

## WSGR ALERT

DECEMBER 2010

### NEW INCOTERMS 2010 TO BECOME EFFECTIVE JANUARY 1, 2011

On January 1, 2011, the new Incoterms 2010 published by the International Chamber of Commerce (ICC) will go into effect, reflecting developments in international trade within the last decade such as the increased use of electronic documentation and heightened global concerns about cargo security. Incoterms, similar to Uniform Commercial Code (UCC) provisions such as Free on Board (FOB) and Free Alongside Ship (FAS), are trade rules that are used to clarify the rights and obligations of parties with respect to the delivery of goods. However, Incoterms are used primarily in an international context, while the UCC generally applies to domestic sales of goods. Incoterms 2010 is the eighth revision of the Incoterms rules, supplementing the prior revision to the rules in 2000.

Incoterms 2010 provides for several significant changes, including (i) the replacement of four rules (DAF, DES, DEQ, and DDU) with two new rules (DAT and DAP); (ii) reclassification of the categories of Incoterms rules into terms suitable for any mode of transport and terms used for shipping by sea or inland waterways; and (iii) changes dealing with electronic communications, security, and insurance. The Incoterms rules also have been generally updated to make them easier to use and to expand their usage to include purely domestic commercial transactions.

#### **New Incoterms Rules Replacing Current Rules**

Incoterms 2010 includes two new rules, Delivered at Terminal (DAT) and Delivered at Place (DAP), that replace current rules

Delivered At Frontier (DAF), Delivered Ex Ship (DES), Delivered Ex Quay (DEQ), and Delivered Duty Unpaid (DDU). DAP replaces DAF, DES, and DDU, while DAT replaces the current DEQ. Both of the new rules may be used for any mode of transportation with delivery taking place at a named destination, either the specified terminal for DAT or the specified place for DAP. These changes were implemented to reduce the number of terms that had little difference between them, leaving a total of 11 rules in Incoterms 2010 compared to 13 rules in Incoterms 2000.

#### **Reclassification of Incoterms Rules**

In earlier versions of Incoterms, the rules were grouped into four categories in order of increasing responsibility for the seller. Incoterms 2010 instead separates the rules based on mode of shipping, with a first group of terms suitable for any mode of transportation (EXW, FCA, CPT, CIP, DAP, DAT, and DDP) and a second group of terms used for the delivery of goods by sea or inland waterway (FAS, FOB, CFR, and CIF). For the second group of terms, reference to the "ship's rail" has been replaced with "on board," meaning that the goods have been delivered when they are on board the vessel, thus shifting the risk of loading the goods on board to the seller.

#### **Electronic Records**

While earlier versions of Incoterms allowed for the use of electronic data interchange (EDI) messages if the parties had agreed on their use, Incoterms 2010 provides that paper documentation may be replaced with equivalent electronic records if agreed

between the parties or customary. This gives electronic means of communication the same validity as paper documentation. In addition, the scope of what is covered by electronic communications has been specifically left open to allow the Incoterms rules to stay current as electronic communications evolve over time.

#### **Security**

Following the heightened security applied to shipping transactions, many countries require mandatory security screening of goods and containers crossing their borders. The new Incoterms rules have not been changed to address these procedures, instead viewing the screening as a mandatory requirement for the import/export of goods. However, Incoterms 2010 adds clauses requiring the parties to provide information required to obtain import/export clearance and allow international carriers to transport the goods. Previous versions of Incoterms did not require this level of cooperation between buyer and seller.

#### **Application to Both Domestic and International Trade**

While the Incoterms rules primarily have been used in international commerce, they have also increasingly been used for domestic commerce in countries such as the United States or in trade areas such as the European Union that have minimized the use of border formalities. Incoterms 2010 formally recognizes that the Incoterms rules can be used in purely domestic contracts as well. This may lead to an increase in the use of Incoterms rules within the U.S. in place of

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## **New Incoterms 2010 . . .**

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equivalent rules such as those within the Uniform Commercial Code.

### **String Sales**

In contracts for the sale of commodities, it is common for the commodities to be bought and sold several times through a “string” of contracts while the commodities are in transit. A seller in the middle of the string does not actually “ship” the commodities, as they have been shipped earlier in the sales process. Instead, the seller in the middle of the string is responsible for procuring the shipped goods for the next buyer. The rules in Incoterms 2010 have been amended to address this practice, with sellers either having the obligation to ship the goods if they are the initial seller, or “procure goods shipped” if they are a seller in the middle of the string of contracts.

### **Insurance**

The Incoterms 2010 rules take into account the recent revision of the Institute Cargo Clauses in 2009 and clarify the parties’ obligations regarding insurance. Specifically, the rules state that the seller may be required to provide the buyer with additional information that is necessary to procure insurance for the goods. These changes only apply to Incoterms rules where a party is required to obtain insurance, namely CIP and CIF.

### **Terminal Handling Charges**

For selected Incoterms rules where the seller is required to arrange and pay for the transport of goods to the specified destination (CPT, CIP, CFR, CIF, DAP, DAT, and DDP), the cost of unloading and handling the goods often is passed down to the buyer as part of the sales price. However, in some cases the buyer is also responsible for paying the terminal or port for this service, resulting in a double charge. The Incoterms 2010 rules address this issue by

clearly allocating the costs of terminal-handling charges between the parties, thus avoiding the potential for double payment by the buyer.

### **Conclusion**

The changes in Incoterms 2010 do not represent a dramatic departure from previous versions of the rules, but instead update the rules to accommodate recent developments in international commerce. Given the upcoming effective date of January 1, 2011, for Incoterms 2010, parties should review and, if necessary, amend their commercial agreements to ensure that the proper Incoterms rules are used or clarify whether they will rely on Incoterms 2000 or Incoterms 2010 in those cases where the parties may not have designated a date in the contract. If parties historically have used UCC trade terms in their commercial transactions, this may be an opportunity to move toward the use of Incoterms, which are more applicable to international business. If parties intend to use Incoterms 2010, a specific reference to “Incoterms 2010” should be made to avoid any potential dispute as to which version of the Incoterms is applicable. If parties intend to continue the use of older versions of the Incoterms, specific reference to those versions should be made in their commercial agreements.

Wilson Sonsini Goodrich & Rosati’s technology transactions practice regularly advises clients on issues relating to international commercial agreements and transactions, and we will continue to follow developments in this area. Please contact Suzanne Bell, Selwyn Goldberg, Sara Harrington, or any other member of the firm’s technology transactions practice to discuss any questions that you may have regarding the use of Incoterms 2010 or any related matter.



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