

Method of Payment in International Trade

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WHAT IS INTERNATIONAL TRADE ?

- ▶ Exchanging of goods and services between countries
- ▶ Provide opportunities to countries to purchase or sell their goods or services unavailable to their own country
- ▶ Comparative advantages
 - ▶ - Costs advantages, etc



Global Trade Risks



What are Incoterms ?

- ▶ Created by the International Chamber of Commerce (ICC) since 1936. Amendments were later made in 1953, 1967, 1976, 1980, 1990, 2000
- ▶ Facilitate the conduct of international trade
- ▶ Define obligations of parties (seller and buyer)
- ▶ Use exclusively in sales/purchase contracts
- ▶ Always abbreviated by a three character English language acronym.
- ▶ Always accompanied by a geographic place

Purpose and Scope

- ▶ Parties to a contract are unaware of the different trading practices in different countries.
- ▶ It indicates how the costs relating to the export and import of goods should be divided between the seller and buyer.
- ▶ It covers the rights and obligations of the parties in the delivery of goods under the contract of sale.
- ▶ It does not apply to the contract of carriage.
- ▶ It specifies the point for transfer of risk from seller to buyer. Risk of misunderstanding and subsequent disputes is eliminated.

Incoterms 2010 (Effective date : Jan. 1, 2011)

- ▶ Rules for any mode or modes of transport :
 - ▶ EXW ex works
 - ▶ FCA free carrier
 - ▶ CPT carriage paid to
 - ▶ CIP carriage & insurance paid to
 - ▶ DAT delivered at terminal
 - ▶ DAP delivered at place
 - ▶ DDP delivered duty paid

- Rules for sea and inland waterway transport :
 - FAS free along ship
 - FOB free on board
 - CFR cost & freight
 - CIF cost, insurance & freight

Obligations of the Parties

Seller's Obligations

- ▶ **A1 General obligations**
 - ▶ Electronic records & procedures
- ▶ **A2 Licence, authorization, security clearances & formalities**
- ▶ **A3 Contract of Carriage and insurance**
- ▶ **A4 Delivery**
 - ▶ Procurement for FOB, CFR & CIF
- ▶ **A5 Transfer of Risks**
 - ▶ Exception in B5

Buyer's Obligations

- ▶ **B1 General obligations**
 - ▶ Electronic records & procedures
- ▶ **B2 Licence, authorizations, security clearance & formalities.**
- ▶ **B3 Contract of Carriage and Insurance**
- ▶ **B4 Taking delivery**
 - ▶ Procurement of FOB, CFR & CIF
- ▶ **B5 Transfer of risks**
 - ▶ Exception in B5

Obligations of the Parties

- ▶ **A6 Allocation of costs**
 - ▶ Terminal handling charges
- ▶ **A7 Notice to the buyer**
 - ▶ Delivery & carrier fails to take delivery
- ▶ **A8 Delivery document**
 - ▶ Title and/or negotiable document
- ▶ **A9 Checking**
 - ▶ packaging - marking
- ▶ **A10 Assistance with information & related costs**

- ▶ **B6 Allocation of costs**
 - ▶ Terminal handling charges
- ▶ **B7 Notice to the seller**
 - ▶ Delivery & carriage fails to take delivery
- ▶ **B8 Proof of delivery**
- ▶ **B9 Inspection of goods**
- ▶ **B10 Assistance with information & related costs**

EXW

- ▶ The seller delivers when the goods are at the disposal of the buyer at the seller's premises or another named place (i.e. factory or warehouse) not cleared for export and not loaded on any collecting vehicle. It is suitable for domestic trade.
- ▶ This term represents the minimum obligation for the seller, and the buyer has to bear all costs and risks involved in taking the goods from the seller's premises.

FCA

- ▶ The seller delivers the goods to the carrier nominated by the buyer at a named place..
- ▶ FCA requires the seller to clear the goods for export. However, the seller has no obligation to clear the goods for import or pay any import duty..

CPT

- ▶ The seller delivers the goods to the carrier nominated by the seller at an agreed place
- ▶ When CPT is used, the seller fulfill its obligation to deliver when the seller hands the goods over to the carrier and not when they reach the buyer at the place of destination.
- ▶ CPT requires the seller to clear the goods for export. However, the seller has no obligation to pay any import duty.

CIP

- ▶ The seller delivers the goods to the carrier nominated by the seller at an agreed place
- ▶ The seller also contracts for insurance cover against the buyer's risk of loss of the goods during the carriage
- ▶ When CIP is used, the seller fulfill its obligation to deliver when the seller hands the goods over to the carrier and not when they reach the buyer at the place of destination.
- ▶ CIP requires the seller to clear the goods for export. However, the seller has no obligation to pay any import duty.

DAT

- ▶ The seller delivers when the goods, once unloaded from the arriving means of transport, are placed at the disposal of the buyer at a named terminal at destination.
- ▶ The seller has to bear all risks involved in bringing the goods to the terminal at destination.
- ▶ DAT requires the seller to clear the goods for export. However, the seller has no obligation to pay any import duty.

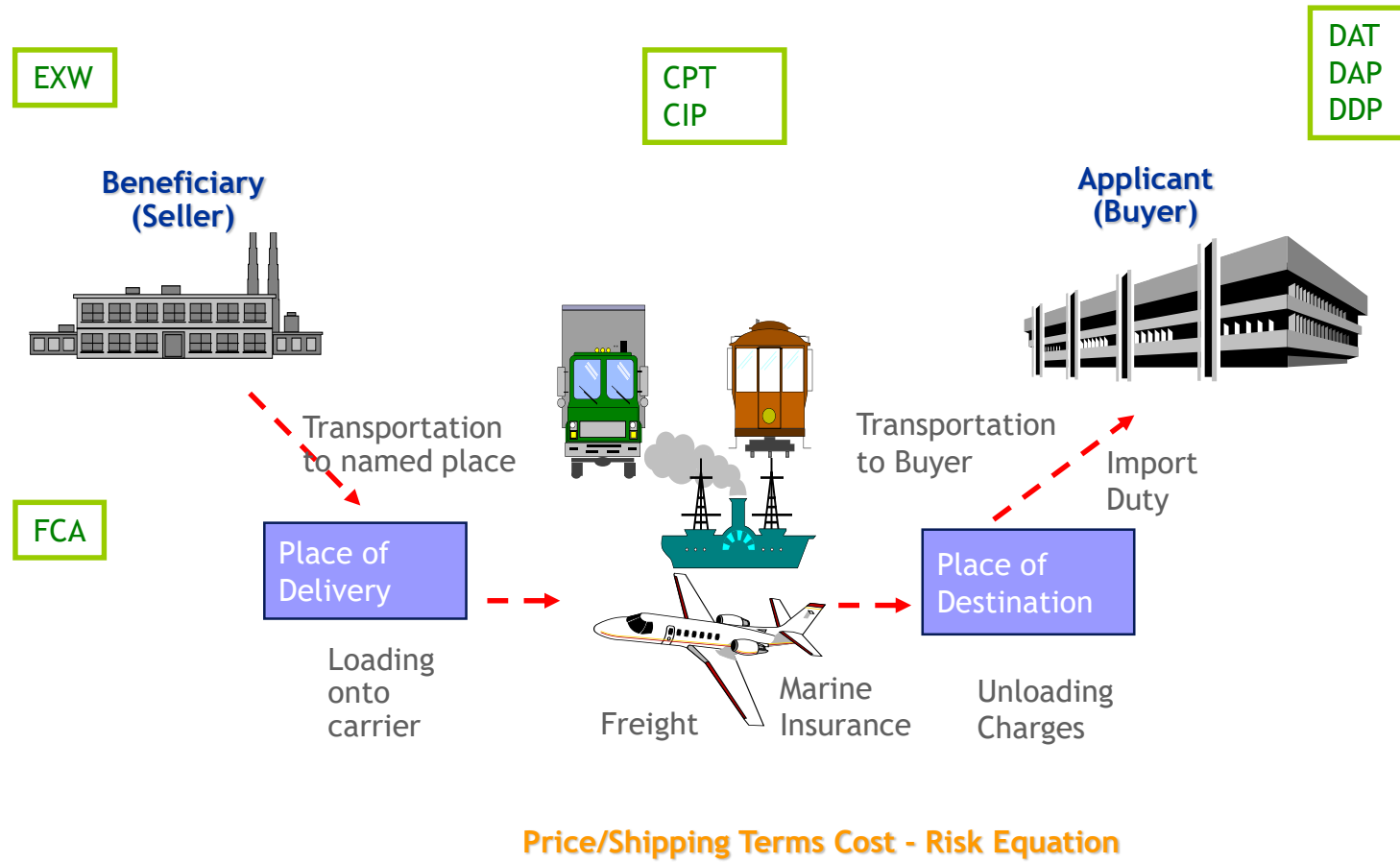
DAP

- ▶ The seller delivers when the goods are placed at the disposal of the buyer on the arriving means for unloading at the named place of destination.
- ▶ The seller has to bear all risks involved in bringing the goods to the named place.
- ▶ DAP requires the seller to clear the goods for export. However, the seller has no obligation to pay any import duty.

DDP

- ▶ The seller delivers when the goods are placed at the disposal of the buyer, cleared for import on the arriving means of transport at the named place of destination.
- ▶ The seller has to bear all risks involved in bringing the goods to the named place.
- ▶ DDP requires the seller to clear the goods for export and import and to pay any import duty and for any customs formalities.
- ▶ The parties are well advised not to use DDP if the seller is unable directly or indirectly to obtain import clearance.

Incoterms 2010 (Rules for any mode or modes of transport)



FAS

- ▶ The seller delivers, when the goods are placed alongside the vessel (e.g. on a quay or a barge) nominated by the buyer at the named port of shipment
- ▶ When the goods are packed in containers, the FAS rule would be inappropriate, and the FCA rule should be used.
- ▶ FAS requires the seller to clear the goods for export. However, the seller has no obligation to clear the goods for import or pay any import duty.

FOB

- ▶ The seller delivers when the goods on board the vessel nominated by the buyer at the named port of shipment.
- ▶ The seller is required either to deliver the goods on board the vessel or to procure goods already delivered for shipment in order to cater for multiple sales down a chain (String sale)
- ▶ For goods deliver in containers, FCA rule should be used.
- ▶ FOB requires the seller to clear the goods for export. However, the seller has no obligation to clear the goods for import or pay any import duty.

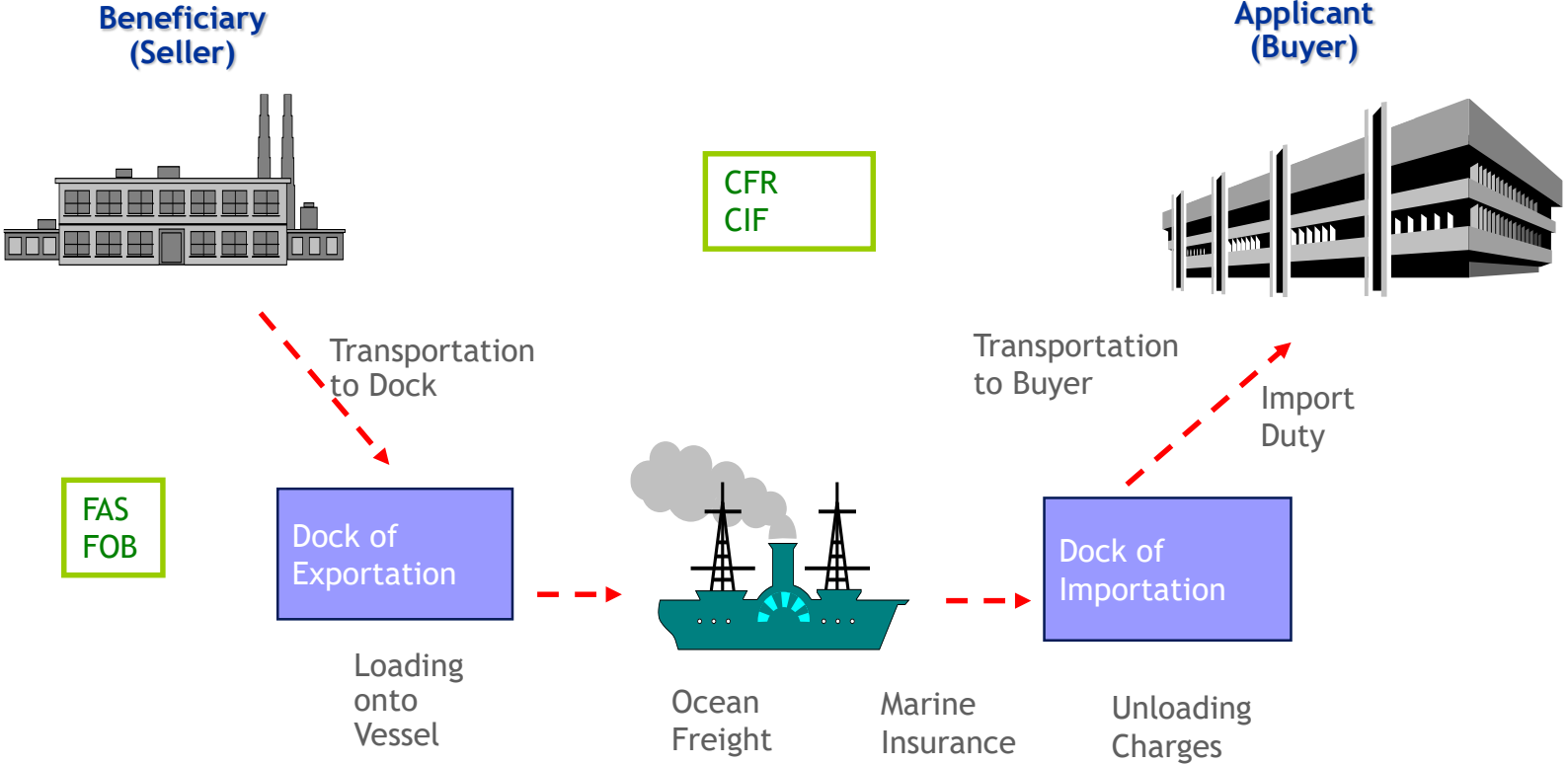
CFR

- ▶ The seller delivers when the goods on board the vessel.
- ▶ If CFR is used, the seller fulfils its obligation to deliver when the seller hands the goods over to the carrier in the manner specified and not when they reach the buyer at the place of destination
- ▶ CFR requires the seller to clear the goods for export. However, the seller has no obligation to clear the goods for import or pay any import duty.

CIF

- ▶ The seller delivers the goods on board the vessel. The seller also contracts for insurance cover against the buyer's risk of loss of or damage to the goods during the carriage. Only minimum cover is needed unless otherwise agreed between the parties
- ▶ For goods in containers, CIP Rule should be used.
- ▶ When CIF is used, the seller fulfils its obligation to deliver when the seller hands the goods over to the carrier and not when they reach the buyer at the place of destination.
- ▶ CIF requires the seller to clear the goods for export. However, the seller has no obligation to clear the goods for import or pay any import duty.

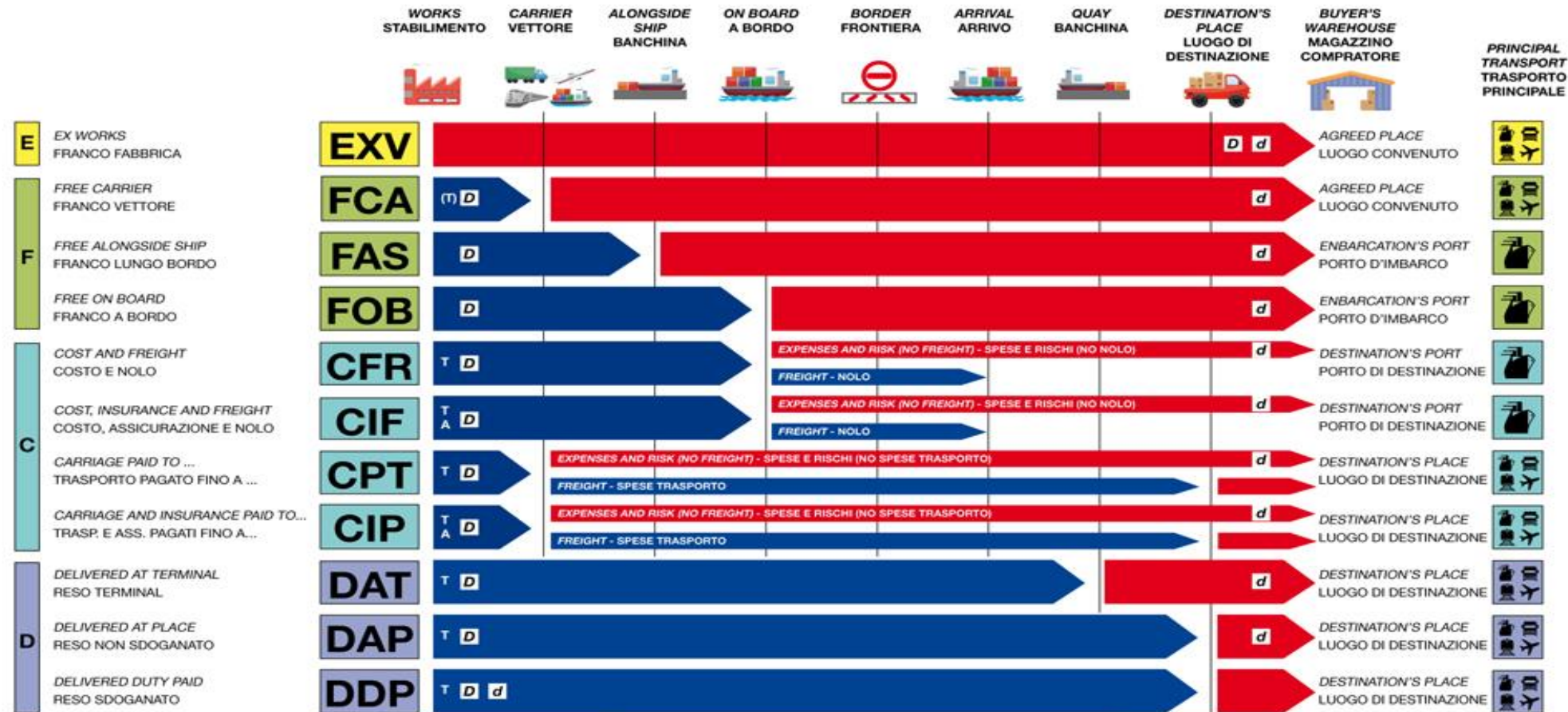
Incoterms 2010 (Rules for sea and inland waterway transport)



Price/Shipping Terms Cost - Risk Equation

Incoterms® 2010

by the International Chamber of Commerce (ICC)



BASIC GROUPS - CATEGORIE FONDAMENTALI

- EX WORKS - FRANCO FABBRICA
- FREE - FRANCO
- CARRIAGE - TRASPORTO
- DELIVERED - CONSEGNA

EXPENSES AND RISKS SPESE E RISCHI
SELLER'S OBLIGATIONS OBBLIGHI VENDITORI

- D Export Clearance Sdoganamento in Esportazione
- d Import Clearance Sdoganamento in Importazione

EXPENSES AND RISKS SPESE E RISCHI
BUYER'S OBLIGATIONS OBBLIGHI COMPRATORI

T It's specifies the obligation to stipulate the freight contract
Indica l'obbligo di stipulare il contratto di trasporto

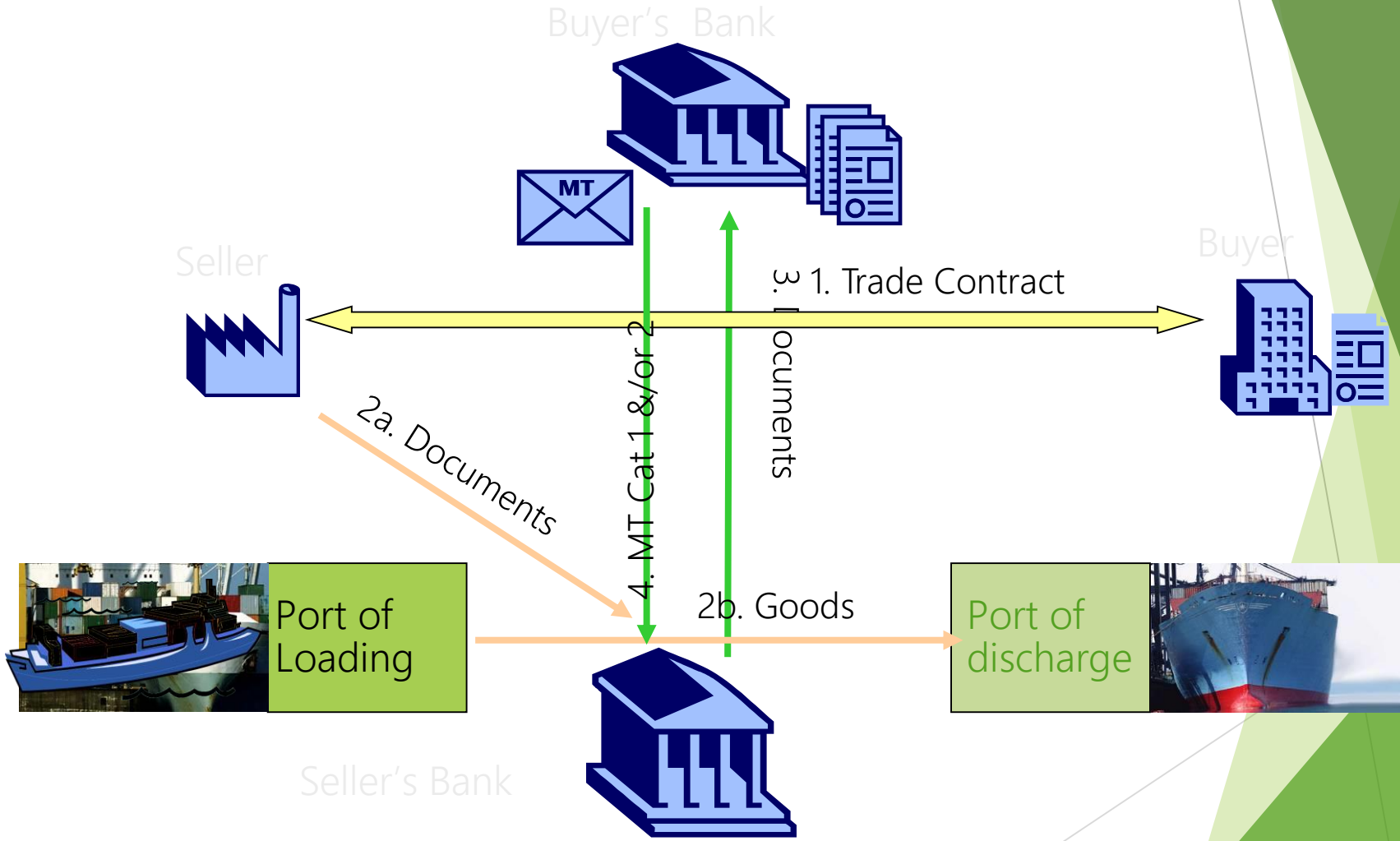
(M) It's specifies the power to stipulate the freight contract
Indica la facoltà di stipulare il contratto di trasporto

A It's specifies the obligation to stipulate the insurance contract
Indica l'obbligo di stipulare il contratto di assicurazione

Allocations of costs to Buyer/Seller

Incoterm 2010	Export customs declaration	Carriage to port of export	Unloading of truck in port of export	Loading on vessel in port of export	Carriage (Sea/Air) to port of import	Insurance	Unloading in port of import	Loading on truck in port of import	Carriage to place of destination	Import customs clearance	Import taxes
EXW	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
FCA	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
FAS	Seller	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
FOB	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer	Buyer
CPT	Seller	Seller	Seller	Seller	Seller	Buyer	Seller	Buyer/Seller	Seller	Buyer	Buyer
CFR(CNF)	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer/Seller	Buyer	Buyer	Buyer	Buyer
CIF	Seller	Seller	Seller	Seller	Seller	Seller	Buyer/Seller	Buyer	Buyer	Buyer	Buyer
CIP	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer/Seller	Seller	Buyer	Buyer
DAT	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer	Buyer	Buyer
DAP	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Buyer	Buyer
DDP	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller	Seller

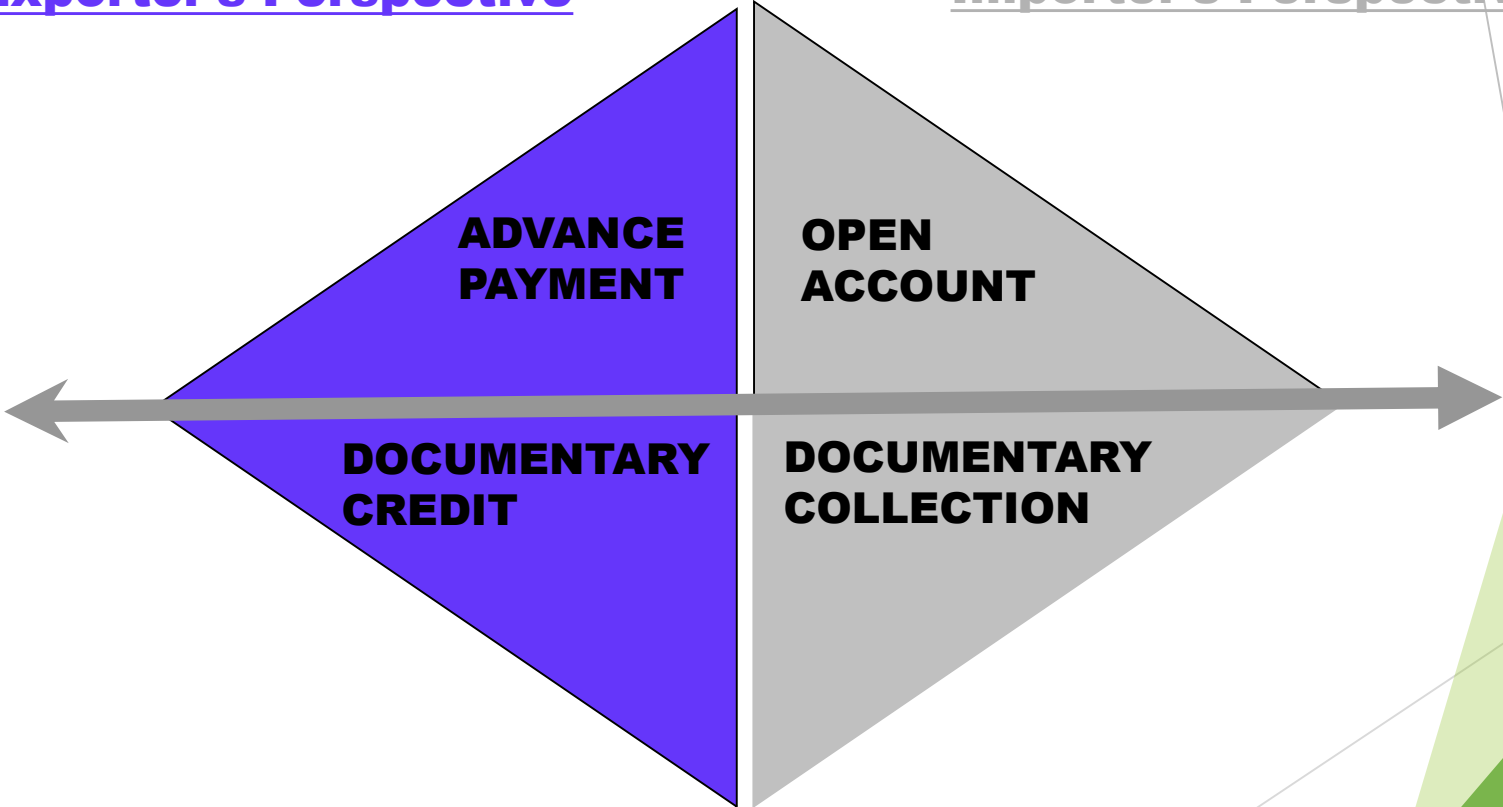
Payment cycle



International Trade Payment Methods

Exporter's Perspective

Importer's Perspective



Methods of Settlement

- ← Cash in advance:
- ← Buyer pays seller before receipt of the goods.
- ← Characteristics:
- ← Favourable to seller
- ← Buyer's absolute trust on seller

Methods of Settlement

- ← Open account:
 - ← Seller ships the goods and sends the documents directly to buyer.
 - ← Buyer pays seller at a future date.
- ← Characteristics:
 - ← Seller's absolute trust on buyer
 - ← No control over the goods by seller
 - ← Political and economical risk of the buyer's country

Methods of Settlement

- ← Collection:
- ← A payment mechanism in which a seller (drawer) uses a bank or banks as his agent for collecting payment from a buyer (drawee).
- ← Sight bill and usance/time bill
- ← Documents against payment (D/P)
- ← Documents against acceptance (D/A)
- ← Uniform Rules for Collections ICC Publication No. 522

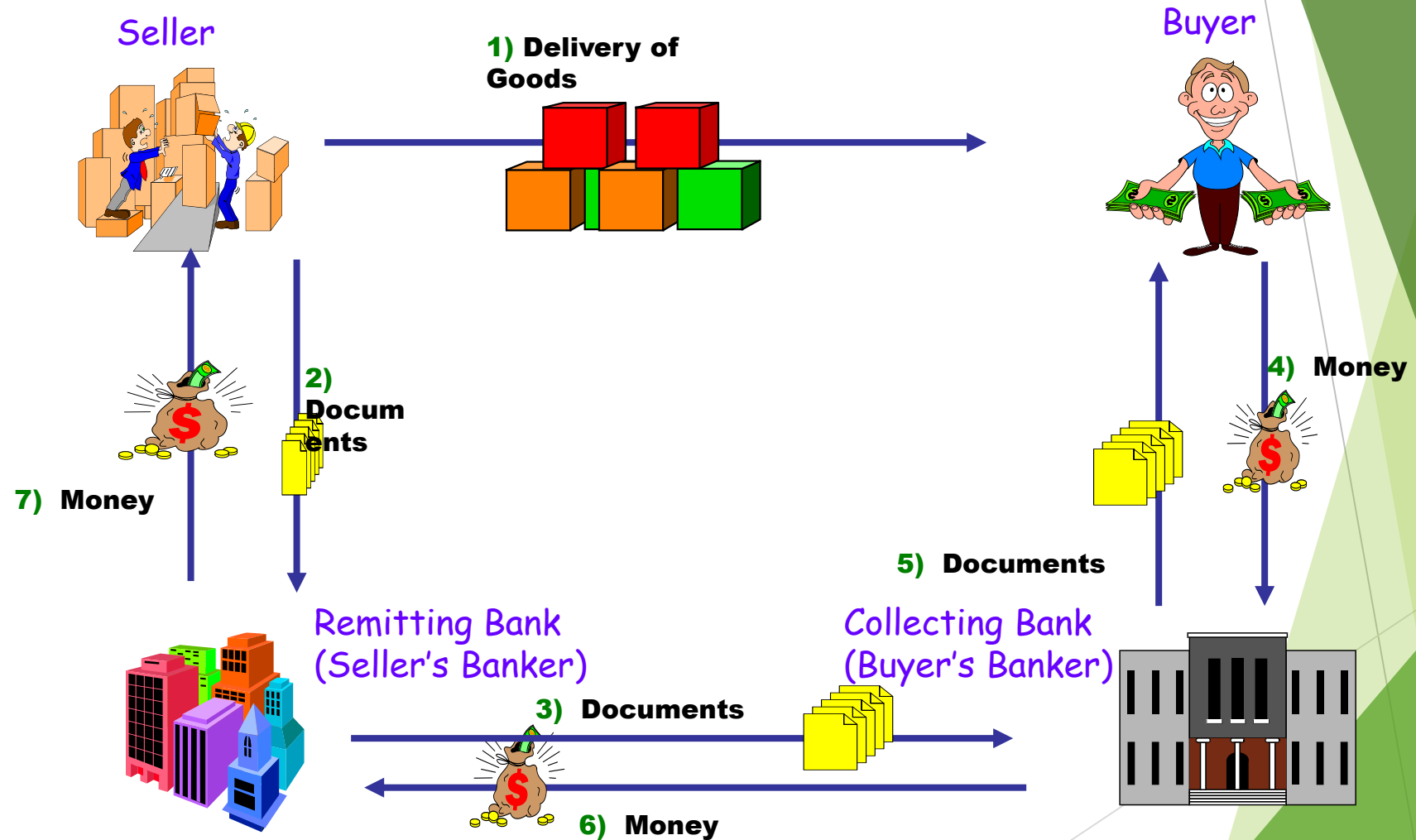
Collections under URC 522



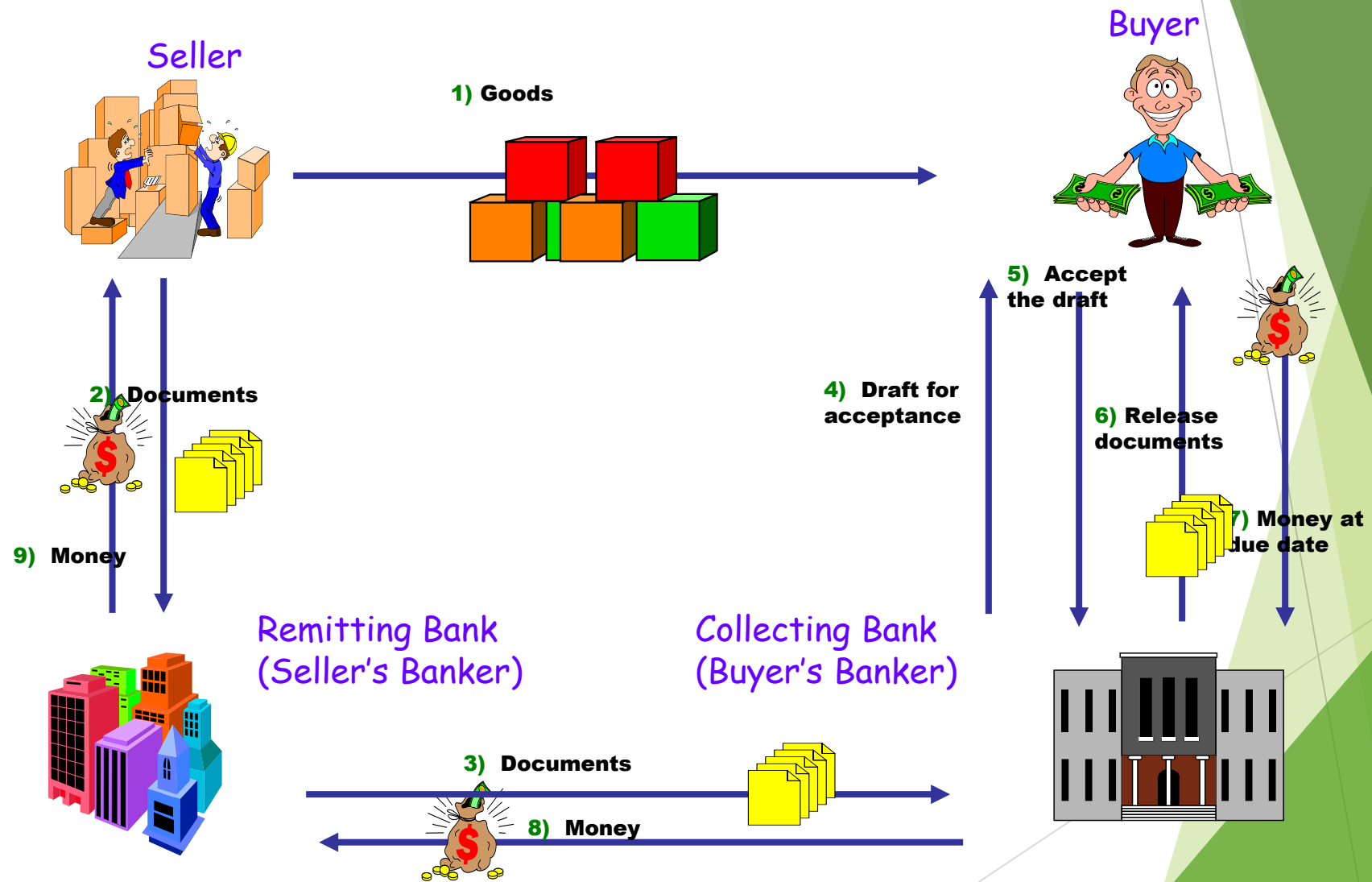
- **Documents Against Payment**
 - Release of documents to the buyer to take delivery of goods only upon receiving the whole sum of money from him

- **Documents Against Acceptance**
 - Release of documents to the buyer against his acceptance on the Bill of Exchange
 - Presentation of the accepted Bill of Exchange to the buyer for payment on maturity date

Payment Cycle for D/P Collection



Payment Cycle for D/A Collection



Collection

Risks Involved

- **To Buyer**
 - Goods shipped are not as contracted
 - Goods are perishable
 - No Control over documents presented

- **To Seller**
 - Buyer may be unable / unwilling to honour demand of payment
 - Buyer may extend payment terms and/or request for reduction

Letter of Credit

A definite undertaking issued by a Bank (the Issuing Bank) acting at the request and on the instructions of a customer (the Applicant) or on its own behalf,

- to make a payment to / or to the order of a third party (the beneficiary), or is to accept and pay bills of exchange (Drafts) drawn by the beneficiary; or
- to authorize another bank to effect such payment, or to accept and pay such bills of exchange (Drafts)
- to authorize another bank to negotiate, against stipulated documents, provided that the terms and conditions of the credit are complied with.

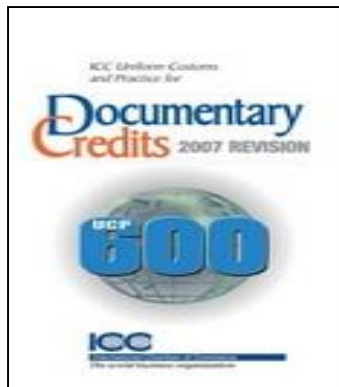
What is letter of credit (LC)?

Credit means:

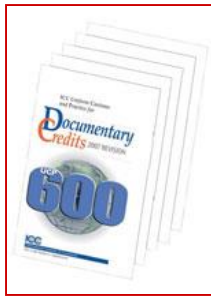
- Any arrangement, however named or described
 - That is irrevocable
 - And thereby constitutes the issuing bank's definite undertaking
 - To honour a complying presentation
- complying presentation means:
- A presentation
 - In accordance with the terms and conditions of the credit,
 - The applicable provisions of UCP 600,
 - And international standard banking practice

What is UCP 600?

- The Uniform Customs and Practice for Documentary Credits, 2007 Revision, ICC Publication No. 600
- Rules apply to LC that is issued subject thereto
- Binding on all parties to the LC unless expressly modified or excluded by the LC



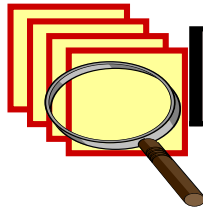
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UCP 600

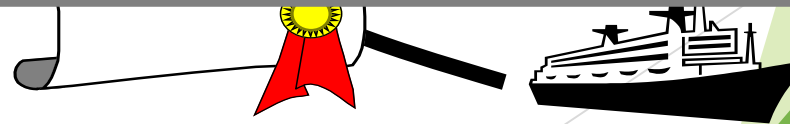
Article 34 Disclaimer on Effectiveness of Documents

A bank assumes no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document..... Or standing of the consignor, the carrier, the forwarder, the consignee or the insurer of the goods or any other person.



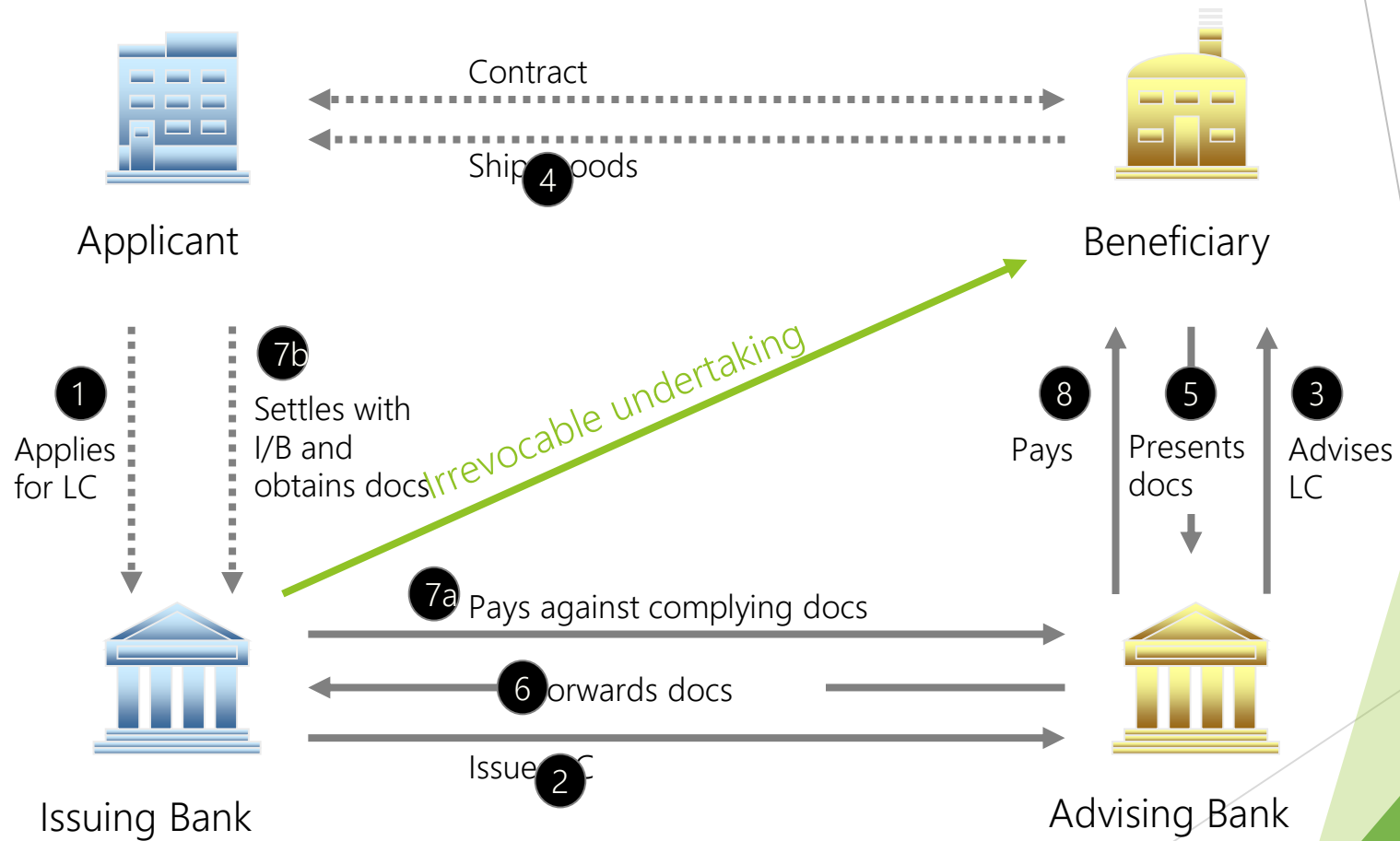
Article 5 Documents v. Goods, Services or Performance

Banks deal with documents and not with goods, services or performance to which the documents may relate.



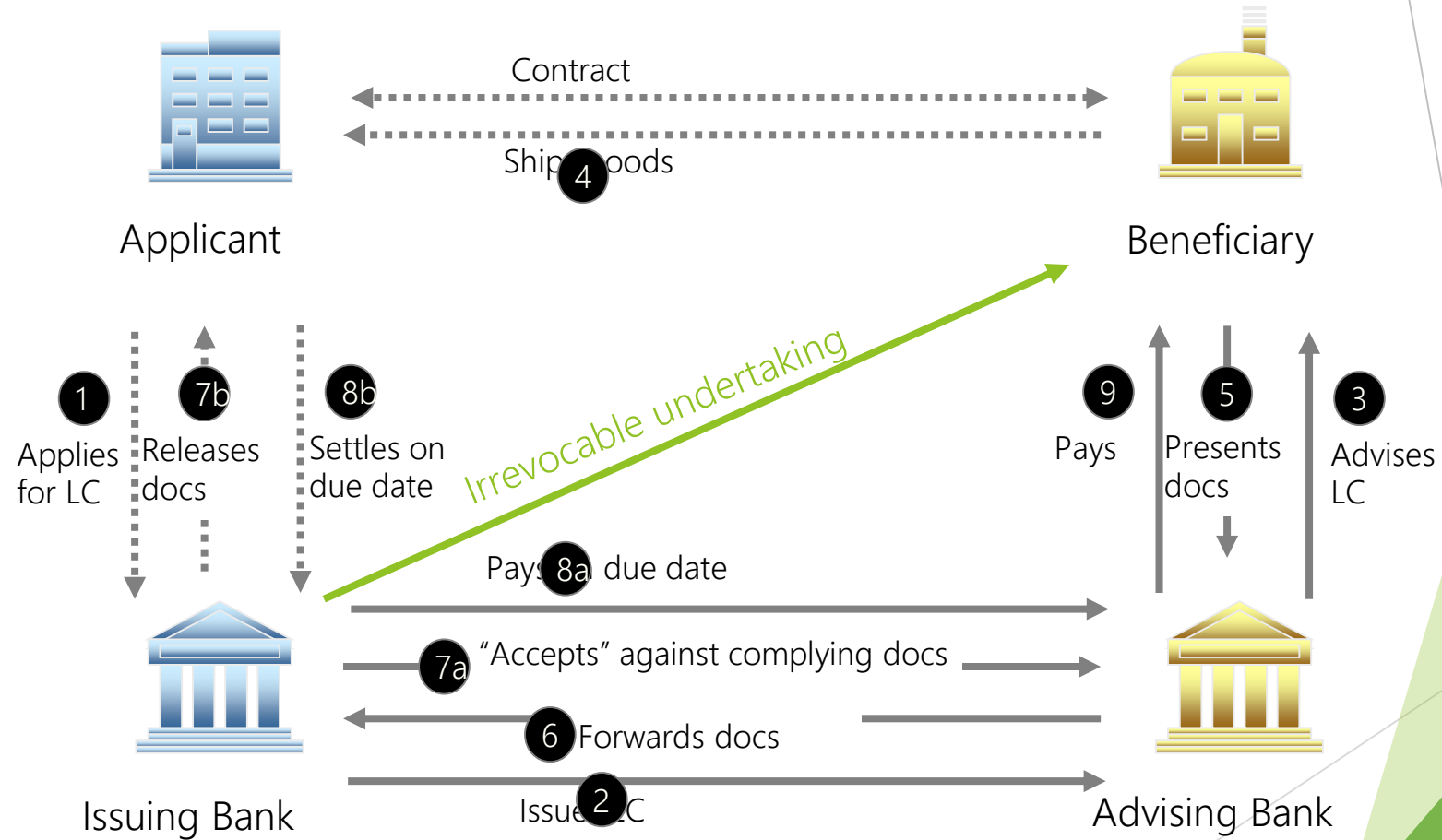
Sight LC

Payable promptly upon presentation of complying documents

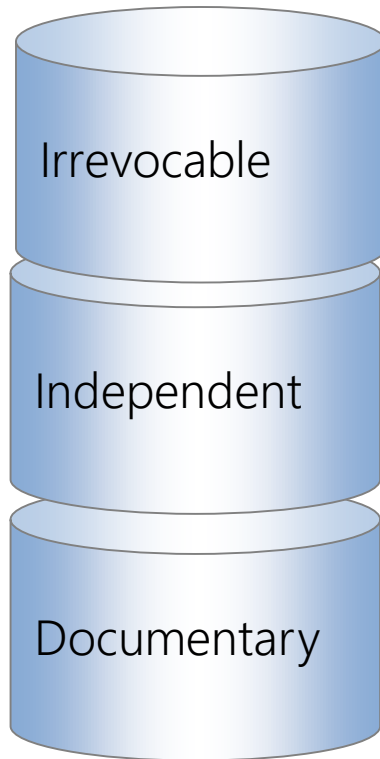


Usance LC

Payable on due date in accordance with the tenor



What make LCs valuable ...



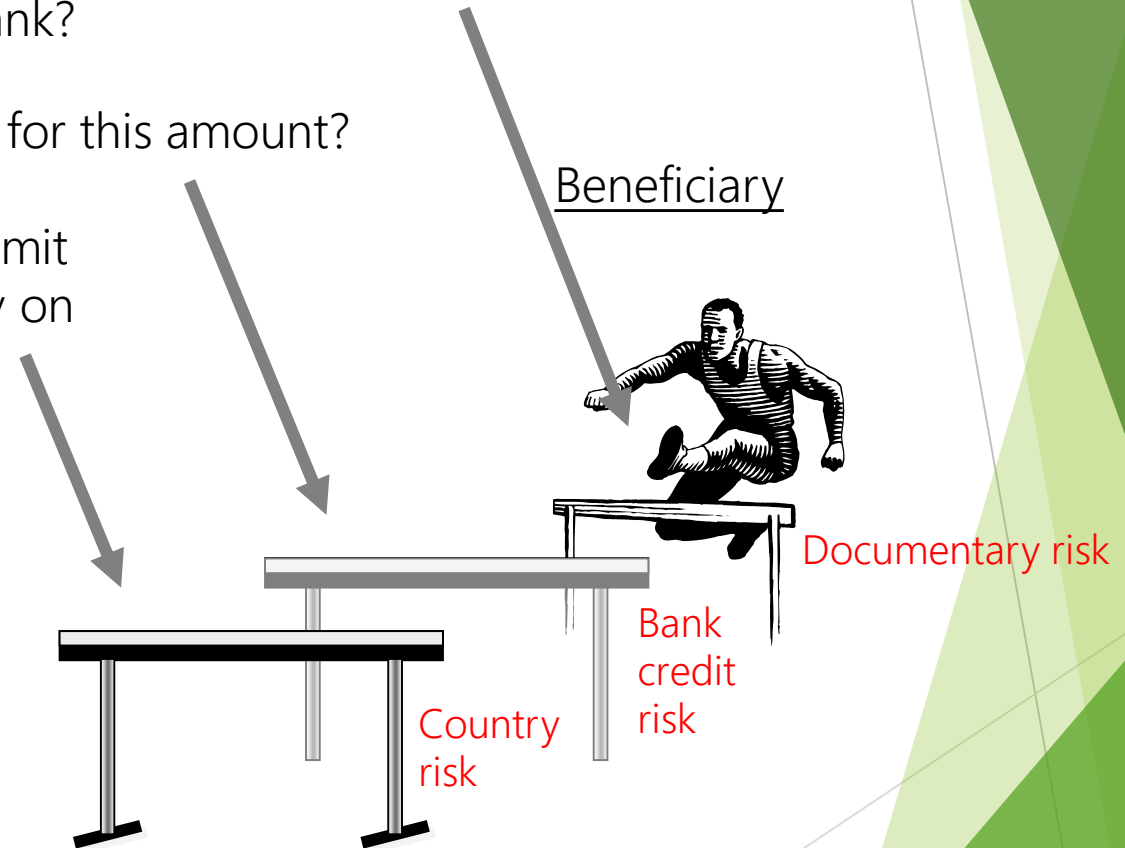
Once issued, an LC cannot be cancelled or amended unilaterally.

LC is separate transaction from the sales contract – banks are in no way concerned with, or bound by, such contract.

Banks deal with documents and not with goods, services or performance to which the documents may relate.

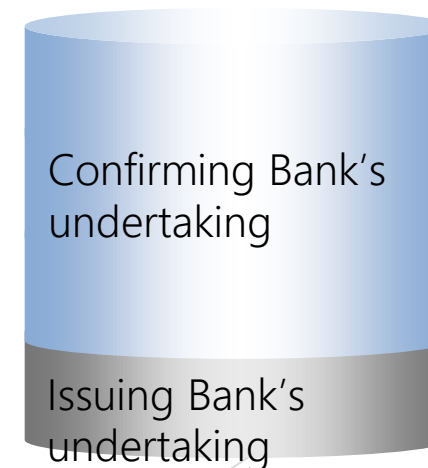
But LCs are not risk-free!

- Will compliant documents be presented under the LC to bind the issuing bank?
- Is the issuing bank good for this amount?
- Can the issuing bank remit payment in LC currency on due date?

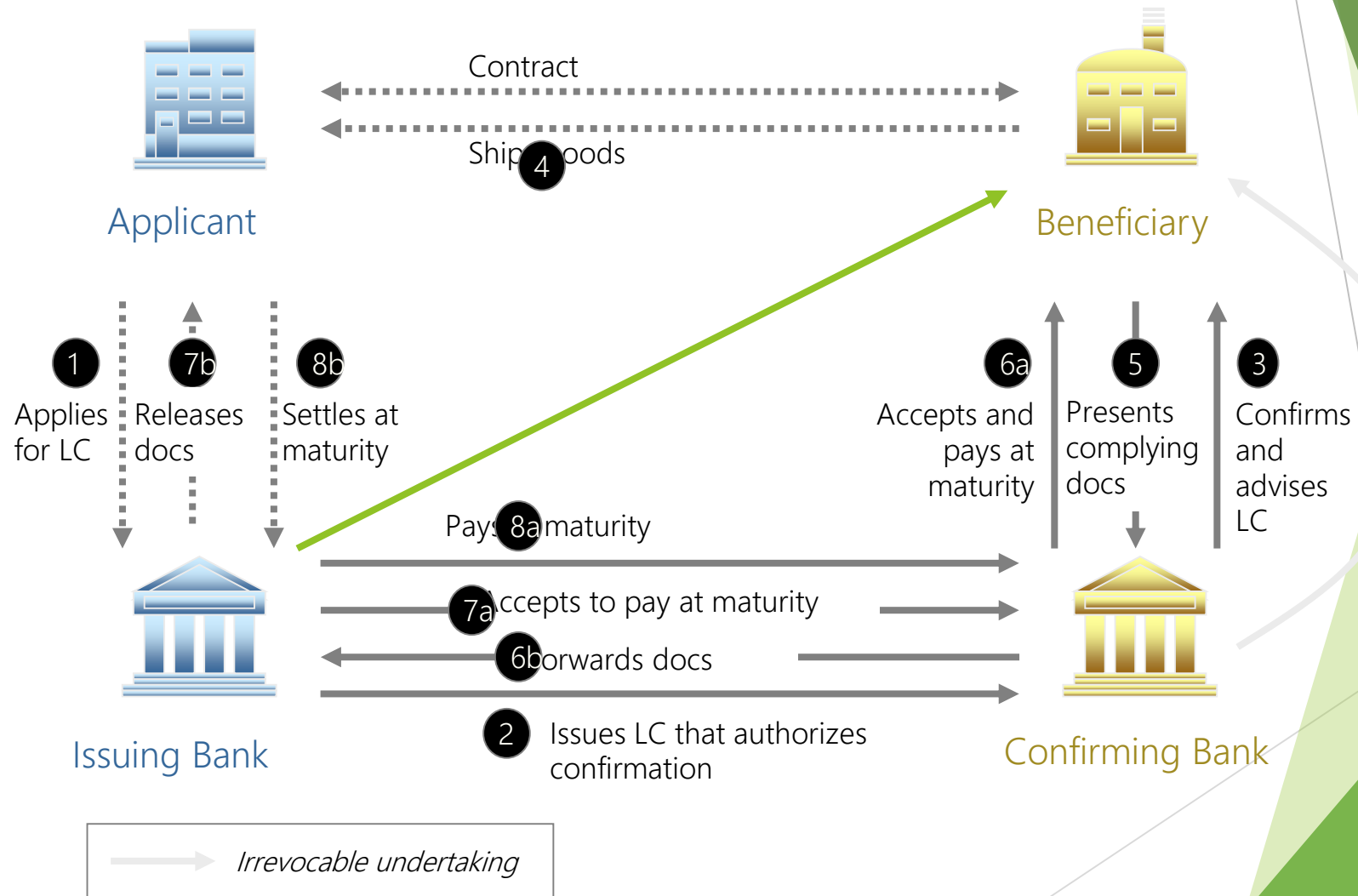


“Confirmation” for risk mitigation

- Confirmation: Definite undertaking of the confirming bank, in addition to that of the issuing bank.
- Confirming bank pays beneficiary against complying documents, regardless of whether it is reimbursed by issuing bank.
- Beneficiary is protected as of date of confirmation.



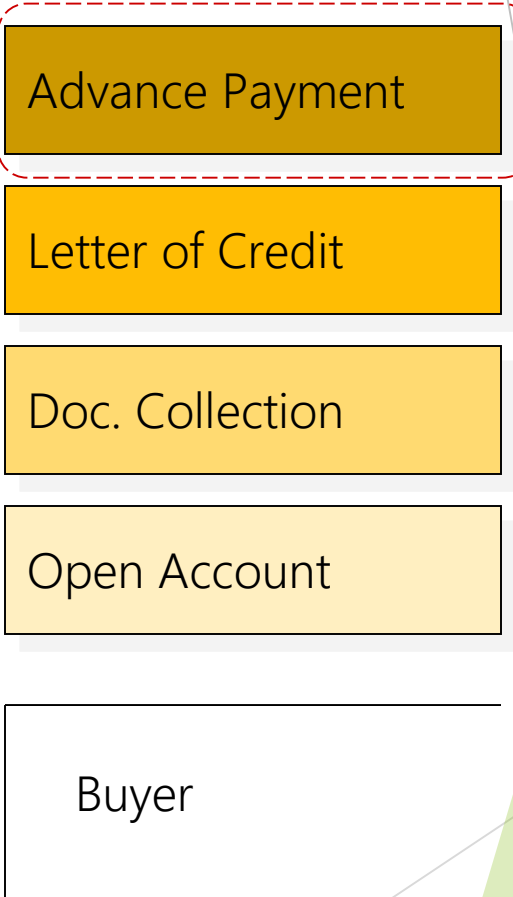
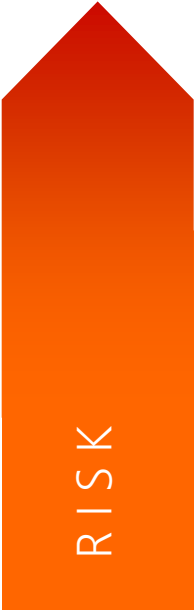
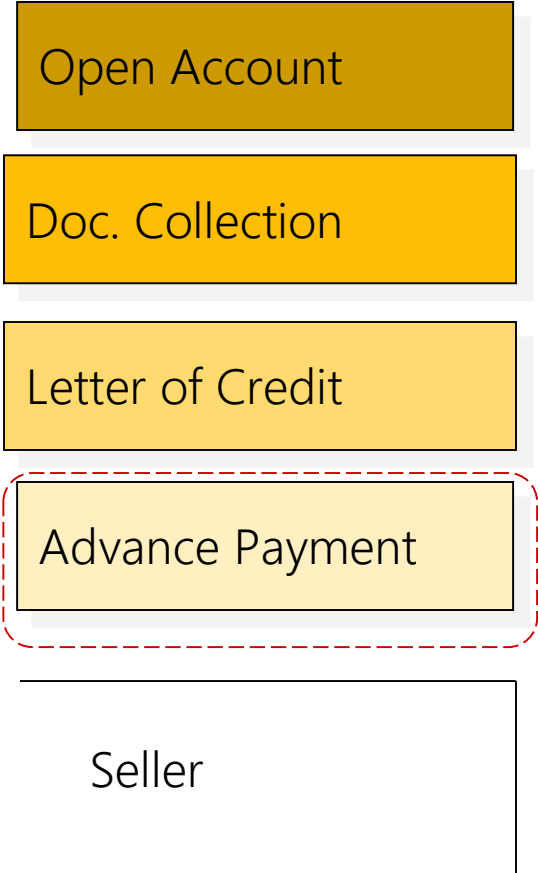
LC Confirmation: How it works



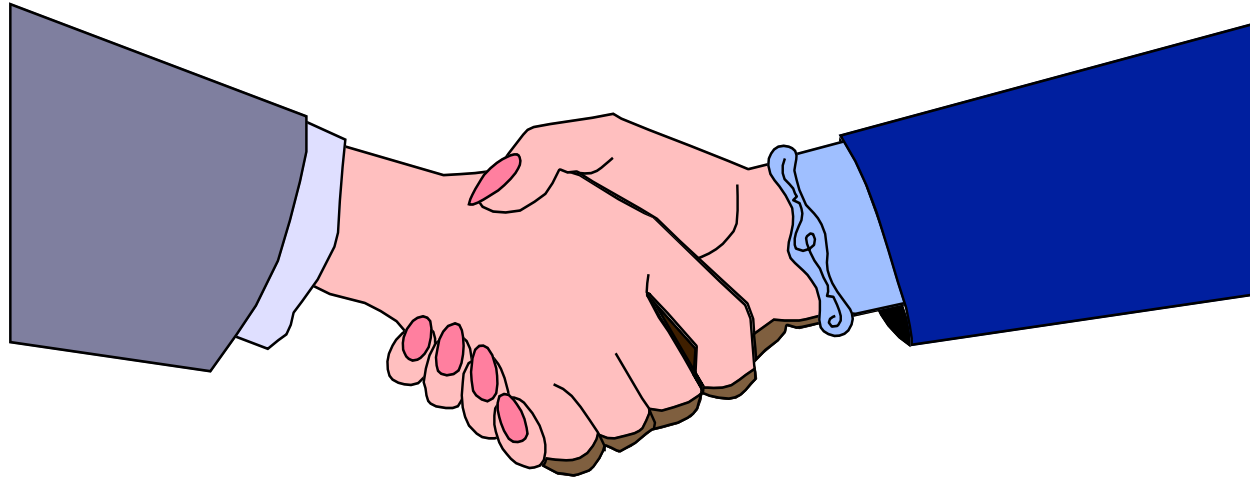
Silent Confirmation

- Confirmation of a credit is made by bank upon the authorization or request from the issuing bank.
- In order not to offend the buyer or issuing bank with a requirement that the credit must be confirmed, or perhaps also not to inconvenience the applicant with a request for an amendment to the credit, some banks are prepared to guarantee payment under the credit without the request of the issuing bank. This method is usually referred to as a “silent confirmation” or “without recourse negotiation”.
- It is important to note that it is not a confirmation in a technical sense of the word. A bank issuing a “silent confirmation” does not enjoy the protection under UCP 600.
- It is rather a kind of guarantee to pay provided that complying documents are presented. The scope of risks covered is exclusively regulated by the agreement entered into. For example, most banks do not want to cover documentary risks, therefore, they will only discount after the issuing bank has accepted the documents.

Conflicts in preference



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Thank You