Important documents to be attached with the claims are (i) certified copy of the export order (ii) certified copies of invoices (iii) certified copies of bills of lading (iv) copies of the correspondence with the buyer. All claims are paid in Indian rupees through the bank which handled the bills concerned. Small Exporters Policy has been introduced to encourage small exporters.

The ECGC provides guarantees to protect the banks from losses on account of their lendings to exporters. Six guarantees have been evolved for this purpose. These include (i) Packing Credit Guarantee, (ii) Export Production Finance Guarantee, (iii) Post- Shipment Export Credit Guarantee, (iv) Export Finance Guarantee, v) Export Performance Guarantee, (vi) Export Finance (Overseas Lending) Guarantee.

9.11 KEY WORDS

Buyer's Credit: A loan extended by a financial institution or a consortium of financial institutions to the buyer for financing a particular export contract.

Credit Limit: The limit upto which claim can be paid under the policy for losses on account of commercial risks.

Services Policy: Policy against rendering of services to foreign parties by Indian firms.

9.12 ANSWERS TO CHECK YOUR PROGRESS

A) 3 i) False ii) False iii) True iv) True v) False

B) 3 i) False ii) True iii) True iv) False v) False

4 24 Months ii) Credit Limit iii) Indian iv) Banks

9.13 TERMINAL QUESTIONS

1) Evaluate the services provided by the ECGC to the exporters.
2) How far has the ECGC helped the exporters in obtaining export finance?
3) Describe the different kinds of policies and financial guarantees issued by the ECGC.
4) "Credit is a major weapon of international competition but it involves risk." Discuss.
5) What is the nature of the risks faced by the international marketer in financing his operations and granting credit to his customers ? What are the means available in India to handle these risks ?

UNIT 10 IMPORT FINANCE

Structure

10.0 OBJECTIVES

After studying this unit, you should be able to:

- explain the nature and significance of import financing decisions
- describe the institutional regulatory framework of import financing
- discuss the exchange control regulations concerning imports.
- explain various methods of import financing

10.1 INTRODUCTION

Imports play an important role in the economy of every country, rich and poor alike. Rich countries need to import capital goods, raw materials and technology to ensure an optimum utilisation of their production capacity. They need to import a wide variety of consumer goods to enable their people to enjoy a high standard of living. Poor countries need to import technology and capital equipment and some time strategic raw materials to develop industries for accelerating pace of their development. In India, for example, the pace of industrial isation, level of exports and consequently the rate of economic growth is heavily dependent upon imports. A low level of imports usually indicates low purchasing power of its people and also emergence of recessionary trends in economy. At a firm's level efficient management of import operations is a critical factor in determining the overall profitability of its imports. Hence, a through understanding of import financing techniques and practices is necessary for concerned managers. In this unit, you will learn the regulatory framework and related exchange control mechanism of import financing and various methods of import financing.

10.2 IMPORT FINANCING

India followed a restricted import policy till mid eighties. Nothing could be imported without a licence involving cumbersome procedures alongwith intricate documentation. Although some liberalisation measures were taken in second half of eighties, real breakthrough came only in 1991.

Steady progress has been made in nineties in replacement of quantitative restrictions, licensing and discretionary control over imports by deregulation, simplification of procedures and protection through tariff and exchange rates. Export Import policies of 1992-97 and 1997-2002 were the steps in this direction.

It is against the background of nature and significance of India's import trade, one has to understand import financing methods and techniques. Import financing involves making payment to foreign entities for the goods purchased from them. From the management decision making viewpoint, it means making decision regarding terms of payment (i.e. choosing one among several alternatives), arranging funds, involving choice of financial institution and the instrument to be used for making payment and involving choice of intermediary, through whom the payment is to be made.

10.3 THE REGULATORY FRAME WORK

The principal objectives of India's Export Import Policy is to accelerate the country's transaction to an internationally oriented economy with a view to derive maximum benefit from the expanding global market. Various policy objectives are achieved basically through three legislations.

These are:

1. **Foreign Trade (Development & Regulation) Act, 1993** administered by Director General, Foreign Trade (DGFT) replacing the earlier legislation Import & Export (Control) Act, 1947, administered by the Chief Controller of Imports & Exports (CCIE).
2. **Foreign Exchange Management Act, 1999** administered by the Department of Economic Affairs, Ministry of Finance and the Exchange Control Development of the Reserve bank of India. FEMA has been brought is place of Foreign Exchange Regulation Act.
3. **Indian Customs and Excise Act, 1962** administered by Central Board of Excise and Customs.

The rules and operational procedures and changes relating to imports are framed by the Foreign Exchange Dealers Association of India (FEDAI). In addition, Uniform Customs & Practice for Documentary Credit (UPDC) formulated by International Chamber of Commerce, Paris which has a global acceptance, is indispensible to cover transactions under documentary credits.

India's import policy is formulated within the framework of obligations of the membership of World Trade Organisation (WTO). Hence, the policy does not have a discriminatory and restrictive dimension. Whatever restrictions on imports continue are the ones which have been allowed under the WTO regime. In line with WTO provisions for according preferential treatment of imports from developing countries, India has signed several preferential treading arrangement with some South Asian Countries and the products which will attract concessional rate of duty are also specified.

Physical control over imports is exercised by DGFT and the Customs Deptt. RBI exercise financial controls through the guidelines provided to authorised dealers. Of late, tariffs rather than quantitative restrictions are being used to regulate import trade.

Under the present policy, all goods, except those appearing on Negative list can be freely imported in India. For goods included in the restricted, or banned list, import licence may be issued by the Director General of Foreign Trade. An import licence is an authorisation which includes a customs clearance permit (CCP) indicating *inter alia*, quantity description and value of the goods, actual user conditions if any, the minimum export value if any, export obligation, if any, and value addition obligation, if any. Import licences which are issued on C.I.F. basis, is given in duplicate viz. Customs Copy (for clearance from customs) and Exchange Control copy for remittances.

For exporting units, certain special facilities have been provided under the present policy. Under the Export Promotion Capital goods (EPCG) Scheme, capital goods can be imported at a concessional rate of custom duty, subject to an export obligation to be fulfilled within a specified period of 5-8 years. Under the Duty Exemption Scheme, the government permits import of raw materials, intermediates, components, consumables, spare parts, accessories, packing materials and computer software required for direct use in the product to be exported duty free under different categories of licences. Advance licence is issued for inputs needed for export production. It can be issued for physical exports, intermediate supply and deemed exports.

10.4 EXCHANGE CONTROL REGULATIONS CONCERNING IMPORTS

Exchange control regulations refer to rules and regulations framed and administered by the Reserve bank of India (RBI) under the provisions of Foreign Exchange Management Act, 1999. These regulations aim at pooling resources for national development in the best interest of the country. Under the provisions of the Act, RBI regulates sale and purchase of foreign currencies, Commercial banks with a licence to deal in foreign currencies, called authorised dealers (ADs) buy and sell foreign currencies in accordance with the guidance provided by the RBI. Let us learn various regulations regarding payment of imports.

Mode of Payment: Exchange control regulations govern sales of foreign currencies to non-residents against import of goods from any country except - Nepal and Bhutan. It may be pointed out that residents of these two countries are residents for the purposes of exchange control regulations, hence, ADs cannot sell any foreign exchange for financing imports from these two countries.

Under the existing regulations, ADs provide foreign currencies to importers:

i) for remittance to foreign supplies as advance payments.

ii) Paying the foreign supplies in compliance of their undertaking under the letter of credit.

iii) discounting on purchasing except documents.

iv) advances against shipping documents.

Authorised dealers can open a letter of credit (L/C) to facilitate imports, subject to following regulations:

a) Letters of credit may be opened by banks only on behalf of their customers who maintain account with them.

b) L/C should be opened in favour of overseas suppliers of shipper of goods.

c) Application for L/C must be accompanied by sale contract and other documentary evidence relating to the order and its confirmation and import licence, if any.

Authorised dealers have been permitted to sell foreign currencies for making payment towards imports into India. For this purpose, importers have to submit an application in form A giving the necessary details including classification of goods based on Harmonized system. It is also obligatory on the part of an importer to submit exchange control copy of customs bill of entry to the authorised dealer through whom the relative remittance was made as evidence that the relative goods for which the payment was made have actually been imported into India within three months from the date of remittance.

In respect of imports by post parcel, postal wrappers are required to be submitted as documentary evidence in support of imports into India.

Currency of Payment: According to exchange control regulations, payment for imports should be made in a currency appropriate to the country or through an account appropriate to the country of origin of goods irrespective of the country from where they are shipped or supplied. RBI has given a list of permitted currencies and approved methods of payment for imports in Exchange Control Manual for guidance of importers.

Time limit for settlement of imports bills: Time limit for settlement of import bill is 6 months from the date of shipment, but authorised dealers can settle without reference to RBI even if the period of six months has expired, provided the AD is satisfied about the bonafides of the circumstances.

Check Your Progress A

1) What is import financing ?

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2) What do you mean by import licence?

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3) What is advance licence?

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4) State whether following statements are **True** or **False**.

i) Time limit for settlement of import bill is 6 months from the date of shipment.

ii) Uniform Customs and Practice for Documentary Credit is not indispensible to cover transactions under documentary credit.

iii) Import licences are issued on CIF basis.

iv) Authorised dealers can sell foreign exchange for financing imports from Bhutan.

v) Payment of import should be made in a currency appropriate to the country.

10.5 METHODS OF IMPORT FINANCE

The methods of import financing include: financing under L/C, financing against bills under collection, financing against deferred payment, financing under foreign credit and finance by EXIM Bank of India. Let us discuss them in detail.

10.5.1 Financing Import Under Letter of Credit

Letter of credit can be defined as a commitment of bank to pay the seller of goods or services a certain amount provided he presents stipulated documents evidencing the shipment of goods or the performance of services within a prescribed period of time. As a credit instrument and as a means of making and securing payment, the letter of credit is an essential instrument for conducting world trade today. It fulfils all the requirements provided the conditions regarding its use are stated in clear and unambiguous terms.

Import letters of credit financing involves three principal stages:

i) Requesting bank to open a letter of credit

ii) Retiring documents under letter of credit

iii) Import Trust receipt facility.

Each time a L/C is opened, the importers has to file a formal stamped "Letter of credit application and Agreement" in the prescribed form. The application should set forth the precise terms and conditions under which the importer wishes his bank to establish the credit, and describe the documents covering the goods purchased which the bank is to receive in exchange for payments.

As the correct opening of the credit is the first essential to the ultimate success of the transaction and as the L/C will.be issued on the basis of information supplied by the importer in the L/C application, it is absolutely necessary that the information supplied by him must be complete and precise. After due scrutiny of the application form, the relevant letters are issued by the bankers subject to the Uniform Customs And Practice for Documentary Credits, in order to guard against confusion and misunderstanding.

Letters of credit may be opened by mail or Fax depending upon the urgency of the situation. It may be revocable or irrevocable. Irrevocable L/C implies that the terms and conditions of the credit can be amended only with the consent of all the concerned parties. At times, the importer may ask the issuing bank to get the credit confirmed by another bank. It means that in addition to the issuing bank (the confirming bank) assumes the commitment to pay provided the terms of the credit are fulfilled.

L/C is sent by the issuing bank to a bank in the suppliers country with a request to deliver the same to the supplier, called the beneficiary. If the beneficiary is satisfied with terms and conditions mentioned in L/C he ships the goods, obtains the required documents and submits them to bank, usually his own, unless a name has been specified in the credit. Bank scrutinises the documents and if he finds them in conformity with the L/C and the reimbursement instructions, he pays the suppliers. Thereafter he sends the documents to the issuing banker who again scrutinises the documents with references to the terms of the credit. If he is satisfied, he pays the negotiating banker.

After paying the negotiating banker the issuing banker releases documents of title to the importer on his executing a stamped Letter of Trust (Trust Receipt). It means that the importer undertakes to deposit with the bank the sale proceeds immediately on relisation but in no case later then period stipulated in the trust letter. The import trust receipt facility is given by the banks to first class customers only.

Bankers also grant import loans to their approved customers and undertake the clearance of goods on their behalf. In such cases, the bills received under letter of credit are retired to debit of loan account of the customer by the bank and the relative documents forwarded to an approved clearing agents for clearance of goods. After the goods are cleared, despatched and Railway Receipts sent to the bank, the relative goods or Railway Receipts are delivered to the importer after receiving the due amount. Where arrangements exist, the goods may be stored in the bank godown under bank's lock and released against proportionate payments as and when desired by the importer.

10.5.2 Financing against Bills under Collection

In the case of imports not covered by letters of credit, the documents are forwarded by a bank in the supplier's country, known as the collecting bank, for collection of proceeds from the importer and payment to the supplier through the remitting bank. In such cases, the collecting bank would examine the documents and the instructions stated in the covering schedule to ensure that all the stated documents have been received intact and the bill of lading and the bill of exchange are endorsed in its favour or blank endorsed to enable the bank to handle the documents. The bank than presents the documents to the importer on payment (in case of sight or D/P Bill) or against written acceptance (in case of usance or D/A bill). Where the importer is eligible to receive the documents only on payment, he can avail an import loan or a trust receipt facility, as discussed before. Obligations of various parties involved are provided in Uniform Rules for Collection (URC) Publication No. 322 issued by International Chamber of Commerce, Paris.

Sometimes, shipping documents may be sent by the exporter directly to his importer. In such a case, the bank may receive clean bills for collection of proceeds. In such cases, banks are required to call for documentary evidence of imports such as custom noted invoice, exchange control copy of bill of entry and import licence, if any.

Payment for bills in respect of imports through post can also be arranged through a bank. In such cases, the relative postal receipts must be produced as evidence of shipment through post and an undertaking to submit postal wrappers within three months from the date of wrappers.

10.5.3 Financing Imports against Deferred Payment

Imports under deferred payment implies that the supplier has agreed to supply goods on credit terms extending beyond six months. In such cases, authorised dealer has to refer each deferred payment case to RBI for prior approval of advance payment, bank guarantee and instalments (principal and interest) with documents viz. exchange control copy of import licence, if any, contract copy and statement of desired facilities.

Appraisal for issue of guarantees or loans is similar to term finance. For importing under deferred payment, the importer should have sufficient cash generated to pay the due instalments. He should arrange for payment of advance and down payments from his own resources which would cover bank's margin requirement. Imported machinery has to be hypothecated to the bank and the importer should counter guarantee the transaction.

10.5.4 Financing under Foreign Credit

Government of India gets assistance in the form of loans and development credits from international financial institutions as also foreign governments. These loans are of two types - tied loans and loans in free foreign currencies. Terms and conditions of each loan along with detailed instructions regarding the procedure to be followed for opening letters of credit, submission of documents etc. are set out in public notices issued by DGFT. RBI also issues circulars for each foreign credit giving important instructions relating to such imports.

Payment under foreign credit may be made under (a) letter of commitment method or (b) reimbursement method. Under the letter of commitment procedure, remittances from India for the relative imports are not permitted. The importer in India obtains a letter of commitment from the Government of India after furnishing a bank guarantee for payment of rupee equivalent of the import value. The importer furnishes the letter of commitment to the bank opening L/C. Then the usual procedure follows. The shipping documents are delivered to the importer on payment / acceptance. Where no L/C is opened at all and on receipt of document covering imports rupee deposits are made to Government account by the importer through the bank.

Under the reimbursement method, the aid giving the country makes available to the Government of India on production of evidence of payment of imports. Hence, payment to the suppliers is made by the L/C opening bank through the normal banking channels and reimbursement is by the Government of India by submitting the required documents.

10.5.5 Import Loans by Export-Import Bank of India

Bank finances imports from third countries required for executing projects overseas for which contracts have been won by Indian exporters.

Regarding imports into India, Exim Bank finances such imports which are export-related, i.e. imports by Export Oriented Units, import of computer systems for development and export of software, import of plant, machinery, technology for upgradation/expansion of production capability for export markets.

Exim Bank also finances bulk imports of consumable inputs and canalized items. Under this scheme, promissory notes drawn in favour of commercial banks by their importer borrowers are discounted, Exim bank will issue letter of commitment for finance on request from commercial bank indicating its requirement. The quantum of finance depends on the condition that import order should not be less than Rupees one Crore.

Check Your Progress B

1) What do you mean by letter of credit?

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2) What is Trust receipt?

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3) What do you mean by deferred Payment?

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4) State whether the following statements are **True** or **False**.

i) Letter of credit can not be opened by mail.

ii) After paying the negotiating bankers, the issuing bankers release documents of title to the importer on executing a stamped letter of Trust.

iii) When shipping documents are directly sent to importer by exporter, the bank receives clean bills for collection of proceeds.

iv) For importing under deferred payment, the importer need not generate cash for advance and down payments.

v) Government of India gets assistance in the form of loans and development credits from International Financial Institutions.

10.6 LET US SUM UP

Imports play an important role in economy of every country - rich and poor a like. Their role in India is particularly crucial in view of country's continued dependence of foreign capital and technology. Hence, it is necessary to ensure that import operations at firm's level also are managed efficiently. Significant changes in India's import policy aiming at removing bottle-necks on account of red tape and lengthy documentation have taken place in recent years.

Import financing means making decisions regarding term of payment (choosing one among several alternatives) arranging funds, involving choice of financial institution and the instrument through which the payment is to be made. The choice is conditioned by regulatory framework concerning imports and availability of foreign currencies.

In India, Foreign Trade (Development and Regulation) Act 1993, Foreign Exchange Management Act 1999 and Indian Customs and Excise Act 1962 are the three legislations constituting the regulatory framework. While Foreign Trade (Development & Regulation) Act and Indian Customs & Excise Act regulate the physical importation, Foreign Exchange Regulation Act regulates remittances on account of payment for imports. As a result of liberalisation in foreign trade sector, import licensing has been abolished and import licences are needed only for terms included in the negative list on imports at concessional rates of import duty. Exchange control regulations have prescribed requirements regarding mode of payment, currencies to be used and the period within the payments for imports have to be paid.

Imports can be financed in several ways. Importer can request his banker to open a letter of credit in favour of his supplier. Under the system supplier gets paid immediately upon submission of specified documents to the bank. Importer obtains release of these documents either upon payment or debit to his loan account. He can ask the supplier to send the documents to the banker. Whom he instructs to make payment by debiting his account. Importer gets a loan either on Trust Receipt or hypothecation of imported goods to pay for the imports. Where an importer contracts to pay instalments, permission of RBI needs to be taken. He can obtain a loan from the bank to pay for the instalment. Imports under credit extended International Financial Institutions and foreign Governments can be financed either through commitment (i.e. Government of India commits a part of loan to the importer and gets paid in Indian rupees) or reimbursement method i.e. after paying the supplier, the bank gets reimbursed by loan giving agency. Export Import Bank of India lends to importers to finance their export related imports.

10.7 KEY WORDS

World Trade Organisation (WTO): A voluntary organisation through which groups of countries negotiate trading agreements and which has authority to oversee trade disputes among countries.

Bill of Exchange: An unconditional order in writing - signed by a person, usually the exporter, and addressed to the importer - ordering the importer or the importer's agent to pay on demand (sight draft) or a fixed future date (time on usance draft), the amount specified on its face.

Letter of Credit: A letter addressed to seller, written and signed by a bank acting on behalf of the buyer, in which the bank promises to honour drafts drawn on itself if the seller conforms to the specific conditions contained in the letter.

Issuing Banker: Under the letter of credit arrangements, a bank who, acting on behalf of the buyer writes and signs the letter sent to the seller.

Negotiating Banker: Under the letter of credit, the bank who pays the supplier for the goods supplied to the importer, (the applicant for the credit) after scrutinizing the documents to ensure their conformity with the provisions of the credit.

Document Against Payment: refer to the terms, which implies that the buyer agrees to pay for his purchases immediately after presentation of documents.

Documents Against Acceptance: means that the exporter has agreed to receive payments for goods supplied by him at a fixed future date. Under the system, the buyer receives the shipping documents on accepting the bill (meaning thereby undertaking to pay at a fixed future date).

Duty Exemption Scheme: Under the scheme, importers are issued, licence for enabling to get their goods cleared to the customs without paying the import duty.

Bill of Entry: A document to be signed by the importer or his agent for getting the goods cleared from customs.

10.8 ANSWERS TO CHECK YOUR PROGRESS

A 4 i) True	ii) False	iii) True	iv) False	v) True
B 4 i) False	ii) True	iii) True	iv) False	v) True

10.9 TERMINAL QUESTIONS

1. What is importing financing? Describe the regulatory framework related to import financing.
2. Explain various exchange control regulations concerning imports.
3. Enumerate the methods of import finance. Describe the procedure of financing import under letter of credit.
4. Explain various methods of import finance alongwith the documentation procedure.
5. Write notes on:
   i) Financing against bill under collection
   ii) Financing under foreign currency
   iii) Import loan by Exim Bank of India
   iv) Financing under deferred payment arrangement

SOME USEFUL BOOKS

Bare Act, Foreign Exchange Management Act, 1999, New Delhi.

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