Question No. 2 What are the regulatory framework for Import finance? Explain various methods of import finance available to Indian Importers

Solution:

Regulatory Framework for Import Finance

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.

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.

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

1. for remittance to foreign supplies as advance payments.

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

3. discounting on purchasing except documents.

4. advances against shipping documents.

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

1. L/C may be opened by banks only on behalf of their customers who maintain account with them.

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

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

ADs 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 AD 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.

Currency of Payment

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 bill

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

METHODS OF IMPORT FINANCE

The methods of import financE 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.

1. Financing Import Under Letter of Credit (L/C)

L/C 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 FOR

instrument and as a means of making and securing payment, the L/C 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:

1. Requesting bank to open a L/C
2. Retiring documents under L/C
3. Import Trust receipt facility.

Each time a L/C is opened, the importer 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.
L/C may be opened by mail or Fax depending upon the urgency of the situation. It may be revocable or irrevocable. At times, the importer may ask the issuing bank to get the credit confirmed by another bank. 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 realisation 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 L/C 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.

2. Financing against Bills under Collection

In the case of imports not covered by L/C, 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. 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.

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, AD has to refer each deferred payment case to RBI for prior approval of advance payment, bank guarantee and instalments 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.

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.

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.

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.