modes of transport.
- Terms appropriate only for sea and inland waterway transport, specifically non-containerized goods.
- Terms where responsibility for the goods takes place where the seller – or seller's designated carrier – physically hands them over.
- Terms where responsibility has passed to the buyer before the seller physically hands them over. Although responsibility passes to the buyer within the seller's country, the seller contracts for transport to the buyer's country and physically hands over the goods there.

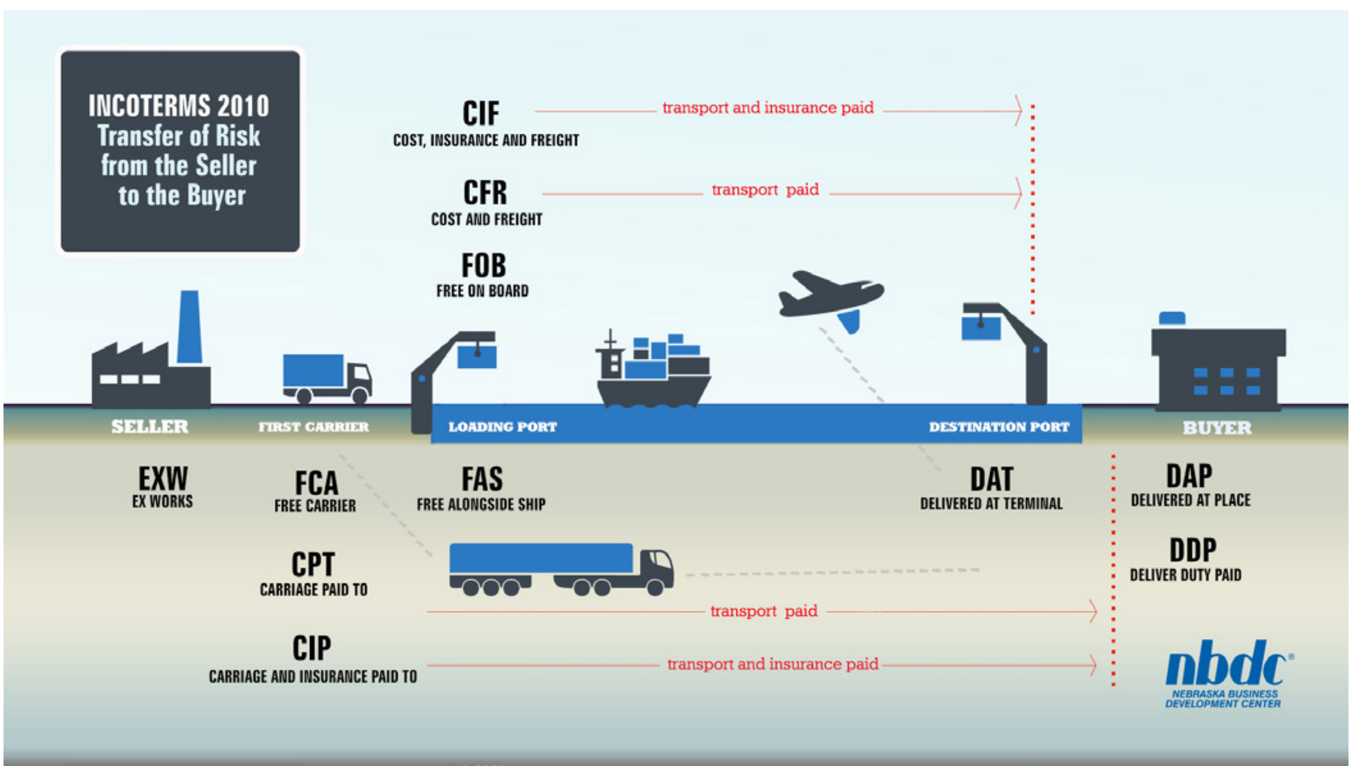
7 Complete definitions are available from ICC in the Incoterms 2010 handbook, which can be purchased at http://store.iccwbo.org/incoterms-2010

To choose an appropriate Incoterm, the first consideration is straightforward. The Incoterms marked with red in the table cover omni-modal transport. This means that a container of goods could be loaded onto a truck, transferred to a train, placed on a ship, and unloaded at a port (then repacked and delivered by plane). The Incoterms marked with blue represent those appropriate only to non-containerized shipments transported via water vessel. Most small businesses will use the Incoterms marked with red.

The next consideration relies more on the small business' relationship with its foreign buyer, depending on where sellers would feel comfortable transferring responsibility of the goods to buyer.

EXW and DDP represent extreme cases that should not see much use in practice. With EXW, the seller loses all control as soon as the seller physically hands over the goods to the buyer[11] in the seller's country. The buyer could re-sell the goods in the seller's country, or export to somewhere besides the buyer's country. The seller would have no idea where their goods end up, despite being liable for their end use. From an export compliance standpoint, representatives of federal agencies have expressed concern with such arrangements.[12]

With DDP, the seller retains control all the way to the buyer's facility in the buyer's country, making the seller responsible for the duties and other import requirements in foreign jurisdictions.




8 These three letters are used regardless of the language used by the parties of the transaction

9 The more precise you make the location in parenthesis, the better. Go beyond naming the factory and include the full address, even the number of the loading dock, if known.

10 under at least the minimum cover of the Institute Cargo Clauses of the Institute of London Underwriters (which would be Institute Cargo Clauses (C)), or any similar set of clauses

11 or the buyer's designated representative, such as a carrier.

12 Consultants at NBDC can educate clients about such compliance requirements and help them navigate the appropriate federal agencies.

For the Incoterms marked with yellow, responsibility transfers somewhere in between the extremes represented by EXW and DDP, at the place where the goods physically are handed over.

For the terms marked with green, responsibility passes to the buyer in the seller's country, even if the goods aren't physically handed over until they reach the buyer's country. With these "C terms," the seller retains control over the transaction — and documents. Because the seller will build shipping into the price of the goods, these Incoterms might be difficult for buyers to accept as they take on the risk — and cost — but have no control over the shipment until the goods arrive in their country.

The Incoterms more favorable to buyers are DAT, DAP, and DDP. With these "D terms," the buyer is responsible for nothing until the goods arrive in the buyer's country.

For small businesses, FCA might represent an attractive compromise. With this flexible term, responsibility transfers in the seller's country, but only after goods have been physically handed over to the buyer's designated carrier. The seller can ensure the shipment gets to a port for export, with the buyer taking it from there.

Additionally, Incoterms can play a role in figuring import duties, affecting goods' total landed costs.[13] For example: South African customers could pay taxes on the "FOB" value of imports and Brazilian customers could pay taxes on goods' "CIF" value.[14]

Also when invoicing, small businesses must consider how payment methods work with each term. The seller might want to retain control of the goods into the buyer's country if selling open account,[15] and the buyer might want to take possession of the goods in the seller's country if paying cash in advance.[16] Additionally, if payment involves a letter of credit, the seller will not want to rely on the buyer's carrier to provide the documentation necessary to exercise it.

Incoterms, then, work with other elements of the contract between the seller and buyer. Knowledge of them can help exporters and their customers negotiate terms that work for parties on both sides of the shipment. In an increasingly crowded global marketplace, Incoterms are a useful tool that can help small businesses differentiate their goods through customer service.

## Questions about Incoterms?

The Nebraska Business Development Center (NBDC) provides a variety of consulting services to small businesses, including business planning, government contracting, and export assistance. Resources for current and future exporters are available on NBDC's website at nbdc.unomaha.edu/export. The site features an export readiness assessment tool as well as a *Step-by-Step Guide to Exporting.*

Contact Josh Nichol-Caddy at (402) 554-4092 or jnicholcaddy@unomaha.edu to discuss international marketing strategies for your small business.

13 This is the total amount it will cost for the goods to arrive at the customer's door.

14 https://www.dutycalculator.com/ These rates apply regardless of whether FOB or CIF are the Incoterms actually used in the sales contract between the buyer and seller, so invoices (starting with the pro forma) should itemize the necessary elements for figuring duties as well as the costs associated with the Incoterm that will be used for the shipment.

15 "C terms" and "D terms."

16 Ex Works or "F terms."

## ABOUT THE AUTHOR

Josh Nichol-Caddy, MBA, MA, CGBP, is a market research analyst and export consultant for NBDC. He received a master's degree in journalism as well as an MBA from the University of Missouri. While a student at MU and faculty member at Stephens College in Columbia, Missouri, he worked with various organizations to develop marketing and media strategies. He also has worked as a video editor, copy editor, social media marketer, reporter and freelance writer.

## ABOUT THE NEBRASKA BUSINESS DEVELOPMENT CENTER

NBDC provides various services to small businesses, including market research. For companies interested in exporting or commercializing new technologies, the cost for the in-depth report packages frequently are covered by grants.Researchers' global demand surveys provide analysis to companies that want to export but don't know where to start. International market research also can provide leads to specific foreign markets.

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