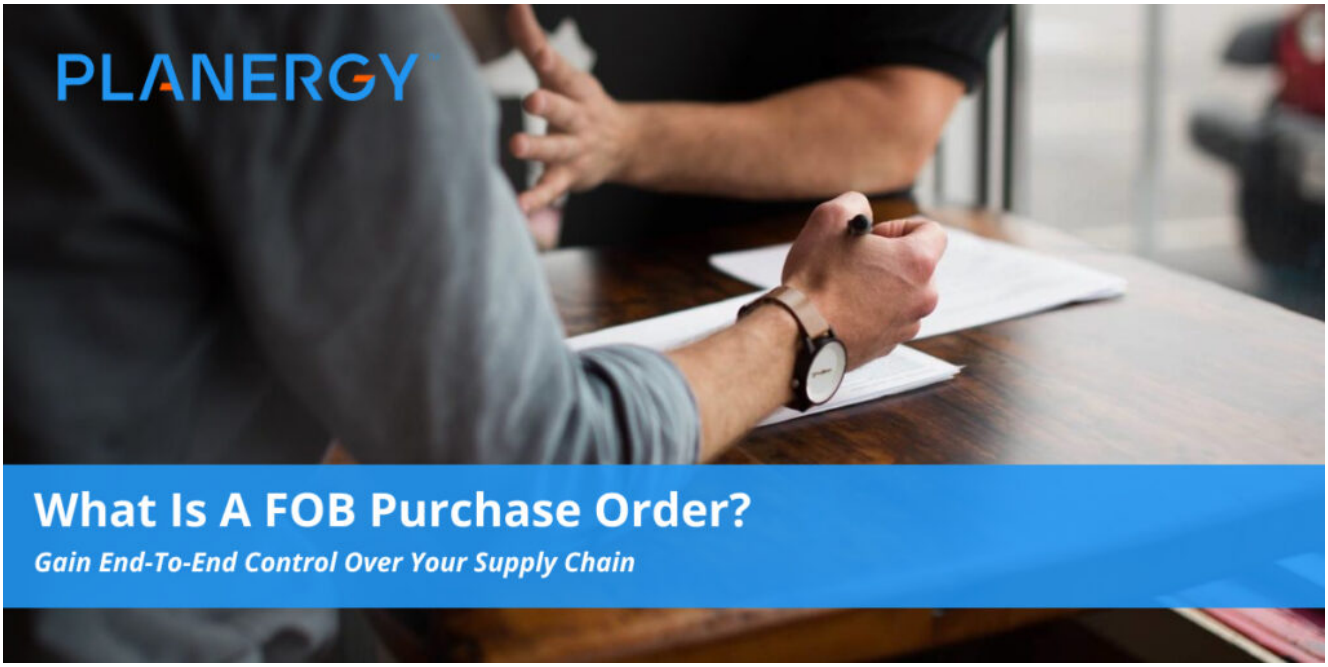
What is a FOB Purchase Order?



Free On Board, or Freight on Board, is commonly shortened to FOB within the shipping industry. It's a key part of purchase order financing documentation necessary for shipping goods internationally or within the United States. The FOB is an addendum to your purchase order that serves as a blueprint for your shipping process – every step of the way.

What is FOB?

The FOB is used in the retail industry to define the party responsible for paying the shipping charges and provides information about where during the journey the goods change ownership from seller to buyer. All domestic shipments must be accompanied by a bill of lading, a bill of sale, and an FOB, which defines the terms of sale.

Typically, the seller pays the initial shipping charges to the warehouse or distribution point, and the buyer takes it from there. Ownership and responsibility for the goods change hands and the buyer picks up transportation costs to retail locations or local warehouses.

> *There are two possible FOB conditions: FOB destination and FOB origin. The details of the FOB are noted on the purchase order and copied to the invoice.*

The Purpose of FOB

The FOB is part of the sales agreement. Since a shipment of goods may have a long way to travel, the FOB determines whether the seller or the buyer is responsible at each stage of the trip. Spelling this out ensures that the shipment is continually insured by one party or the other throughout the journey.

The FOB also declares whether the buyer or the seller can control the journey itself, which may be important in the event of supply chain disruption, dealing with the freight company, or situations where additional costs are incurred.

The shipping company, freight hauler, or delivery company is not involved in the FOB, but also bears responsibility for the goods while in transit. They are liable for delivering the goods on time and without damage.

Most buyers define a standard set of terms for all transactions, and then negotiate with specific vendors if adjustments need to be made.

While the purchase order defines the purchase itself, the FOB adds information for how the goods are handled, insured, moved, and who owns them until what point. The documents go hand-in-hand to completely define the transaction.

FOB Terms and Conditions

FOB Destination

The buyer accepts all responsibility when the shipment arrives at the receiving dock. Ownership of the goods changes hands from the seller (manufacturer or distributor) to the buyer (customer). Within the FOB Destination structure, there are three possible payment arrangements:

1. **FOB Destination – Freight Prepaid:** The seller is responsible for the goods and the shipping or freight charges until the shipment changes hands at the specified destination point.
2. **FOB Destination – Freight Collect:** The supplier is liable for the goods during transit, however, the buyer pays the freight charges upon delivery.
3. **FOB Destination – Freight Collect/Allowed:** The shipper is liable for the goods in transit. The buyer pays the shipping costs upon receipt and

deducts the cost of shipping from the invoice total.

With an FOB Destination agreement, the buyer should record the new inventory at the destination point, when the goods change hands, since that is when the buyer accepts the liability and risk of ownership. Purchase order software makes shipment tracking easy and error free.

The seller subtracts the items from his inventory at the same time. In this case, if the shipment is lost or damaged in transit, the seller would file a claim against his insurance.

FOB Origin

With an FOB origin, also known as shipping point) arrangement in place, the buyer accepts delivery of goods at the point of origin, as soon as the shipment leaves the supplier's shipping dock. The buyer is responsible – and liable – throughout the shipping process, and is responsible for shipping expenses.

In this case, the buyer should add the goods to inventory at the start of the shipping process, and the seller should subtract the inventory from stock at the same time.

If the shipment is lost or damaged during the shipping process in this case, the buyer should file and insurance claim, since he is the legal owner of record.

Payment Considerations

Understanding the details outlined in the FOB is critical to your bottom line. It spells out who is liable for unforeseen charges or fees at each stage of the supply chain.

It's also important to understand how the date impacts your accounting. For example, in the case of an FOB origin agreement, the deadline date the buyer is expected to pay for the shipment may be based on the FOB date, which may include weeks or even months in transit and in customs. Mistaking the terms of the agreement could lead to a very late payment, along with the associated fees and resulting bad faith damage to your supplier relationship.

Global Perspective

As global trading continues to grow, goods may be shipped from anywhere in the world. When dealing with international boundaries, different country laws, port fees, tariffs, and taxes, buyers and sellers need a detailed understanding of who owns the goods, who is liable for the goods, and who pays in the event of an unexpected charge. Imagine a sudden storm forces a cargo ship to take cover in an unscheduled port. An FOB would spell out who pays additional expenses, such as port fees and extra fuel.

When dealing with global shipments, both customer and supplier also need to understand the rules governing trade. The International Chamber of Commerce has established a set of global common rules for international trade, called Incoterms®. Domestic shipping within the United States falls under the Uniform Commercial Code. More than one set of rules might come into play during a long journey, and the FOB should specify the applicable governing laws.

FOB Advantages

Negotiating favorable FOB agreements gives you control over your supply chain. You can choose the shipping line and freight company, specify shipping terms, define the destination and transfer points, and control distribution. And with an automated procurement system, you can track your packages, rate your suppliers, make sure everything arrives on time and invoices are paid in a timely manner.

What’s your goal today?

1. Use PLANERGY to manage purchasing and accounts payable

We’ve helped save billions of dollars for our clients through better spend management, process automation in purchasing and finance, and reducing financial risks. To discover how we can help grow your business:

- Read our case studies, client success stories, and testimonials.
- Visit our Purchase Order Software page to see how PLANERGY can

digitize and automate your purchase order process saving you time and money.
- Learn about us, and our long history of helping companies just like yours.

Book a Live Demo

2. Download our guide “Indirect Spend Guide”

Download a free copy of our guide to better manage and make savings on your indirect spend. You’ll also be subscribed to our email newsletter and notified about new articles or if have something interesting to share.

download a free copy of our guide

3. Learn best practices for purchasing, finance, and more

Browse hundreds of articles, containing an amazing number of useful tools, techniques, and best practices. Many readers tell us they would have paid consultants for the advice in these articles.

Related Posts