



## Methods of Payment in International Trade and Risk Mitigation August 11, 2016

### How Can International Trade Products Help You?

- Mitigates international risk
- Assists by meeting objectives of parties in the transaction – foreign buyer and exporter/seller
- Expands business between foreign buyer and exporter/seller
- Provides assurances of payment for both foreign buyer and exporter/seller
- Offers extended payment terms



## What Are Objectives Of The Buyer And Seller?

The exporter/seller's main objective is:

- Assurance of payment



The foreign buyer's main objectives are:

- Credit Terms
- Assurance that goods have been shipped timely and will be received in the quantity and quality ordered



## What are International Risks to Consider?

- **Commercial** – risk assumed by seller when extending credit without any collateral or recourse.
- **Political** – risk of loss when investing in a given country's political structure or policies, such as tax laws.
- **Sovereign** – risk that a foreign government will default on its loan or fail to honor other business commitments because of changes in national policy.
- **Market conditions** – characteristics of a market into which a firm is entering or into which a new product will be introduced, such as number of competitors, level or intensity of competitiveness and market growth.



## Incoterms 2016

TERMS	CONTROL OF COSTS	MAIN CARRIAGE COSTS	RISKS OF COSTS
EXW (Ex-Works)	BUYER	BUYER	BUYER
FCA (Free Carrier)	BUYER	BUYER	BUYER
CIP (Carriage & Insurance Paid to)	SELLER	SELLER	BUYER
CPT (Carriage Paid To)	SELLER	SELLER	BUYER
DAT (Delivered at Terminal)	SELLER	SELLER	SELLER
DAP (Delivered at Place)	SELLER	SELLER	SELLER
DDP (Delivered Duty Paid)	SELLER	SELLER	SELLER
FAS (Free Alongside Ship)	BUYER	BUYER	BUYER
FOB (Free on Board)	BUYER	BUYER	BUYER
CFR (Cost and Freight)	SELLER	SELLER	BUYER
CIF (Cost, Insurance, and Freight)	SELLER	SELLER	BUYER'



## Most Common Payment Methods



- Cash In Advance
- Documentary Letters Of Credit
- Documentary Collections
- Open Account

## Cash In Advance



**Foreign buyer prepays by wiring the funds to the exporter/seller prior to shipment of the goods or services.**

### **Advantage To The Exporter/Seller:**

- This is the most secure method of payment for the exporter – there is no risk as the exporter has immediate use of the funds remitted by the foreign buyer.

**BUT**

- Cash In Advance could cause exporters to lose customers to other competitors who offer more favorable terms to foreign buyers.

### **Disadvantages To The Foreign Buyer:**

- They have paid in advance and tied up capital before receiving goods or services.
- The foreign buyer has no assurance that what they contracted for will be shipped or received timely and in the quality or quantity ordered.

## Documentary Letters Of Credits



**An undertaking issued by a bank for the account of the buyer, to pay the beneficiary the value of the draft and/or documents provided that the terms and conditions of the Documentary Credit are complied with.**



Documentary Credits are governed by the Uniform Customs and Practices for Documentary Credits Publication No. 600. Rev. 2007.

## Documentary Letters Of Credit



Letters of Credit are irrevocable: can only be changed/amended or cancelled with agreement of ALL parties to the letter of credit.

The foreign buyer cannot refuse payment based on a complaint about the goods. Any complaint has to be resolved between the foreign buyer and the seller/exporter outside of the letter of credit.



## Advantages To Exporter/Seller By Using Documentary Letters Of Credit

- **The creditworthiness of the foreign buyer is substituted by that of the issuing bank.**
- **Protects against cancellation of the underlying sales contract.**  
The foreign buyer cannot back out of the transaction if goods have been shipped and the documents required in the letter of credit are presented in strict compliance with the Terms and Conditions of the Letter of Credit and subject to the Uniform Customs and Practices for Documentary Credits, Publication No. 600, Rev. 2007.
- **The exporter can offer extended payment terms of 30 to 180 days to the foreign buyer.**
- The exporter's bank can discount the drafts and pay the exporter when goods are shipped and complying documents are presented.



## Advantages To Foreign Buyer By Using Documentary Letters Of Credit

- **The foreign buyer has assurance that the exporter will be paid based only if all terms and conditions of the letter of credit have been complied with.**
- The foreign buyer cannot back out of the transaction if goods have been shipped and the documents required in the letter of credit are presented in strict compliance with the Terms and Conditions of the Letter of Credit and subject to the Uniform Rules for Documentary Credits, Publication No. 600, Rev. 2007
- **The foreign buyer has reasonable assurance that shipment is made prior to payment for the goods.**
- **The foreign buyer might be able to negotiate more favorable terms with the exporter since there is reduced credit risk for the exporter/seller.**



## Documentary Collections



**Shipping documents are presented to the foreign buyer's bank *without any prior conditional bank guarantee of payment.***

### **ADVANTAGES:**

- The collecting bank releases the shipping documents to the foreign buyer only upon full payment or acceptance of the draft.
- The exporter retains title to the goods until the importer makes payment.
- Documentary Collections are subject to the Uniform Rules for Documentary Collections, Publication No. 522.

### **DISADVANTAGES**

- The foreign buyer can decide he does not want the goods shipped and does not have to pay. The exporter/seller would still retain title to the goods but would have to find another buyer or have the goods shipped back at their expense.

## Open Account



**An arrangement between the foreign buyer and the exporter/seller where the goods are manufactured and shipped to the buyer before payment is required.**

### **Disadvantages to Exporter/Seller:**

- The exporter risks not being paid.
- Use of open account is advisable only if the foreign buyer has a long-time well-known customer of the exporter/seller in a low risk country.
- The foreign buyer can delay making payment until the goods have been examined and decision is made to make payment.
- A sudden drop in prices could encourage the foreign buyer to break the contract which would expose the exporter/seller to issues of non-payment, country instability or import regulation issues.

### **Advantages to Buyer:**

- The buyer does not have to pay until the goods are received and inspected.

## Standby Letters of Credit

- Unlike a Trade Letter of Credit, a Standby is NOT meant to drawn upon. The Standby is used as a form of “back up”, to “stand by” in case of default in payment or performance.
- A Standby is not a Guarantee, although it does guarantee payment or performance of an obligation to a beneficiary.
- Many U.S. Banks do not issue Guarantees, due to Federal regulations.

## Performance Standby Letter of Credit

### Used to guarantee some sort of a contractual obligation.

For example, a construction company building a bridge might be required by the foreign government or foreign entity to put up a performance standby, ensuring that they will complete the job or to warrant the work. Under normal circumstances, the standby would not be drawn upon, however, if the construction company abandoned the project midway through the completion, or if the bridge is deemed unsafe, the LC could be drawn upon.



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## Financial Standby Letter of Credit



- Similar in concept to the Performance LC, but instead, acts as a guarantee for payment of financial obligations. For example, customer promises to make payment to the beneficiary for a loan or other financial commitment.
- In the event customer does not make payment as agreed, LC can be drawn upon by the beneficiary.



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## Bonds and Guarantees

- Companies who are bidding for overseas jobs may need bid bonds, and, once they have won the bid, they may need advance payment guarantees, performance guarantees, or warranty guarantees.
- Most foreign beneficiaries will not accept a Standby LC and will only accept a guarantee issued by a local bank in their country. We have a network of banks that issue these on our behalf.



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## Questions?

# Contact



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