TRADE FINANCE TERMS

Below are some of the frequently used terms in Trade Finance.

**ACCEPTANCE**
The beneficiary presents its documents together with a bill of exchange payable at a future date stipulated in the credit. The bank accepts the bill of exchange by signing it, and returns it to the beneficiary. Acceptance of a draft obliges the acceptor to pay it at maturity.

**ADVANCE PAYMENT GUARANTEE/BOND**
A guarantee or bond provided by a bank to the buyer. The guarantee/bond undertakes to return to the buyer on behalf of the supplier, usually on demand, down payments or progress payments made if the supplier fails to complete the contract.

**ADVISING BANK**
A bank in the beneficiary’s country – usually a correspondent of the issuing bank – through which the issuing bank communicates the credit to the beneficiary. It may also be asked to confirm and/or pay the credit.

**AMENDMENT**
Changes made to the original terms of a credit. The applicant initiates the amendment which then follows the same process as a letter of credit.

**APPLICANT**
The buyer who applies for a letter of credit.

**ASSIGNMENT OF POLICY**
The assignment of a policy’s rights and benefits from the exporter to a lender.

**AVAILABILITY**
The date by which a set of documents has to, or will, be delivered to the Advising Bank ready for discounting/Negotiating.

**AVAL**
An unconditional, irrevocable, divisible and freely transferable guarantee to pay the beneficiary on the due date.

**AVALISING BANK**
A bank in an importer’s country which adds its aval to notes or bills in a forfaiting transaction.

**AVALOR**
An institution or person acting as a guarantor.
**BASIS POINT**  
One hundredth of one percentage point (0.01%). 100 basis points = 1%.

**BENEFICIARY**  
The person (for example, the exporter) in whose favour the credit is issued.

**BID BOND**  
A bond provided by a bank to the buyer promising compensation, usually on demand, in the event that a supplier declines to enter into a contract in conformity with the bid he has put forward.

**BILL OF EXCHANGE**  
An unconditional order in writing addressed by one person to another, signed by the person creating it (drawer), and requiring the addressee (drawee) to pay a certain sum of money to the drawer at a fixed or determinable future time.

**BILL OF LADING**  
A document issued by a shipping company to the shipper as a receipt for the goods, a memorandum of the contract of carriage and a document of title.

**BUYER CREDIT**  
A financing arrangement under which a lending bank in the supplier’s country lends directly to the buyer or to a bank in the buyer’s country to enable the buyer to make payments due to the supplier under a contract.

**CASE OF NEED**  
The person or firm to whom collecting banks will refer if instructed to do so by collection orders in case of difficulty. The powers of case of need may be advisory only or full and must be specified.

**CLAIMING BANK**  
The bank entitled to claim reimbursement of sums it has paid in respect of a payment, deferred payment, acceptance or negotiation that it has carried out under the credit.

**COLLECTIONS**  
The provision by a bank of a service to a customer allowing documents proving shipment of customers’ goods to be transmitted via itself and another bank to the buyer of the goods. The release of documents to the buyer, thereby giving him title to the goods, is normally dependent upon payment by him or the promise to pay.
COLLECTING BANK
The bank in the buyer’s (drawee’s) country to whom the collection order and documents are directed.

COLLECTION ORDER
The set of instructions given to the remitting bank by the principal in a transaction. The remitting bank relays the collection order to the collecting bank.

COMMERCIAL LETTER OF CREDIT
A name sometimes given to a variant of documentary credit under which the credit is negotiable by any bank. The issuing bank requires all drawings to be noted on the credit document.

COMMERCIAL RISK
The possibility of non-payment arising from commercial causes such as bankruptcy, insolvency, protracted default and/or failure to accept goods that have been shipped according to the supply contract.

COMMUNITY FEES
Fees, payable usually on a semi-annual or quarterly basis, by the buyer to reserve the availability of a loan. The fee is payable on the undrawn balances.

CONFIRMING
The practice by advising banks of adding their separate undertakings to those of issuing banks and assuming liability under documentary letters of credit.

CONFIRMING BANK
A bank which adds its own independent payment undertaking to that of the issuing bank. The confirming bank is normally in the beneficiary’s country. The confirmation protects the beneficiary against the issuing bank defaulting, and political risk with regard to the country in which the issuing bank is situated.

CONSIGNEE
The drawee (importer) in a collection.

COUNTER-INDEMNITY
An exporter’s irrevocable commitment to repay the bank if a bond/Guarantee is called.

CREDIT INSURANCE
Insurance provided in exchange for a premium covering the loss incurred by a supplier in the case of non-payment by the supplier’s customer, due to the customer’s legal or de facto insolvency or simple failure to honour its commitments (default), or for political reasons or as a result of force majeure.
CUSTOMS GUARANTEE
A guarantee providing cover against possible customs duties. It is often used when goods are imported into the country on a temporary basis. If the goods are not re-exported within the prescribed time limit the customs authorities can claim under the guarantee for the customs duties which subsequently become payable.

DEFERRED LETTERS OF CREDIT
A credit providing for payment at a determinable future date following the presentation of documents which do not include a draft.

DEFERRED PAYMENT
The credit sum is payable at a stipulated period of time after presentation of documents.

DEMURRAGE
A form of rent charged on undeclared goods by, for example, ship owners or port authorities. Also charged by container owners on boxes delayed.

DISCOUNTING
Buying accepted term bills of exchange at a discount to allow for loss of interest on the funds until the bills mature.

DISCREPANCY
When documents presented do not agree with the terms of the credit or with each other.

DISHONOUR
The refusal to pay or accept a bill of exchange.

DOCUMENTARY CREDIT
A letter of credit that calls for the presentation of specified documents, issued to effect payment during a business transaction. It usually provides exporters with an independent bank promise of payment against presentation of shipping documents.

DOCUMENTS AGAINST ACCEPTANCE (D/A)
Where payment is to be made on documents against acceptance (D/A) terms, the presenting bank releases the documents to the importer against his acceptance of a bill of exchanges. Sometimes the buyer must sign a promissory note. The importer gains possession of the goods before making payment and can sell the goods immediately to get funds to pay the bill of exchange, thereby obtaining a period of credit. Payment terms are usually between 30- to 180-days after sight.

DOCUMENTS AGAINST PAYMENT (D/P)
Where payment is to be made on documents against payment (D/P) terms, the presenting bank is authorized to release the documents to the importer only against immediate cash payment.
**DRAWEE**
The party on whom a bill of exchange is drawn and which owes the indicated amount. In a collection this is the buyer.

**DRAWER**
The party that issues or signs a bill of exchange and stands to receive payment from the drawee.

**ESCROW ACCOUNT**
A bank account set up in hard currency in the joint names of the buyer and seller and in which the various monies involved in the countertrade agreement (usually a forward purchase) are held in trust.

**EXCHANGE CONTROLS**
Restrictions that are applied by a country’s monetary authority, or central bank, to limit the convertibility of the local currency into other specific foreign currencies.

**EXPORT CREDIT**
A loan to help the financing of the sale of capital goods and/or services eligible for a minimum repayment period of two years.

**EXPORT CREDIT AGENCY (ECA)**
The organization which provides official support to facilitate exports from its country. Its main function is to provide insurance against the commercial and political risk of non-payment for the exports. Commercial risk cover includes eventualities such as the buyer going into liquidation. Political risk cover includes the eventuality of war, or a change in the importing government’s foreign exchange controls which might prevent the importer from effecting payment. Some export credit agencies provide insurance cover only; others provide both insurance and medium- and long-term finance for capital goods.

**EXPROPRIATION RISK**
Risk of loss of an investment due to expropriation, nationalization, or confiscation by a foreign government. This risk is typically covered by political risk insurance.

**FACTORING**
The purchase from a company of some or all of its trade receivables with or without recourse to the company itself in the event that the receivables are unpaid. The service may also involve administration of the sales ledger for the company.

**FLOATING RATE**
An interest rate usually consisting of a variable market rate plus a fixed margin.
**FORCE MAJEURE**
Events over which none of the parties to a transaction has control or influence (acts of God).

**FORFAITING**
The purchase (without recourse to any previous holder of the debt instrument) of negotiable trade instruments resulting from the export of goods and services.

**FORWARD PURCHASE**
A compensation agreement under which the buyer’s goods are delivered to the exporter in advance to enable him to raise the foreign exchange to pay for his own sale.

**FRONT END FINANCE (DOWNPAYMENT FINANCING)**
A commercial loan under which separate credit facilities are provided to finance the down payment and/or other direct payments not covered under a buyer or supplier credit financing.

**HEDGING**
Reducing or mitigating risk, for example protecting against adverse foreign-exchange movement.

**ICC (International Chamber of Commerce)**
The voice of world business championing the global economy as a force for economic growth, job creation and prosperity.

Because national economies are now so closely interwoven, government decisions have far stronger international repercussions than in the past.

ICC activities cover a broad spectrum, from arbitration and dispute resolution to making the case for open trade and the market economy system, business self-regulation, fighting corruption or combating commercial crime.

**INCOTERMS**
An ICC published set of rules which define the responsibilities of buyers and sellers concerning who pays which expenses in the transit of goods from seller to buyer, over and above the original cost of the goods.

**IRREVOCABLE CREDIT**
The issuing bank and any confirming bank undertake an irrevocable payment obligation towards the beneficiary. The undertaking cannot be cancelled or amended unless the beneficiary agrees.
**ISLAMIC FINANCE**
Islamic finance is based on the principle that money must never spontaneously generate money. Instead, capital must be fecundated by labour, material or intellectual activity, or be invested in a wealth creating activity. Interest is replaced by a return obtained from wealth-generating activities. Islamic banking is regulated by the Sharia Law, Islamic law. The Sharia law encourages the use of profit sharing and partnership schemes and prohibits interest on money. Sources are the Qur’an and the Sunna (teachings from the Prophet Mohammed’s acts and paroles).

**ISSUING BANK**
The bank which issues a documentary credit. It may also be referred to as an opening bank.

**LETTER OF CREDIT**
A document established by the buyer for the purpose of financing international trade via substituting the bank’s credit for that of the buyer. A letter of credit is usually subject to the ICC Uniform Customs and Practice (UCP600) for documentary credits. The document states the amount and the terms under which the bank will pay the exporter when documents are presented to the bank.

**LETTERS OF INDEMNITY**
Letters of indemnity, or guarantees, are sometimes issued by banks when bills of lading or other transport documents go missing on goods shipments. Typically, such guarantees are issued for between 100% and 200% of the value of the goods.

**LIBOR**
London Interbank Offered Rate (Libor) of interest on deposits traded between banks. These rates are commonly quoted on a one-month, three-month, six-month and twelve-month basis.

**LINE OF CREDIT**
A buyer credit arrangement set up to finance multiple contracts subsequently entered into and nominated to the lender by the buyer and accepted by the lender as eligible for finance under the line. Lines of credit may either be for miscellaneous capital goods purchases (usually known as general purpose lines of credit) or for multiple contracts associated with one project (usually known as project lines of credit).

**MIXED CREDIT**
Export financing that includes a combination of export credit agency credit and concessional financing. Under the OECD if the subsidy element (concessional) is greater than 35% the entire loan is considered aid. This is also referred to as tied aid.
MULTILATERAL LENDING AGENCY
Financial institution jointly owned by a group of countries designed to promote international and regional economic cooperation.

These lending agencies are designed to help develop productive facilities and to further social and economic growth in member countries. Examples are the Asian Development Bank (ADB), the Inter-American Development Bank, the International Finance Corporation (IFC), and the European Bank for Reconstruction and Development (EBRD).

NEGOTIATION FEE (MANAGEMENT FEE)
Additional amounts payable to lenders. A once-only fee payable on establishment of the finance.

NEGOTIATING BANK
A bank buying the documents which obtains the right to deal with the documents any way it must to ensure repayment.

NOMINATED BANK
A bank designated by the issuing bank to which the beneficiary presents its documents and from which it obtains payment of the credit sum. Depending on the terms of the credit, this may be the issuing bank, the advising bank or some other bank.

NOSTRO ACCOUNT
Used to facilitate international payments, this is the account of a bank with its agent or correspondent in a foreign country which is recorded in the currency of that country.

PAYMENT METHODS
Sight payment: The credit is payable immediately against presentation of documents. Negotiation: The credit sum is available immediately against presentation of documents and negotiation (purchase) by the bank of (normally) a bill of exchange (draft) drawn up by the beneficiary.

PERFORMANCE BOND
A bond provided by a bank or an insurance company on behalf of a contractor in favour of the buyer promising compensation, usually on demand for bank bonds, in the event that the goods supplied/services performed do not meet the agreed contractual specifications.

POLITICAL RISK
Risk that execution of a contract will be prevented by political causes such as political violence, expropriation or currency inconvertibility. Political risk also covers default by a public-sector buyer.
**PRE-EXPORT FINANCE**
Financing that takes place before the product is ready for export. For example, an edible oil exporter might receive pre-export finance to enable it to buy seeds which it will eventually use to make the oil. This term is most often used in relation to the petroleum sector.

**PRE-SHipment RISK**
Event causing loss which occurs after contract signature but before shipment of the goods.

**PROTEST**
A legal document showing that a bill of exchange was presented to the drawee for acceptance/payment and was refused.

**RECEIVABLES**
Money owed to a business for merchandise or services sold on open account. Receivables are a key factor in analyzing a company’s liquidity.

**RECOURSE**
The lender’s right to recover funds (including interest where appropriate) from borrowers if they fail to pay.

**RED CLAUSE**
A credit where the advising bank makes pre-shipment advance payments to the beneficiary to help with the beneficiary’s pre-export financing.

**REIMBURSEMENT AUTHORISATION**
The authorization or request to reimburse provided by the issuing bank to the reimbursing bank.

**REIMBURSEMENT UNDERTAKING**
An independent undertaking to reimburse provided by the reimbursing bank in favour of the claiming bank in accordance with a request to that effect by the issuing bank.

**REIMBURSING BANK**
A bank designated by the issuing bank from which an authorized bank that has made a payment under the credit may obtain reimbursement.

**REMITTING BANK**
The bank instructed by the exporter/seller in the handling of collections. The remitting bank will, in its turn, instruct the collecting bank.

**RETENTION BOND**
A guarantee to a buyer that, if problems occur in a contract subsequent to its completion, retention funds will be callable.
**REVOCABLE CREDIT**
A credit which can be cancelled or amended unilaterally by the issuing bank.

**REVOLVING CREDIT**
A credit where the amount of available drawings is reinstated automatically after a stated period of time.

**SOVEREIGN BUYER**
A buyer that is owned by a national government and carries the full faith and credit backing of that government when entering into sales and credit agreements.

**STANDBY LETTER OF CREDIT**
A letter of credit that provides for payment to the beneficiary evidenced by certification that certain contractual obligations have been fulfilled.

**SUPPLIER CREDIT**
A financing arrangement under which the supplier agrees to accept deferred payment terms from the buyer, and funds itself by discounting or selling the bills of exchange or promissory notes so created with a bank in its own country.

**SWIFT**
Swift is the Society for Worldwide Interbank Financial Telecommunication, a member-owned cooperative through which the financial world conducts its business operations with speed, certainty and confidence. Over 8,300 banking organisations, securities institutions and corporate customers in more than 208 countries trust Swift every day to exchange millions of standardised financial messages.

**TOLLING**
In a tolling deal the customer provides the raw material (for example, steel ingots) and hires the capacity of the factory to turn it into the final product (for example, steel tubes). The final product is then supplied to the customer, who pays in cash. Throughout the process, the customer retains ownership of the raw material.

**TRANSFER RISK**
The risk or inability to convert local currency into the currency in which debt is denominated and/or the ability to transfer the funds to the country of the lender/exporter. Also known as conversion risk.

**TRANSFERABLE CREDIT**
A credit which allows the beneficiary to transfer part, or all, of the credit rights to a third party, or parties, if part shipments are allowed.

**TRANSIT CREDIT**
This is where a bank in a third country acts as an intermediary between the issuing bank and the advisory bank.
UNIFORM CUSTOMS AND PRACTICE FOR DOCUMENTARY CREDITS (UCP)
A set of rules and guidelines, drawn up by the ICC primarily for banks, relating to the issue and handling of letters of credit. It is applied virtually worldwide. The latest revision is UCP600 which came into effect on July 1 2007.

UNIFORM RULES FOR COLLECTION (URC)
A code of practice for banks regarding collections drawn up by the ICC. It is observed by most trading nations.

USANCE LETTER OF CREDIT
A deferred letter of credit without bills or notes issued under it.

VALIDITY DATE
The date on which a bond or guarantee expires.

VOSTRO ACCOUNT
Used to facilitate international payments, this is the account of a bank with an agent or correspondent in a foreign country which is recorded in the currency of the bank’s own country.

WAREHOUSE RECEIPTS
Warehouse receipts provide evidence that specified physical assets of a creditor are being held in storage. They may be used as a form of guarantee in countertrade operations.