UNIT 6 TERMS OF PAYMENT

Structure

6.0 OBJECTIVES

After studying this unit, you should be able to:

- explain various methods of payment in export business
- discuss the implications in terms of risks and time under various methods
- describe various types of letter of credit
- explain the documentation and related procedures covering realisation of export proceeds under various terms.

6.1 INTRODUCTION

You have learnt the regulatory framework of export import trade, the export sales contract, various aspects of export import documentation, the electronic data interchange system and processing of an export order in Block 1. In international trade today, the competition is no longer confined to price, quality or delivery schedule but extends to terms of payments. The terms of payment are often decisive in obtaining an order. In this unit, you will learn various methods of payment in export business. You will also be acquainted with the documentation and related procedures regarding realisation of export proceeds.

6.2 TERMS OF PAYMENT

The terms of payment play a very important role in export business. The terms are instrumental in attracting foreign buyers and thus expanding the export business. Many exporters are able to clinch an order on the basis of attractive payment terms, even though they may not be competitive from the viewpoint of price or quality. Payment terms are determined by a host of factors, such as exchange control regulations, trade practices, financial position of buyers and above all bargaining strength of the trading partners. In India, exchange control regulations play an important role in this regard. According to these regulations, the amount representing the full export value of the goods exported to all countries, other than Bhutan and Nepal, must be realised within six months from the date of shipment. Any deviation from the rule will require the Reserve Bank's prior approval. There are four methods of receiving payments from the overseas buyers. These methods carry risks of varying nature. Hence, the choice depends largely on the bargaining strength of the trading partners. Let us discuss various methods of receiving payments in detail.

6.3 ADVANCE PAYMENT

In this method, the payment is made either at the time of acceptance of the order, or at the same time before the shipment. This is the safest and ideal method from the exporter's side. In most cases, however, this method is not likely to be favoured by the buyer, the buyer may favour this method when he is an overseas affiliate of the exporter, or urgently requires the goods and the exporter is in a position to dictate his terms. The buyer may make remittance by: (a) purchasing a draft from the bank payable at a bank in India and despatching it to the exporter, or (b) arranging through his bank for a bank in India to be instructed by mail or capable to pay the exporter (i.e., by mail transfer or telegraphic transfer). The draft, mail or telegraphic transfer will be in the currency specified in the contract of sale.

From the exporter's point of view, it is not only the simplest method but also free from any kind of credit or transfer risks. Payment is received before the shipment, and hence there is no need for prior post - shipment finance of any kind. And as no interest or commission is charged by Indian banks for payment of clean remittances, it works out to be the cheapest method as well. However, in case the exporter has quoted in a foreign currency, an exchange risk exists from the date of contract until payment is received from the buyer.

6.4 DOCUMENTARY CREDIT

Where an exporter is unable to procure order with advance payment, the next best alternative is the documentary credit method. In this method at the instance of importer, bank usually in the importing country sends a letter to the exporter giving an assurance or an undertaking that the payment will be made soon after shipment. In order to ensure that the exporter complies with the agreed terms and conditions of sales contract, the letter from the bank stipulates submission of certain documents. As credit is given to the exporter on the basis of documents, the methods is referred to as a system of payments through documentary credits.

According to the Uniform Customs and Practices relating to Documentary Credits (UCP), documentary credit has been defined as 'any arrangement whereby a bank acting at the request and in accordance with the instructions of a customer (the importer) undertakes to make payment to or to the order of a third party (the exporter) against stipulated documents and compliance with stipulated terms and conditions.

Payment through documentary credits have become popular because the mechanism therein reconciles the conflicting interest of buyers and sellers. In this method, a bank gives an undertaking to the importer that he will make payment to the exporter only after he has ensured compliance with stipulated terms and conditions. At the same time, he also gives an undertaking to the exporter that payment will be made as soon as documents evidencing compliance with stipulated terms and conditions are submitted.

6.4.1 Parties in Documentary Credits

There are several parties involved in the documentary credit arrangement. Let us discuss them in detail.

Firstly, it is the importer, who is referred to as **an applicant** in terms of UCP, who initiates the process. Having agreed to buy under such arrangements, he approaches his bankers and requests him to issue a documentary letter of credit in the name of the exporter. While requesting the banker, he mentions the documents to be submitted by the exporter in compliance of the terms and conditions stipulated in the sales contract.

Secondly, the banker who issues the letter of credit to the exporter, is referred to as the **opening or issuing banker**. It is the issuing banker who, at the request of and on the instructions of a customer (the applicant for the credit) undertakes to pay the exporter.

Thirdly, the banker to whom the letter of credit is sent for authentication and delivery is referred to as **advising banker**. According to Article 8 of the UCP, 'advising bank shall take reasonable care to check authenticity of the credit which advises'. **Fourthly**, a banker, who adds his confirmation to the credit is called a **confirming banker**. Confirmation of credit implies an undertaking to pay to the beneficiary in the event of issuing banker's inability or refusal to pay. Confirmation can be added only at the instance of the issuing bank. Usually, the advising and the confirming bankers are one and the same.

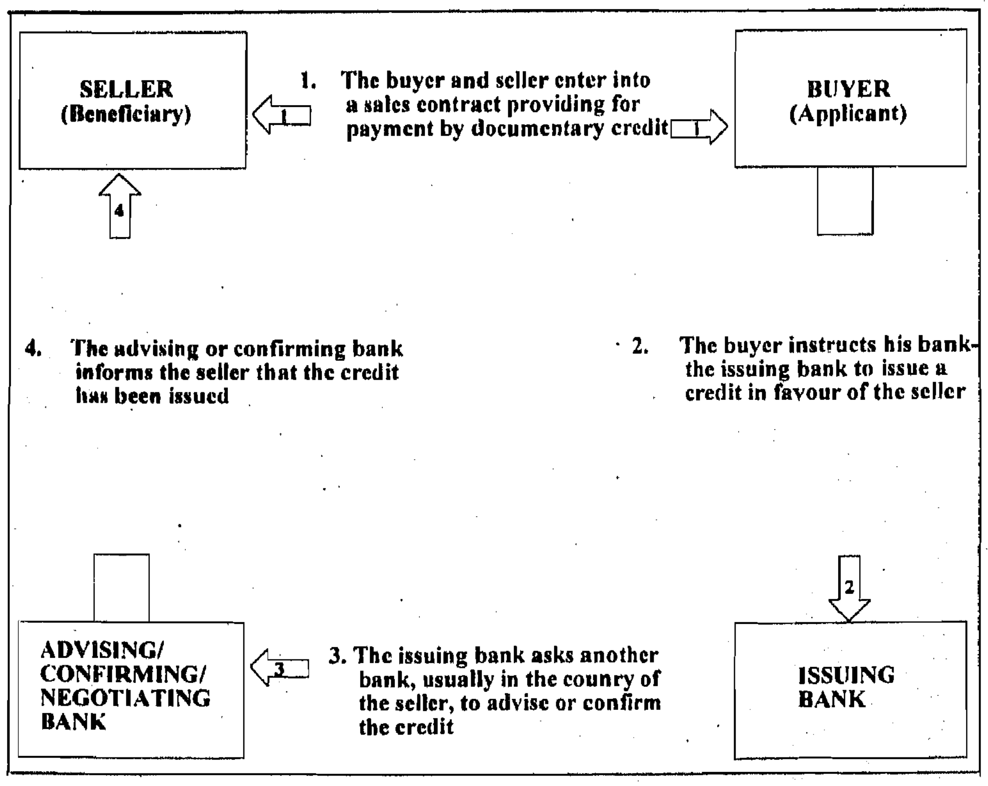
Fifthly, where a credit provides for bills of exchange, the **paying bank** is the bank on which such bills are drawn. This may be the issuing bank, or another bank (either in the country of the beneficiary, or in a large financial centre such as London or New York). If the credit provides for bills to be drawn on the buyer, the issuing bank is the paying bank.

Sixthly, where the paying bank is not located in the exporter's country, credits usually permit a bank or bankers in the beneficiary's country to negotiate drawings under the credit and disburse the amount of the exporter. This banker is called a **negotiating bank**. Negotiating bank must present the relative bill of exchange to the paying bank, and until that bank pays the bill the drawing is not finalised.

Finally, the exporter who concludes the contract with the importer providing for payment under the documentary credit arrangement is called **beneficiary**.

Hence, in any documentary credit, there can be at least four parties, viz., the applicant, the issuing banker, the beneficiary and the advising, confirming and negotiating banker rolled into one.

Figure 6.1: Relationship among the parties to the Letter of Credit



6.4.2 Details included in Letters of Credit

The documentary credit gives the following particulars, though, the form and order vary among banks:

1) Name of the issuing bank,and type of credit with number and date
2) On whose behalf the credit is issued (the applicant / buyer)
3) The amount (including the currency)
4) The date upto which the credit is valid (expiry date). The last date for shipment may also be specified
5) Since the beneficiary is usually required to draw a bill of exchange (normally referred to as a 'draft' in documentary credits)
   i) the terms of the draft (i.e., sight or usance)
   ii) whether the draft is to be drawn on a named bank or the buyer
6) Brief details of the goods
7) Documents required-usually the documents are: Commercial Invoice, Packing List, Insurance Policy- Certificate, Inspection Certificate, Transport document- Bill of Lading, Airway Bill or a Combined Transport Document
8) Port (s) of shipment and destination of shipment (only country's name may be written)
9) Price and terms of shipment (whether FOB, C& F or CIF)
10) Whether the part shipment and /or transhipment permitted
11) Any other conditions applicable to the credit
12) Certificate as the issuing bank's responsibility in the credit. If the certificate is omitted, it may be implied from type of credit indicated in (a) above, e.g., irrevocable, etc.
13) Statement that the credit is subject to the provisions of the Uniform Customs & practices for Documentary Credits.

6.4.3 Practical Mechanism

The general procedure in a letter of credit usually follows the sequence given below:

i) The buyer and seller agree terms of sale, including payment by letter of credit
ii) The buyer issues an instruction to the issuing bank to issue the credit
iii) The issuing bank instructs the advising or confirming bank, including specification of documents
iv) The advising bank informs the beneficiary
v) The beneficiary, if he accepts the advice and is happy with it, arranges shipment
vi) The seller obtains the bill of lading and the other required documents. He delivers them to the issuing. Paying, accepting or negotiating bank, whichever is the appropriate one for the settlement
vii) The bank checks the documents. If they are in accordance with the instructions from the issuing bank, (or the applicant) if the issuing bank is the paying bank, effects payment as appropriate
viii) If the paying bank is not the issuing bank, it sends the documents to the issuing bank. The issuing bank checks them and, if they are correct, release them to the buyer upon payment of the amount of credit.
ix) The buyer uses the documents to get possession of the goods.

6.4.4 Different Kinds of Letter of Credit

There are various kinds of letters of credit. Let us discuss them in detail.

1) **Revocable and Irrevocable Letter of Credit:** Under the revocable letter of credit, the issuing bank retains the right to cancel or modify the credit. Whereas in an irrevocable letter of credit, the issuing bank gives a binding undertaking to the beneficiary.
2) **Confirmed Letter of Credit:** This implies that a banker other than the issuing banker, by adding its confirmation, assumes the responsibility of payment, in case of the issuing banker's inability or refusal to pay.
3) **Restricted Credits:** This refers that negotiations under a credit may be restricted by the issuing bank to a named bank.
4) **Revolving Credit:** This process is arranged where regular, continuing shipments are made by seller. It may be available even after the credit has been utilised once.
5) **Red Clause Letter of Credit:** This process is in the nature of pre-shipment finance given to the seller by the buyer. This credit thus enables the beneficiary to draw an advance against shipments. The advance is liquidated by the amount due on presentation of documents.
6) **Transferable Credit:** This enables the beneficiary to make the credit available, in whole or in part, to one or more third parties (second beneficiaries). This can only be done if the credit clearly states it is 'transferable' (no other term is acceptable). It is used when the seller is a 'middleman' who transfers part of the credit to the supplier who ships the goods. Credit can be transferred once only.
7) **Back to Back Letter of Credit:** The bebeficiary of an irrevocable letter of credit may not be the actual supplier of the goods (he would be a middleman as in the case of the transferable credit). He will request his banker to open a further letter of credit (the back to back credit) favouring the supplier, based on original credit.
8) **Standby Credit:** This is similar to a performance Bond on Guarantee, but in the form of an L/ C. It thus assures the beneficiary that in the event of non-performance or non-payment of an obligation, the beneficiary may request payment from the issuing banker. The claim would be a draft accompanied by the requisite documentary evidence of non-performance as stipulated in the credit.
9) **Deferred Payment Credit:** These credits are used where supplier wishes to allow the buyer time to pay for the documents. He provides the beneficiary a specified time for payment after presentation of the documents which the bank will deliver to the applicant / buyer in the meantime.
10) **Payment Credit:** This is a sight credit which will be paid at sight basis against presentation of requisite documents to the designated paying bank. In a payment credit, beneficiary may or may not be called upon to draw a draft. In many countries, because of stamp duties even on sight drafts, it has become increasingly customary not to call for drafts under credit available by sight payment.
11) **Acceptance Credit:** This is similar to Deferred Payment Credit except for the fact that in this credit, drawing of a usance draft is a must. Under this credit, drafts must be drawn on the specified bank/drawee for specified period.

    The designated bank will accept the drafts and honour the same by making payment on the due dates.
12) **Negotiation Credit:** This can be sight credit or a usance credit. But drawing a draft is must in Negotiation Credit. Further the draft can be drawn either on the beneficiary or any other drawee as per credit terms. In a Negotiation Credit, the nomination can be restricted to a specific bank or it may allow free negotiation in which case it is called as 'Freely Negotiable Credit'. Under a Negotiation Credit, if the bank nominated as a Negotiated Bank refuses to negotiate, then the responsibility of Issuing Bank would be to pay as per terms of that credit.

13) **Sight and Usance Credit:** When a LC states that the payment will be made by the bank at sight, on demand or on presentation, such credit is called **Sight Credit.** However, drawing of a draft is not always needed; payment can be made on presentation of specified documents. Under Usance Credit, LC calls for drawing drafts at a stated usance period. This type of credit is also referred as 'Term Credit'.

14) **Fixed and Revolving Credit:** When a credit is available for fixed amount and period it is called Fixed Credit. In this type of credit, the credit gets exhausted once it is utilised for the stipulated amount or after the stated validity date.

15) **Under Revolving Credit:** Under this credit, the amount is revived or reinstated without requiring re-enhancement in credit.

16) **Transit Credit:** This is issued in one foreign currency with beneficiary in another but is advised through an usually confirmed by a bank in London.

Check Your Progress A

1) Distinguish between revocable and irrevocable letters of credit.

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2) Distinguish between sight and usance credit.

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3) What do you mean by deferred payment credit ?

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

i) Documentary credits have become popular because it reconciles the interest of buyers and sellers.

ii) Advance payment is the safest method from the importer's side.

iii) The banker to whom the letter of credit is sent for authentication and delivery is known as confirming banker.

iv) Commercial Invoice is a document of content.

v) Red clause L/ C is in the nature of pre-shipment finance given to the seller by the buyer.

6.4.5 Documents required under Letter of Credit

According to Article 4 of the Uniform Customs and practice for Documentary Credit in credit operations all parties concerned deal in documents, and not in goods, services and or other performances to which the documents may relate. Hence, it is necessary that the beneficiary tenders documents in conformity with the requirements of letter of credit. Usual documents prescribed in letters of credit are discussed below:

1) **Bill of Exchange:** It is an instrument drawn by one person (the seller of the goods) on another (the buyer) directing him to pay to or to the order of drawer (i.e., the seller). The person whom payment is to be made is called "payee", who can be either the drawer himself or a third person. Most letters of credit require that the exporter will prepare the bill, called the draft and submit it to the banker along with other documents. It is document through which payment is arranged.

2) **Commercial Invoice:** It is document of content. It contains details about the goods sold, the price and any other charges, which may be on account of buyer. It also contains information about any discounts, if given by the seller. A correctly completed commercial invoice should conform to the sale contract.

3) **Packing List:** This gives details of the individual parcels/packets shipped to the buyer.

4) **Transport Documents:** As shipment is the most crucial condition for payment, all letters of credit insist on lodgement of documentary evidence in support of exporter's contention of having shipped the goods. Bill of Lading is issued by the shipping company in case goods are sent by a sea vessel. Airway bill is issued in case of air consignment, Railway Receipt / Truck Challan in case the goods are sent by land route. Combined Transport Document is issued where the exporter chooses a multimodel transport system. These documents are accepted as proof of shipment.

5) **Inspection Certificate:** As the goods must conform to agreed quality standards, all letters of credit require an Inspection Certificate. The Inspection Certificate has to be submitted as a proof of the goods having been inspected by a qualified government or private agency.

6) **Insurance Policy Certificate:** Insurance policy is a legal evidence of contract of insurance, showing full details of risks covered. Insurance certificate, applicable in case of 'Floating' OR 'Open' cover, contains a declaration regarding value of each shipment and is signed by the exporter himself. Insurance certificate is not normally acceptable unless specifically provided in the letter of credit.

Besides, some letters of credit require documents such as Certificate of Origin, Analysis and Weight Certificate, Health and Sanitary Certificate to be submitted to the negotiating bank.

6.4.6 Guidelines for the Exporters

As stated earlier, payment under letter of credit is available only if the exporter has tendered correct documents. These documents are carefully scrutinised first by the negotiating banker in the exporting country, before he makes payment to exporters. The issuing banker in the importer's country also scrutinises it before reimbursing the negotiating banker. Any discrepancy in document can lead to delays in payment. Quite often documents are rejected on first presentation because they are either incomplete or incorrect. Some of the typical errors are as follows:

1) The letter of credit had expired.
2) The bill of lading was claused (unclean or dirty).
3) A charter party bill of lading was presented when L /C called on on-board shipment.
4) The goods were shipped on dock when it was not permitted.
5) Shipment was made between the ports other than those stated in the letter of credit.

6) Insurance cover was inadequate and expressed in a currency other than that required by the letter of credit.

7) The description (or spelling) of goods on invoice (s) differed from that in the letter of credit.

8) The weights, marks and numbers differed between export documents.

9) The amounts of value shown on the invoice (s) and bill of exchange (draft) differed.

10) The drawing was for less than the leltter of credit amount (when part shipment) were not permitted.

11) The bill of lading did not evidence whether freight was paid or not.

12) The shipment was short.

13) The bill of exchange (draft) was drawn on wrong party.

14) The bill of exchange was payable on indeterminable date.

15) The bill of lading, insurance document or bill of exchange (draft) were not endorsed correctly.

16) The copy of the freight account was not attached (when called for by the letter of credit).

17) There was an absence of signatures of witnesses, when required, on document presented.

18) The facsimile signatures were used when not allowed.

In view of such common errors, it is necessary to read the letter of credit very carefully and check the terms against the contract of sale. It is fundamental to check that the letter of credit:

i) is of the type agreed, e.g. irrevocable and confirmed or just irrevocable.

ii) has an expiry date that is sufficiently far ahead for the goods to be shipped and the required documents obtained and presented in time.

iii) has terms and conditions that can be met and that the required documents can be obtained exactly as called for.

iv) has correct spelling-and misspellings should be taken up immediately with the buyer.

If any amendment or extension is necessary, the buyer should be asked immediately to instruct the issuing bank accordingly. A watch should be kept to see that advice of amendment of the credit is received without delay. It should be remembered that bank is not allowed to overlook or approve errors and inconsistencies, however small in the documents presented and will not pay in such circumstances.

6.5 FORMS OF DOCUMENTARY CREDIT

Documentary credit may be issued in the form of Sight Credit and Acceptance Credit. Let us discuss them in detail.

6.5.1 Documents Against Payment

It is a widely used methods for receiving payments in respect of exports. The essence of this type of transaction is that the exporter is willing to ship the goods before payment. However, he is not prepared to allow the buyer to take possession of them before the buyer has paid.

The mechanics of the system requires the exporter to draw a bill of exchange on the buyer, payable at sight. The exporter then hands over the bill to his banks together with the documents of title to goods. The documents include commercial invoices, packing list, marine insurance policy or certificate and a full set of bill of lading/airway bill/combined transport

document. The documents are to be surrendered to the importer only upon payment of the bill. These bills are presented to the buyer for payment through a branch or a correspondent in the buyer's country. The amount is realised and remitted back to the exporter's bank for his account.

In case of goods sold on documents against payment basis, the exporter retains control of goods till payment is received but risks still exist. If the bill is not paid on presentation and the goods are lying in the foreign port, custom duties, warehouse and insurance charges and other incidental expenses may be incurred. It may be impossible to find another buyer, and difficult to reship the goods. In cases where the bills are in foreign currencies, exchange risks also exist from the time sales contract is concluded until the bill is realised. If the exporter's bank purchases such bill and the bill is not paid by drawee, exporter's account will be debited with the amount of the bill and related charges.

There are transfer risks arising from possible delays in remittances from the buyer because of shortage of foreign exchange in his country. Incidence of such risks, can however, be minimised by taking recourse to an export credit insurance policy.

6.5.2 Documents Against Acceptance

Under the documents against acceptance method, the exporter draws a usance or time bill in the importer. He forwards the bill along with the export documents to the bank for delivery to importer against acceptance of the bill. The essence of this type of transaction is that the exporter is willing not only to ship the goods before payment but is prepared to wait even after the buyer has taken delivery of goods. He, therefore, draws a bill and insists upon its acceptance before the documents are handed over to the importer. These bills have a usance period, usually of 30,60,90,120 or 180 days. Accepting the bill (which means writing the word ACCEPTED and putting the signature) implies an unconditional undertaking to pay on the due date mentioned in the bill. On the due date, the bill is presented for payment and the amount remitted to the exporter.

There are several risks associated with the system. Firstly, there is a credit risk. Failure or unwillingness to pay on the due date may force the exporter to take recourse to legal action. Secondly, there are transfer risks arising from possible delays in remittances from the buyer because of shortage of foreign exchange in his country. Incidence of such risks, can however, be minimised by taking recourse to an export credit insurance policy. Lastly, where the bills are drawn in foreign currencies, exchange risks as also the time contract is concluded and the bill is paid.

6.6 OPEN ACCOUNT WITH PROVISIONS FOR PERIODIC SETTLEMENT

This method is generally used in cases of inter- company relationship between seller and buyer. This is also used where the exporter and overseas buyers have had long and favourable dealings together and there are no exchange restrictions that might complicate settlement. Sales on open account are settled through periodic remittances to exporters. In such cases, financing is carried by the exporter. The exporter has sufficient financial strength or credit worthiness to carry the inventory abroad out of his own resources. Exporting on open account basis requires special permission of the Reserve Bank of India. Normally, it is available only to foreign companies operating in India.

6.7 SHIPMENT ON CONSIGNMENT BASIS

Shipment on consignment basis implies that goods are sent to the importer on the understanding that the latter will sell the goods and remit the sale proceeds. Importer, in most cases, is either the exporter's own agent or certain marketing agencies who undertake to sell the goods on commission basis. A typical example of such sale is export of tea to UK. Tea is sent to London, where it is sold through periodic auctions, and the sale proceed is remitted back to exporters.

Under the exchange control regulations in India, Indian exporters are required to declare the minimum selling price of each consignment. In case the goods cannot be sold at the price declared at the time of shipment, reduction in price can be effected only with the permission from Reserve Bank of India.

Check Your Progress B

1) List four important documents required under letter of credit.

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2) What do you mean by open account method of payment ?

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

i) The exporter draws a usance bill under the documents against acceptance method.

ii) Open account method is generally used in cases of inter-company relationship between seller and buyer.

iii) In documents against payment method, the buyer can take the possession of goods without making the payment.

iv) In shipment of consignment basis, the importer is either the exporter's agent or works on the commission basis.

4) Fill in the blanks.

i) A banker, who adds his confirmation of the market is known as ....

ii) Under ....an arrangement of regular and continuing shipment is made by seller.

iii) Under ....the supplier allows the buyer time to pay for the documents

iv) In ....method, the importers are allowed to take the delivery of goods before he has made the payment of the goods.

6.8 LET US SUM UP

Terms of payment are often decisive in obtaining an export order. Hence, an understanding of alternative payment terms is important for marketing goods abroad. There are four methods of receiving payments. They are: Advance payment, Documentary Credit, Open Account and Shipment on Consignment.

Advance payment, which is the simplest and safest method, involves remittance (by cable or mail) in payment for the goods by the time of acceptance of the order or at some time before the shipment. In most cases, however, it may not be accepted by the buyer, except perhaps when the buyer is an overseas affiliate of the exporter, or urgently requires the goods and the exporter is in a position to dictate his terms..

Where an exporter is unable to procure order with advance payment, the next best alternative for him is to export under 'Documentary Credit' arrangements. Under this method, at the instance of the importer (called applicant to the credit) a banker in the importing country (called the issuing banker) undertakes to make payment to the exporter (called the beneficiary), subject to fulfilment of the terms and conditions mentioned therein. This arrangement is communicated through a banker in the exporting country (called the advising banker). On receipt of the communication called the letter of credit, the exporter ships the goods. At the same time, he brings the shipping documents to a banker (who may be the advising banker, or if not forbidden in the letter of credit can be any banker). If the bank is satisfied with the documents, makes payment. After that, the bank sends the documents to the issuing banker and seeks reimbursement of the amount he has paid. The issuing banker, if satisfied with the documents, reimburses the amount to the negotiating banker. At the same time, the issuing banker hands over the documents to the importer, who takes delivery of the goods and makes payment to the issuing banker. Essence of the documentary credit arrangement is that a bank assures the exporter of payment if he fulfils the terms and conditions of the sales contract. This assurance instils confidence in the exporter, who accepts the order without reservation. Compliance of the terms and conditions is ensured through submission of certain documents. It also helps importer in the sense that it enables him to secure compliance of the terms and conditions of the contract and takes away the risk of placing order with suppliers in far-off countries.

Documents which the exporters are required to submit are (i) commercial invoice which indicates the goods supplied together with price (ii) a bill of lading or an airway bill or a combined transport document as proof of shipment (iii) inspection certificate as evidence of quality (iv) Insurance policy or certificate indicating risk coverage and most often (v) a bill of exchange through which payment is arranged.

The forms of documentary credit may be: Documents against Payment and Documents against acceptance. Under the Documents Against payment, the exporter draws a sight draft and sends it to a bank in the importing country. He also sends the shipping documents and requests the bank to hand over the documents only after the importer has paid. This method ensures safety in the sense that the documents are handed over to him only after payment. Whereas, under the Documents Against Acceptance, documents are handed over to the importer against acceptance of the bill which has a certain usance period (30, 60, 90, 120 or 180 days). Importer takes delivery of the goods and pays on due date. In other words, the exporter sells the goods to the overseas buyer on credit, incurring the usual credit risk.

Under open Account, the exporter ships the goods on a regular basis and receives payment periodically as per the terms of sales contract. Such arrangement is resorted to where either the buyer and seller are the same entity or the seller has full confidence in the buyer's integrity. Whereas, under shipment on consignment basis, the exporter sends the goods to the foreign buyer (who, in most cases, is his own agent) on the condition that the latter will sell the goods and remit the sale proceeds.

6.9 KEY WORDS

Documentary Credit: An arrangement whereby a bank (the issuing bank) undertakes to pay on behalf of its client (the importer or applicant) to make payment to the beneficiary or exporter upon presentation of certain documents specified in the credit.

Uniform Customs and Practices for Documentary Credits: The operation of letters of credit has been regulated and is governed by Uniform Customs and Practices for Documentary Credit of International Chambers of Commerce adopted by 165 countries, including India.

Applicant: The buyer or importer of goods. He is called applicant because he makes an application to the bank for opening a letter of credit in favour of exporter.

Issuing Bank: The bank who, at the request of the importer, issues the letter of credit.

Advising Bank: Issuing bank branch or correspondents in the exporter's country to whom the letter of credit is sent for onward transmission to the beneficiary.

Confirming Banker: The bank who undertakes to pay to the exporter in case the issuing bank fails to do so. Most often, the advising and the confirming banker are one and the same.

Beneficiary: The party to whom the credit is addressed. The seller or supplier of goods.

Revolving Credit: In a revolving credit, the amount of a drawing is reinstated and made available to the beneficiary again after a period of time, on notification of payment by the applicant or merely the fact that the shipment has been made.

Restricted Credits: The credits where a specified bank is designated to pay, accept or negotiate the credit.

Bill of Exchange: An unconditional order given by the drawer of bill to make payment, either at sight or after a specified time period, a specified sum of money to him (the drawer) or to the party named therein (the payee).

Documents Against Payment: An arrangement under which the importer is called upon to pay against documents relating to shipment.

Documents Against Acceptance: An arrangement whereby the bank is instructed by the exporter to handover the documents to the importer against acceptance of the bill presented to him.

Consignment Export: This implies that goods are despatched to the importer, who is either exporter's own branch/ subsidiary or his agent asking him to sell the goods and remit the sale proceeds thereafter.

Red Clause Credit: This authorises the advising bank to advance a part of the credit amount to the seller for the delivery of the merchandise.

Deferred Payment Credit: Under this credit, the issuing bank issues a written promise to make payment on the due date calculated on the basis of the credit terms.

6.10 ANSWERS TO CHECK YOUR PROGRESS

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

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

4 i) Confirming Banker ii) Revolving Credit

iii) Deferred Payment Credit iv) Documents Against Acceptance

6.11 TERMINAL QUESTIONS

1) Discuss the significance of payment terms in export transactions.

2) What are the various alternatives available to an exporter from the viewpoint of realising export proceeds ? Arrange them in order of safety. What are the risks associated with each of these alternatives ?

3) Discuss the mechanism of realising payment under letter of credit arrangements. Enumerate its advantages from the point of view of both exporter and importer.

4) What precautions should an exporter take while exporting under Letter of Credit arrangements ?

5) What is the method of realising payments under Documents Against Acceptance. Discuss? How does it differ from that of Documents Against Payments?

6) Is it possible for an Indian exporter to export on Running Account Basis? Discuss.