



## WHICH INCOTERM WORKS BEST FOR YOU?



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### CHOOSING THE RIGHT INCOTERM



Incoterms<sup>®</sup> are not a customs issue but they have a bearing on how customs processes take place, what value is applied and who is responsible for what. Getting your incoterms<sup>®</sup> right is an essential step in your Brexit preparations and is, in fact, one of the most important initial steps.

The challenge in European trade is not so much the new processes but rather the difficulty in applying them retrospectively to existing and established contracts. Import duty, VAT and documentation charges were not part of the conversation when the seller/buyer relationship was initially created, at least not in most cases.

To make matters slightly worse European trade tends to work on a ‘delivered’ or ‘collected’ basis which is fine in straight-line logistics but no longer fit for purpose in post-Brexit trade flows. Not only do these terms fail to define responsibilities but they tend to infer certain agreements that do not exist. Buying goods ‘delivered’ does not automatically mean that this becomes ‘delivered duty paid’.

Conversations need to take place between buyer and seller so that agreements can be up-dated. There are numerous ways of handling these negotiations and not all need to involve customs processes. Our number one advice, from day one, has always been ‘do not go looking for borders’. When it comes to Incoterms<sup>®</sup> this could equally relate to customs processes : ‘do not go looking for complications’.

There are various Incoterms<sup>®</sup> and you should choose those most relevant to what you want to achieve (and what you can agree). Most are still more suited to ocean freight but this does not mean they cannot be applied successfully to road freight or even short sea container traffic.

INCOTERMS 2020 EFFECTIVE 2020	EXW	BOX 45 CODING	EXPORT CUSTOMS CLEARANCE	LOADING ON TRUCK	CARRIAGE TO PORT OF EXPORT	OFF TRUCK CHARGES AT PORT OF EXPORT	LOADING CHARGES AT PORT OF EXPORT	FREIGHT TO PORT OF IMPORT	UNLOADING CHARGES AT PORT OF IMPORT	ON TRUCK CHARGES AT PORT OF IMPORT	CARRIAGE TO NAMED PLACE	IMPORT CUSTOMS CLEARANCE	IMPORT DUTY	IMPORT VAT
		EXW	A	BUYER	BUYER	BUYER	BUYER	BUYER	BUYER	BUYER	BUYER	BUYER	BUYER	BUYER
<b>RULES FOR ANY MODE OR MODES OF TRANSPORT</b>														
Ex Works	EXW	A	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
Free Carrier	FCA (a)	A	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
Carriage Paid To	CPT	K	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer
Carriage Insurance Paid To	CIP	C	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer
Delivered at Place	DAP	C	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer
Delivered at Place Unloaded	DPU	C	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer
Delivered Duty Paid	DDP (1)	E	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller
Delivered Duty Paid	DDP (2)	E	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer
<b>RULES FOR SEA AND INLAND WATERWAY TRANSPORT</b>														
Free Alongside Ship	FAS	A	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
Free Onboard Vessel	FOB	A	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
Cost & Freight	CFR	K	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
Cost Insurance & Freight	CIF	B	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer

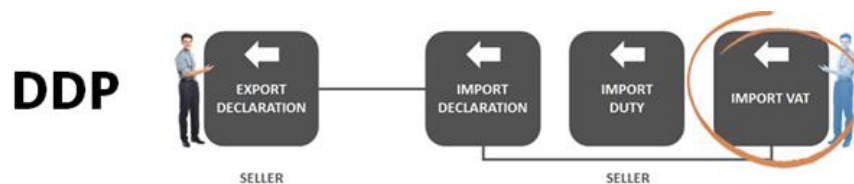


## ZOOMING IN ON DELIVERED

Recognising that delivered and/or collected are the most common terms in current EU flows, it is sensible to zoom in on these terms specifically.

### DELIVERED DUTY PAID - DDP

It would be easy to turn to your supplier and politely inform them that you now buy DDP. In most cases the trader simply wants to inform the seller that they will not accept the additional cost and will leave it to the seller to handle the duty and seek re-negotiation with the buyer as appropriate. However, the customs impact is perhaps greater than you thought:-



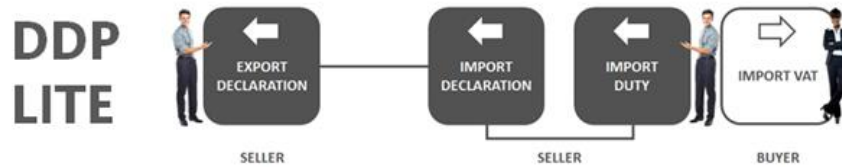
True duty paid means that the seller is not only responsible for the import duty and documentation charges but also the import VAT. This means that the seller requires VAT registration in the country of destination. This is not a quick fix. More of an issue is that the customs broker will also need to operate on an indirect basis as the importer is not established in the customs territory where the import entry is being lodged. This means the broker becomes jointly and severally liable for the customs debt of the non established 'foreign' importer. Customs brokers are in short supply and finding one that will act as an indirect representative is 'needle in a haystack' territory.

The nonsense of DDP is that the buyer still ends up paying the VAT only rather than paying directly to customs they now pay the virtual identity of the foreign supplier who is required to form a VAT identity in the destination country.....and then charge local VAT on the eventual supply.

### DDP LITE



This term does not officially exist. It is a derivation of DDP that is quite commonly used in the UK but not so much in Europe. It has the same agreement on duty and documentation charges as DDP but has the buyer acting as the importer of record and accounting for import VAT directly with customs.



One of the obvious benefits is that the seller does NOT require VAT registration in the country of destination. The customs broker acts as a direct representative of the buyer (importer) and charges the duty and documentation charges back to the seller.

The importer of record is liable for the customs debt should the entry be under-declared but is not responsible for the import duty which is paid by the agent on behalf of the seller. This effectively has the importer (buyer) assuming the same liability as the broker would have done under the conditions of indirect representative, only difference being that the buyer has a relationship with the seller and a financial connection whereas the broker only had customs documentation responsibilities and no other connection with the seller.

Recommendation. If you insist on DDP, then DDP LITE is perhaps a better option. It still leaves the duty with the seller and puts the onus on them to initiate re-negotiation of prices.

## **DELIVERED AT PLACE – DAP**

DAP requires the seller to arrange transport as before and assumes the buyer will arrange import customs clearance and the payment of duty and/or VAT. This appears simple and clean-cut but can be a problem if the buyer does not have an account with customs to pay the duty and or VAT on arrival. In a DAP environment the transporter does not have a relationship with the buyer aside from him being a delivery address. The buyer will probably not even have an account with the logistics provider. He has not needed one before. So, buying goods on DAP terms is fine if you have the import process taken care of or a broker working on your behalf. However, supplying goods on a DAP basis could mean that the goods are not delivered until your customer pays the freight forwarder. This might create a strain that you had not seen coming. DDP LITE might be better and might help to keep goods moving. Although if you sell on a DDP LITE basis the onus is on you to re-negotiate now that duty is involved.



So, looking at DELIVERED terms, who drives what?

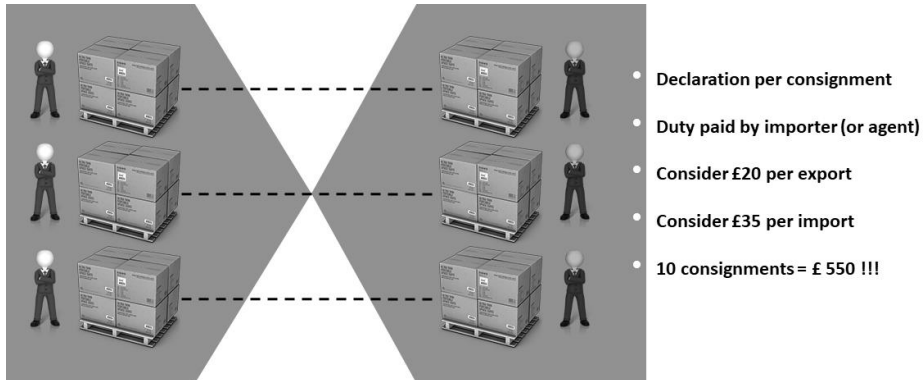
Term	Selling	Buying
DDP	May need VAT registration in the country of destination. Up to seller to initiate negotiations to mitigate additional duty costs at destination	Abdicates responsibility for duty and VAT but creates the need for foreign VAT registration by the seller and the ability to find an agent that will work on an indirect basis.
DDP LITE	Destination VAT is no longer a problem. Easier to find an agent that will work on a direct basis. Duty and documentation charges payable by the seller and up to seller to initiate re-negotiation with buyer to cover additional duty costs.	Buyer accounts for VAT directly with customs. Buyer is the importer of record and may want an indemnity from the seller or insist that your broker is used so that entry accuracy is greater. Duty not your problem although expect contact from the seller regarding prices in general.
DAP	Nice and straight-forward, you supply goods delivered to door and the buyer arranges the import clearance. However the buyer might not have the means to pay the import VAT and/or duty, what happens then? Goods held up through no fault of the seller. Buyer unhappy but unprepared and blames everybody!	Works well in terms of customs clearance and particularly if you have an account with customs for payment of duty/VAT. Does, however, mean that you are accepting the duty/VAT amount and the onus is on you to initiate re-negotiation with the seller in terms of prices/costs.

From the text above (and the table) DDP looks the least attractive. Generally, it should be avoided if possible as the VAT implications and arrangements are cumbersome and perhaps quite unnecessary. Not so with Ireland though. Ironically DDP seems to suit Irish flows better than most and particularly IE to GB.

We have found ourselves talking about FISCAL CONSOLIDATION repeatedly. By this we mean the art of reducing the number of processes involved by consolidating them. It does not suit all but there are certainly times when it suits Irish exports to GB, or at least that has been our experience so far.



We should explain. Take for example, ten consignments from IE to GB, all coming from one exporter but delivering to 10 different locations, all on a DAP basis.

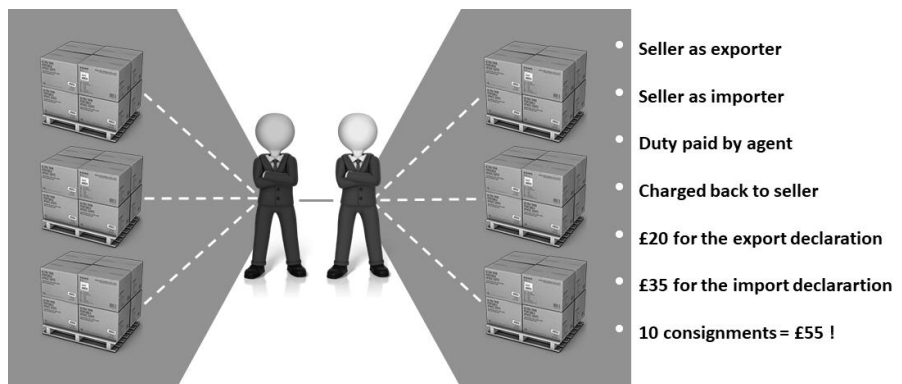


Each consignment would be handled separately and would incur documentation charges in the region of £550. £200 payable by the seller (exporter) and £350 cumulatively but paid individually by the buyers (importers). Nice for the broker, but can be simplified.

In the example above the exporter is £200 worse off and his customers are paying the duty and import documentation charges. The seller, quite rightly, would expect his customers to explore the market for better options, cheaper and less susceptible to cross-border delays. DAP is not a good option.

DDP can work well in this scenario. Say for example the seller (exporter) also registers in the UK (either as a legal entity or simply as a NETP Non Established Taxable Person). The flow is now far more straight-forward:-

The seller is not only the exporter but now is also the importer. Only requires one export declaration and one import. Saving £495 and avoiding the customer having to be



involved in customs matters whatsoever. There are however, two clear down-sides:-

1. In such a scenario all 10 consignments need to cross the border in the same truck (or have individual customs documentation per eventual delivery location)



2. The seller is saddled with the import duty and needs to re-negotiate prices accordingly (perhaps absorbing some/all of the duty to maintain sales)

What is clear from these examples is that no one size fits all. In the first examples DDP was the worst option whereas in the second set DDP was the better choice.



### **CAUTION!**

We have recently spotted an error concerning DDP. EU exporter has created GB identity and will now ship DDP to eventual GB client. EU exporter is now effectively shipping from their EU identity to their new GB identity. EU exporter raises a pro-forma invoice for customs purposes and shows terms as DDP. This is NOT DDP! If, as a customs broker, we see an invoice value and the terms DDP we remove the duty from the price to give us the value for duty. This could result in a significant under-payment of duty. We understand the confusion; EU exporter creates GB identity because of DDP and therefore shows terms as DDP. It is more likely that the initial EU to GB movement is DAP and the eventual GB to GB movement is DDP. Be careful what terms you show on the invoice you will be crossing the border with.

### **ZOOMING IN ON COLLECTED**

Having dealt with DELIVERED, the next most common term we find in Europe is COLLECTED. Goods are bought ex factory gate. This is equally a problem or can be if unless handled correctly.

In current trade there is no VAT as such, the seller quotes the buyer's VAT number (having first checked its validity) and the buyer is responsible for the VAT. No VAT is charged on the invoice as this is an intra-EU movement between two member states. Proof of delivery is required by the seller to prove that the goods left their Member State. This process is known as 'reverse charge'.

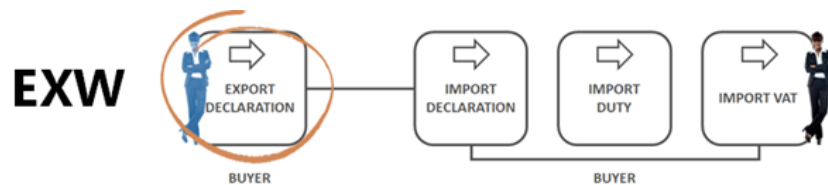
This way of handling VAT stops at the end of the transition period. There will no longer be centralised VAT and intra-EU will exclude GB. Therefore VAT has to be handled in the normal 3<sup>rd</sup> country export manner. Exports are zero rated for VAT and the seller (having not charged VAT) must be able to prove



that the goods were indeed exported. The proof is in the form of an export declaration which is endorsed at exit and sends a message back to the exporter to discharge their VAT liability.

The common collected term is 'ex works' : buyer collects and seller has to do nothing other than sell the goods. This is not, technically, an export. The seller cannot be sure that the goods are leaving their VAT territory.

Ex works is effectively a domestic transaction. The goods are sold ex factory gate plus VAT. This requires the buyer to have VAT registration in the country of purchase so they can recover the purchase VAT and then zero rate the goods for export to themselves. This happens simultaneously.



Not only does the buyer require VAT registration in the country of purchase but he also needs the means to arrange export documentation including export health certification as required. The buyer is essentially the exporter, albeit remotely.

This is a messy and cumbersome solution. A better option would be FCA (Free Carrier). This requires the seller to prepare the goods for export including zero rating the VAT and arranging the documentation. There is still a liability issue but this can be covered by agreement/indemnity. By this we mean there is still a risk that the goods are not actually exported but merely obtained without VAT. One solution is that the buyer pays VAT on deposit which is refunded when the export declaration is endorsed at the exit border.

So, which one works best?

Term	Selling	Buying
EXW	Charge VAT as you cannot be sure that the goods are being exported. At the very least charge the VAT as a deposit which can be refunded on proof of export	You may need VAT registration in the country of purchase so you can buy the goods locally (with domestic VAT) and then export them to yourself (zero rated for VAT).
FCA	Seller arranges export documentation and zero rates the VAT for export. Still requires proof of	Buying goods 'ready to leave' meaning that that they have all of the paperwork required to leave. VAT is zero





export to remove VAT liability but this can be handled by deposit or indemnity.

rated and no requirement to register for VAT in country of purchase unless seller refuses to zero rate.

## CONCLUSION

In all cases, from a customs perspective, the situation is easier if the seller is the exporter and the buyer is the importer. In commercial terms this is not always possible but it does not have to impact the customs process.

Incoterms<sup>®</sup> are International Commercial Terms, not customs conditions. Clearly there will be discussions over who should pay the import duty but Incoterms<sup>®</sup> should not be used as the only solution. There is no better solution than having a discussion with your buyer/seller and agreeing how things will work in the future. You might, for example agree that the seller will pay the import duty, does this make it DDP? Not necessarily. It could be DAP, you pay the duty and simply deduct it from the final payment to the seller. You achieve the same thing but the paperwork is simple and the flow is largely as today.



Many traders are at risk of delaying the goods at the border as a result of Incoterms<sup>®</sup> discussions and the need to take a strong position.

We hope this document has helped explain your options. You need to agree your terms as the customs and border processes will hang off the back of whatever you agree.

Thank you

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