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Financing Exports: Private Methods and Public Assistance

David Morris

Financing Exports: Private Methods and Public Assistance

United States foreign trade is expanding but it has not yet reached its full potential. As a percentage of gross national product, the international trade of the United States, defined as exports plus imports, is less than ten percent. This is significantly less than the similar statistics of some other major western industrialized nations.[1] Nonetheless, foreign trade is an extremely important segment of the United States economy, particularly in the context of the dependence of the economy on certain types of raw materials such as petroleum.[2] Moreover, there has been an unfavorable trend in the balance of foreign trade. Imports grew at a rapid pace during the previous two decades and in 1971 the value of imports surpassed that of exports,[3] resulting in a balance of payments deficit for the United States which has continued to the present time.[4] In an effort to offset the balance of payments deficit, Congress has passed legislation designed to encourage exports. Such legislation includes the Export Expansion Act of 1971,[5] the Foreign Trade Act of 1974,[6] and the Revenue Act of 1971 which provides for the establishment of Domestic International Sales Corporations (DISC).[7] In addition to specific governmental programs designed to increase exports, the collapse of the International Monetary System in 1971 with the resulting devaluation of the dollar will help increase exports by making United States goods and services cheaper in foreign markets.

Given the economic potential and the governmental encouragement of exporting, it is likely that domestic producers of goods and

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[1] F. ROOT, INTERNATIONAL TRADE AND INVESTMENT 44 (3d ed. 1973). While United States international trade is approximately 10 percent of gross national product, the comparable statistics for West Germany, Canada, and the United Kingdom are approximately 35 percent. The implication of these statistics is that there is a substantial and untapped foreign market for Unied States goods and services.

[2] While oil is a prime example, there are many foreign raw materials, metals, and commodities upon which the United States is either totally or to a large degree, dependent. *Id.* at 45.

[3] *Id.* at 37-38. *See also* Campbell, *Foreign Trade Aspects of the Trade Act of 1974*, 33 WASH. AND LEE L. REV. 325 (1976); Minchew, *The Expanding Role of the United States International Trade Commission*, 27 MERCER L. REV. 429 (1976); S. REP. NO. 1298, 93d Cong., 2d Sess. 12 (1974).

[4] While the balance of payments situation has improved somewhat since 1974, these gains have been overshadowed by the large increase in the price of imported petroleum from the Organization of Petroleum Exporting Countries (OPEC).

[5] Pub.L.No. 92-126, Aug. 8, 1971, 85 Stat. 345,346; 12 U.S.C. § 635 (Supp. 1975).

[6] Pub.L.No. 93-618 §1, Jan. 3, 1975, 88 Stat. 1978, codified in 19 U.S.C. §§ 2101-2487 (Supp. 1975).

[7] I.R.C. §§ 991-994. These provisions of the Internal Revenue Code allow for the deferral of Federal income taxes on export income in order to remove tax disadvantages from exporting. For a complete explanation of DISC, see Practicing Law Institute, NEW TRENDS IN SALES FINANCING (1973) [hereinafter cited as NEW TRENDS].

services will become more interested in the prospects of selling abroad. However, because of the greater distance between the parties and the lack of reliable commercial data about the foreign buyer, the risks are greater in export transactions than they are in domestic transactions. Further, there are additional risks inherent in every international transaction: the question of the applicable law and forum in the event of a dispute, and whether this can be controlled by agreement; whether the law to be applied will be solely commercial or will include public law such as export controls, tariffs, and quotas; the effect of currency fluctuations and foreign exchange restrictions on the transaction; the impact that war or expropriation might have on the transaction.[8] While attracted by the potential for increasing both sales and revenues from exports, every exporter will be vitally concerned with eliminating or controlling these risks.

Of all the factors involved in an export transaction, none is more important from the exporter's point of view than receiveing payment for his goods or services. The purpose of this article is to explain the financing aspect of exporting transactions. First, the essentially private methods for financing exports, particularly the role of banks, are considered. The role of the government in assisting the exporter in finacing those transactions where private financing is unavailable is then discussed. Particular attention is given to the protection against the risk of non-payment that the various methods and programs offer the exporter. The choice of any particular method of financing will necessarily depend upon various complex factors, not the least of which is competitive pressure. The selection of a given method calls for the exercise of commercial judgment based upon a working knowledge of the particular advantages and disadvantages of each method. The purpose of this discussion is not to recommend a particular method, but rather to explain the methods available to exporters for financing their sales.

Private Methods of Financing Exports

In every export sale, the agreement between the buyer and seller dealing with payment has four basic elements: time, method, place and currency of payment.[9] The various methods for financing exports represent variations and combinations of these four elements. Typically the interests of the buyer and seller come into conflict over these elements. While the exporter desires payment and the retention of a security interest in the goods until payment, the buyer wants to postpone payment until he has had an opportunity to resell the goods, thus using the proceeds of resale to effect payment. The method of financing the export sale will depend upon the resolution of these

[8] R. LEWENFELD, INTERNATIONAL PRIVATE TRADE (1975).

[9] C. SCHMITTHOFF, THE EXPORT TRADE 205 (6th ed. 1975) [hereinafter cited as SCHMITTHOFF].

conflicting interests in the agreement for sale. There are four methods of payment for exported goods which are available to the parties: sales on open account, consignment sales, bills of exchange or drafts and commercial letters of credit.[10]

The first two methods may be characterized as direct methods of payment in that they do not involve the services of a third party, typically a bank, to assist in securing payment. In the case of sales on open account, there are several variations in the basic method, depending upon the amount of time the buyer is given for payment. "Cash with order"[11] transactions entitle the exporter to payment prior to the time he actually ships the goods. While this type of arrangement eliminates the risk of non-payment for the exporter, it represents a strong conflict with the normal desires of the buyer, not only because this method is expensive for the buyer, but also because it requires him to place ultimate faith in the integrity of the exporter. To alleviate this problem, the parties might agree to a "sight payment"[12] arrangement in which the buyer makes a direct payment to the exporter on receipt of the documents of title, typically a bill of lading, from the carrier. This arrangement will normally be used in situations where the exporter is familiar with the importer and has confidence in the importer's ability to make payment. However, the desire of the importer to have an opportunity to resell the goods before being obligated to pay for them is frustrated by this arrangement. To overcome this problem, the exporter may allow the buyer to settle the account on a time basis,[13] although this arrangement will be agreed to by the exporter only when he is familiar with the importer. Further, while it fully satisfies the importer's desires, it leaves the exporter without a negotiable instrument evidencing the obligation which is immediately convertible into operating capital. Despite this disadvantage to the exporter, the arrangement can be an effective as well as a simple way to extend credit to an importer. The exporter should be extremely cautious, however, as collection problems may be insurmountable should the buyer default.

The above variations of the sales on open account method serve to illustrate the ways that the parties may adjust their conflicting interests with respect to the time element of payment. Another method for handling this aspect of payment is the consignment sale.[14] Goods are shipped to a consignee for sale in the foreign market on behalf of the exporter, who retains title to the goods. The consignee is not obligated to pay for the goods until he sells them. The principal disadvantage to

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[10] NEW TRENDS, *supra* note 7, at 114.

[11] SCHMITTHOFF, *supra* note 9, at 205-06.

[12] *Id.*

[13] NEW TRENDS, *supra* note 7, at 116-17.

[14] *Id.* at 117.

the exporter is that he is required to bear the risk of sale in a foreign market.

Thus far, the methods of financing described have involved direct means of payment in that whatever the time element the parties might agree upon, payment is made directly from importer to exporter. Frequently, however, the parties will agree that payment should be effected with the assistance of a third party, normally a bank. One such method involves bills of exchange[15] which are drafts on the foreign buyer. This arrangement is essentially one step more complex than the open account "sight payment" arrangement previously described.[16] Generally, the buyer will order the goods directly from the seller. The seller will then ship the goods and take a draft to his bank; typically the draft is accompanied by a bill of lading.[17] The exporter's bank will then forward the draft along with the necessary documents to a correspondent bank located near the buyer; the correspondent bank will inform the buyer of the arrival of the draft. The draft on the buyer may be either "sight" or "time". If the draft is sight, the buyer cannot claim the documents and their title until he pays the draft. If the draft is a time draft, the buyer will "accept" it. Upon acceptance, the buyer is obligated to pay for the goods at the expiration of the prescribed time.[18]

This method of financing has advantages for both parties. The exporter obtains a negotiable instrument which can be converted into cash immediately, although the holder of the draft has recourse to the exporter in the event the buyer defaults. Consequently the exporter bears the risk of default. Unless the draft is sight, the importer is extended by this arrangement, although typically for a short period of time.

There are several basic rules[19] which govern this arrangement and which are of particular importance to the exporter. In legal terminology, there are three parties to the draft transaction: the drawer (the exporter), the drawee (the importer) and the payee (the bank). Primary liability for payment of the draft rests with the drawee, although holders subsequent to the drawer will have recourse to him should the buyer default. The time of payment is normally stated in the draft (either sight or time); when the parties fail to make express arrangements, the custom in a particular trade will govern as to which

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[15] *Id.* at 116-17; *see also* SCHMITTHOFF, *supra* note 9, at 206.

[16] See text accompanying note 12 *supra*.

[17] The purpose of this so called "documentary bill" is to insure that the importer will not receive title to the goods until payment has been made or the draft "accepted". *See* SCHMITTHOFF, *supra* note 9, at 213.

[18] Alternatively, the draft by its terms might require the buyer to accept the draft, but not to deliver documents until the buyer has paid the draft. *See* NEW TRENDS, *supra* note 7, at 117.

[19] SCHMITTHOFF, *supra* note 9, at 207-10.

term will apply.[20] The draft must be payable on sight or at a definite time and cannot be subject to any contingencies. The place of payment should be specified in the draft by the drawer, but if he fails to do so, the drawee may speicify a place when accepting the draft. Normally, the drawer will have his bank arrange for payment or acceptance of the draft in the buyer's country, either through a branch or correspondent bank.[21]

While the bill of exchange is a useful device, it leaves the risk of default with the exporter. Even though the exporter has retained a security interest in the goods,[22] they may be thousands of miles away; it may be necessary to seek a legal remedy in a foreign forum at great expense. This problem poses a serious threat in the exporting context which may be eliminated by the use of the commercial letter of credit.

Although there are variations, the basis of any letter of credit is an undertaking by the importer to have a bank in the exporter's country provide for payment to the exporter upon delivery of shipping documents to the bank. The bank pays the purchase price either by "accepting" the documents along with a draft, or by actual payment if the draft is a sight draft. Thus the risk of default by the buyer is shifted from the exporter to a bank.[23] Moreover, this arrangement facilitates and encourages exporting because the seller can rely on the financial integrity of a bank, rather than on a less familiar buyer.

The Uniform Customs and Practices for Documentary Credits defines a letter of credit as follows:

> [D]ocumentary credit(s) and credit(s) used therein means any arrangement, however named or described, whereby a bank (the issuing bank), acting at the request and in accordance with the instructions of a customer (the applicant for the credit), is to make payment to or to the order of a third party, (the beneficiary) or is to pay, accept, or negotiate bills of exchange (drafts) drawn by the beneficiary, or authorizes such payments to be made or such drafts to be paid, accepted, or negotiated by another bank, against stipulated documents and compliance with stipulated terms and conditions.[24]

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[20] Likewise, absent express agreement, trade custom will determine whether payment is to be made on open account or by a bill of exchange. SCHMITTHOFF, *supra* note 9, at 206.

[21] International Chamber of Commerce, Brochure No. 254, *Uniform Rules for Collection of Commercial Paper.*

[22] *See* Schmitthoff, *supra,* note 9, at 213.

[23] "The general course of international commerce involves the practice of raising money on the documents so as to bridge the period between shipment and the time of obtaining payment against documents." T.D. Bailey, Son & Co. v. Ross T. Smyth & Co., 56 T.L.R. 825,828 (1940), *cited in* SCHMITTHOFF, *supra* note 9, at 216.

[24] International Chamber of Commerce, Brochure No. 222, *Uniform Customs and Practices for Documentary Credits* (rev. 1962) [hereinafter cited as *Uniform Customs and Practices*]. These Uniform Customs and Practices have been widely accepted and have gone far in unifying the law of international trade in this particular area. As of 1966, they have been adopted by banks and banking associations in 173 countries.

Several aspects of this definition should be emphasized. First, the applicant for credit is the buyer/importer while the beneficiary is the seller/exporter. Secondly, the definition has a broad scope, allowing for more than one bank to participate[25] and for payment to be immediate as well as extended, thereby granting credit to the buyer. Finally, and of crucial importance, the definition mentions only the documents and never the goods because the basic premise of the letter of credit is that the banks are concerned solely with the documents and not with the goods themselves.[26]

Typically, there are four basic stages in the operation of a letter of credit. The exporter and buyer will agree in the contract for sale that payment shall be effected by a letter of credit. Next, the buyer will instruct the issuing bank to open a credit for the seller on the terms specified by the buyer in his instructions to the issuing bank. At this point, the issuing bank will arrange with a correspondent bank to pay, accept, or negotiate the seller/exporter's draft upon delivery of the shipping documents by the seller.[27] Finally, the correspondent bank will advise the exporter that it will pay, accept, or negotiate the exporter's draft upon delivery of the documents.[28]

Legally, the relationship between the parties coincides with the stages in the operation of the credit. In terms of its basic legal structure,[29] a letter of credit is a legally enforceable commitment by the issuers[30] to pay money to a beneficiary on behalf of a third party, the buyer. It is expected that the buyer will make this arrangement pursuant to his agreement with the exporter. More specifically, the letter of credit transaction involves a sequence of agreements identical to the basic operational steps previously discussed. These agreements,

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[25] The importer may use a bank in the exporter's country, in which case the need for a correspondent bank would be eliminated.

[26] The fundamental principle of the *Uniform Customs and Practices* is to provide for strict separation of the documentary aspect of the transaction from the goods aspect. This essentially means that the bank or banks involved will not be responsible for problems arising from the contract for sale such as breach of warranty. Section B, Article 8 of the Uniform Customs states that "In documentary credit operations all parties concerned deal in documents and not in goods."

[27] Rigid adherance to these basic stages is not necessary. For example, if the buyer instructs a bank in the exporter's country to open the credit there is no need for the correspondent bank stage. *See* text accompanying note 26 *supra*. The procedure outlined is typical in situations where the exporter's bank is unfamiliar with the buyer and would perefer to deal with a bank in the importer's country because it is better able to assess the risk of non-payment by the foreign bank.

[28] As a general rule, letters of credit issued or advised by banks in the United States contain a clause that the creidt is subject to the *Uniform Customs and Practices*. See notes 25-27, *supra*, and accompanying text.

[29] H. HARFIELD, BANK CREDITS AND ACCEPTANCES 31 (5th ed. 1974).

[30] "Issuers" here would include both the issuing bank and its correspondents.

while functionally related, are entirely separate and distinct from one another as a matter of law.[31]

As a practical matter, the exporter is primarily concerned with only two of these agreements — his contract for sale with the buyer and his agreement with the issuing or correspondent bank. When the contract between the exporter and buyer requires payment by a letter of credit, the buyer is legally obligated to open the credit in conformity with the agreement. If he fails to do so, the seller can claim damages for breach, including lost profits where appropriate.[32] The contract for sale also governs when the credit is to be opened, but absent agreement, the presumption is that the opening of the credit is a condition precedent to performance by the exporter and not a condition to the existence of the contract. Even though the credit has been opened by the buyer in compliance with the terms of the contract for sale, the exporter is not entitled to payment until he has satisfied the terms of the agreement with the issuing or correspondent bank. As discussed above, the terms of this agreement provide that the exporter must present certain documents to the bank before he is entitled to payment. It is at this point that the exporter confronts the most technical aspect of the letter of credit transaction.

Under the doctrine of strict compliance, the exporter (beneficiary) must strictly comply with all the terms of the letter of credit before he is entitled to payment.[33] If he does not do so, the bank will be able to reject the documents and the exporter will not be able to compel the bank to make payment. Moreover, the bank will be liable for breach of contract if it makes payment against non-conforming documents[34] or if it wrongfully refuses to make payment when there has been compliance with the terms of the credit.[35] Conversely, the bank is not liable if the documents against which payment is made conform to the credit, but subsequently turn out to be false or fraudulent.[36] When a question as to the sufficiency of the documents arises and it cannot be resolved

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[31] While Harfield describes the parties' relationship as contractual in nature, Schmitthoff, at least for some purposes sees the relationship between the buyer and the bank(s) in terms of agency. *Compare* HARFIELD, *supra* note 29, at 103 *with* SCHMITTHOFF, *supra* note 29, at 218-19.

[32] SCHMITTHOFF, *supra* note 9, at 225.

[33] The classic formulation of the doctrine states "[t]here is no room for documents which are almost the same or which will do just as well." Equitable Trust Co. v. Dawson Partners, 27 Lloyd's List L.R. 49, 52 (1927); *Accord,* Banco Espanol de Credito *v.* State Street Bank & Trust Co., 385 F.2d 230 (1st Cir. 1967) *aff'd after remand,* 409 F.2d 711 (1st Cir. 1969).

[34] Venizelos, S.A. v. Chase Manhatten Bank, 425 F.2d 461 (2d Cir. 1970).

[35] Schmitthoff views the relationship of the banks and the buyer as a special agency. Therefore the banks have limited authority which enables the principal to disavow acts outside the scope of authority. *See* SCHMITTHOFF, *supra* note 9, at 225.

[36] *See* Sztejn v. J. Henry Schroder Banking Corp., 177 Misc. 719, 31 N.Y.S.2d 631 (Sup. Ct. 1941).

by reference to the terms of the credit, the provisions of the Uniform Customs[37] will prevail.

Clearly, the doctrine of strict compliance compels the bank as well as the exporter to insure that the documents presented meet the requirements set forth in the letter of credit. The doctrine stems from the nature of the bank's role in this type of arrangement. It is basic to the law of letters of credit that banks deal in documents and not in merchandise.[38] The letter of credit is entirely separate and distinct from the underlying sales contract.[39] This proposition is so firmly embedded that it has been held that the lack of conformity of the documents to the actual intention of the parties to the sales contract, or even the express terms of the sales contract, is immaterial to the extent that such intention or terms are not expressly set forth in the letter of credit.[40] It follows from these principles that the entire obligation of the bank is contained in the letter of credit and the bank will not be a party to a dispute between buyer and seller over the sales contract. Once the seller has presented the required documents to the bank prior to the expiration date,[41] the bank fulfills its obligation by paying or accepting the draft.

It is vital that the exporter be informed of the documents that are required and the basic rules for their use. Generally, the letter of credit will require the exporter to present, in addition to a draft, a commercial invoice, bills of lading, and an insurance policy or certificate. Depending on the circumstances and the countries involved, additional documents may be required, for example, consular invoices, export licenses, import licenses, packing lists and certificates of origin. The rules relating to the presentation of these documents are crucial. All documents required by the letter of credit must be presented prior to the expiration of the credit or the bank will be released from its obligations.[42] Compliance with specific instructions in the letter of credit is necessary in order to assure acceptance or payment by the bank. For example, the credit may require that the bill of lading be drawn to the order of, or consigned to, the issuing bank. The exporter must insure that the bill is so drawn.[43] Of greater importance in every letter of credit transaction is the requirement that the description of the

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[37] *See* note 28, *supra*.

[38] Sisalcords Do Brazil v. Fiacao Brasileira De Sisal, S. A., 450 F.2d 419 (5th Cir. 1971); *Uniform Customs and Practices, supra* note 24, art. 8.

[39] Banco Espanol de Credito v. State Street Bank & Trust Co., 385 F.2d 230 (1st Cir. 1968), *aff'd after remand*, 409 F.2d 711 (1st Cir. 1969).

[40] Barclays Bank v. Merchantile Nat'l Bank, 481 F.2d 1224 (5th Cir. 1973).

[41] Documents must be presented to the bank before the expiration date of the credit. Back, *Introduction to Commercial Letters of Credit, reprinted in* RRACTISING LAW INSTITUTE, EXPORTING: GOVERNMENTAL ASSISTANCE AND REGULATION, at 133 (1975).

[42] Anglo-South American Trust Co. v. Uhe, 261 N.Y. 150, 184 N.E. 741 (1933).

[43] The purpose of this procedure is to give the issuing bank a security interest in the goods until the importer pays for them.

goods in the commercial invoice correspond with the description of the goods in the credit. This requirement cannot be varied, even by agreement of the parties. In the remaining documents, the goods may be described in general terms.[44]

Letters of credit may be confirmed or unconfirmed. Confirmation is important to the exporter because it represents a legally enforceable obligation on the part of the issuing bank to pay or accept the exporter's draft when presented with the required documents. When the correspondent bank does not specifically advise the exporter of confirmation, the exporter must assume the credit is unconfirmed.[45] These terms, confirmed or unconfirmed, should be carefully distinguished from revocable and irrevocable credits in that they refer to a different aspect of the transaction. The latter terms relate to the instructions received by the correspondent bank from the issuing bank while the former relate to the advice sent from the correspondent bank to the exporter.[46] Only irrevocable credits will be confirmed, though not all irrevocable credits are in fact confirmed.

If, as a result of the buyer's instructions to the issuing bank, the credit is revocable, then necessarily the advice to the exporter will be of an unconfirmed credit. This means that the credit is subject to cancellation at any time without notice. Obviously, this type of credit is "practically worthless"[47] to the exporter. If, however, the exporter finds himself the beneficiary of such a credit, he should seek to protect himself by requiring the bank to give notice of cancellation.

From the exporter's point of view, the most advantageous type of credit is the irrevocable and confirmed credit which obligates the bank to honor the exporter's drafts provided they conform to the terms of the credit. The confirmed credit is a direct undertaking by the bank to pay the exporter, and it must be honored even when the buyer has instructed the bank to cancel the credit due to a breach of the contract for sale.

> The opening of a confirmed letter of credit constitutes a bargain between the banker and the vendor of the goods, which imposes upon the banker an absolute obligation to pay irrespective of any dispute there may be between the parties as to whether the goods are up to the contract or not.[48]

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[44] Laudisi v. American Exch. Nat'l Bank, 239 N.Y. 234, 146 N.E. 347 (1924); *Uniform Customs and Practices, supra* note 24, art. 30. The reason for this rule is that the commercial invoice is the seller's representation of the goods sold while the bill of lading is the carrier's receipt and contract for shipment. Naturally, the carrier will not be concerned with describing the goods accurately. H. HARFIELD, *supra* note 30, at 73; *contra*, J. H. Raynor & Co. v. Hambros Bank. Ltd., [1943] 1 K.B. 37.

[45] *Uniform Customs and Practices, supra* note 24, art. 6.

[46] SCHMITTHOFF, *supra* note 9, at 226.

[47] *Id.* at 227.

[48] Hamzeh Malas & Sons v. British Imex Industries, Ltd., [1958] 2 Q.B. 129.

Where the seller is entitled to a confirmed credit under the terms of the contract, he is under no obligation to make shipment if advised of an unconfirmed credit.[49] Since the confirmed credit eliminates the credit risk, it is particularly desirable when the parties are dealing with each other for the first time.

As previously noted, not all irrevocable credits are confirmed. If the credit is irrevocable and unconfirmed, the issuing bank cannot revoke its undertaking to the exporter but the correspondent bank is not legally obligated to make payment. The advantage of this type of credit is that it is less expensive than the confirmed variety. The risk it poses for the exporter is that it does not localize performance of the contract for sale in the exporter's country. Consequently, it largely defeats the purpose of the letter of credit.

While the types of letters of credit mentioned are the ones most generally used in exporting,[50] there is one further variation which is useful where the exporter and importer envision an ongoing relationship. In these cases, the parties may agree to use a revolving credit, the advantage of which is that it does not have to be renewed with each sale. The buyer establishes a maximum credit amount which will be drawn down as the exporter presents drafts and replenished as the buyer makes payments.

In an area as technical as letters of credit, predictably there are problem areas with which the exporter must be familiar. For example, the exporter will occasionally be unable to comply strictly with all the terms in the letter of credit. In this situation, the exporter has two alternatives to foregoing payment. If time permits, the exporter may contact the buyer and arrange to amend the credit in order that the exporter will be able to comply. If this is not possible, the bank will generally ask the exporter to supply an indemnity before it will make payment. The problem in this case is that the bank will have recourse to the exporter if the buyer defaults. Therefore, the exporter should seek amendment of the credit before resorting to indemnity.

Two aspects of private financing bear further explanation. In the context of bills of exchange and letters of credit, it has been noted that the drafts presented to the bank may be either sight or time.[51] Sight drafts are paid immediately upon presentation, while time drafts are accepted rather than paid on presentation. A time draft drawn in United States dollars and accepted by a bank in the United States becomes a Bankers Acceptance, which is a negotiable instrument convertible by the beneficiary (exporter) into ready funds by discount-

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[49] SCHMITTHOFF, *supra* note 9, at 229.

[50] Other types of specialized letters of credit are discussed in SCHMITTHOFF, *supra* note 9, at 230-35.

[51] PRACTISING LAW INSTITUTE, EXPORTING, *supra* note 41, at 143. *See also* H. HARFIELD, *supra* note 30.

ing. The time draft thus serves the dual purpose of extending credit to the buyer while giving the seller an instrument which is convertible into working capital. Banks in the United States will issue, advise, or confirm credits on a time basis only if the term of the acceptance is no longer than the period during which the related goods will remain in the channels of trade, and in no case for more than six months.[52]

Finally, whatever method of financing is employed, the parties must agree on which currency is to be used in payment. This aspect of the transaction presents significant risks to both parties due to fluctuations in the rate of exchange.[53] Most transactions with United States firms are in dollars and, unless otherwise agreed in the contract for sale, the buyer is expected to make payment in the currency of the seller.[54] If, however, the exporter agrees to take payment in the currency of the buyer, he must be aware of rates of exchange and their possible fluctuation, particularly if there will be a long period of time between the fixing of the price and the actual payment. Unless the exporter takes steps to protect himself, he will essentially become a speculator in foreign exchange. In most cases, the exporter will want to avoid this because even a small decline in the value of the foreign currency against the dollar may be enough to eliminate the exporter's profit on the sale.

In order to avoid speculation in foreign exchange, the exporter can provide in the contract for sale that the rate of exchange for payment is the rate of exchange which exists on the date of execution of the contract for sale. In this way, the exporter can assure himself of a known amount of dollars and the risk of rate of exchange fluctuations will be shifted to the buyer. Alternatively, the exporter can hedge his position in the foreign currency by executing a forward foreign exchange contract with a bank dealing in foreign exchange. Since foreign currency in the United States is regarded as a commodity,[55] the exporter can also hedge his position by trading on one of the commodity exchanges, provided that the particular currency involved in the transaction is traded on a domestic commodity exchange.[56]

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[52] 12 U.S.C. § 372 (1970).

[53] As a practical matter, the United States exporter who is entitled to receive payment in dollars need not be concerned with changes in the value of the dollar relative to other currencies for any particular transaction. Nonetheless, fluctuations in exchange rates will have an impact on the competitiveness of United States goods in foreign markets.

[54] NEW TRENDS, *supra* note 7, at 111.

[55] A. NUSSBAUM, MONEY IN THE LAW NATIONAL AND INTERNATIONAL 318 (1950).

[56] The only difference in whether the bank or the exporter does the actual hedging would be the transactional costs. Foreign currencies currently traded in domestic commodity exchanges include: British Pound, Canadian Dollar, Deutschmark, Dutch Guilders, Japanese Yen, Mexican Peso, Swiss Franc.

Governmental Assistance in Financing Exports.

Private financing by either the exporter or a bank is used principally in situations where the value of the goods exported is relatively small and/or the period of time for payment is short. In most cases, the goods involved in these transactions will be of a type which the buyer will be able to resell immediately or will involve a situation in which the buyer has arranged his own financing. Private lenders have generally been unwilling to finance large export sales of capital goods, particularly when the buyer is in a developing country where the political and economic factors increase the risk of default. In an effort to overcome the lack of private funds and to encourage exporting as a means of solving the current balance of payments problem, the United States government has established institutions and programs designed to facilitate financing exports, especially in those situations where private capital is unavailable.

The Export-Import Bank of the United States (Eximbank) is a primary source of funds which plays a key role in programs designed to assist the exporter. Eximbank was established by Executive Order in 1934 and was established formally by Congress in 1945.[57] One of its primary goals is to increase exports, consequently reducing the balance of payments deficit.[58] If the underlying transaction is sound, Eximbank is determined that United States exporters will be able to offer competitive credit terms to their foreign customers.[59] To achieve this goal, Eximbank offers several programs to assist the exporter.

In some cases, Eximbank will make direct credits available to foreign buyers to enable them to purchase United States goods and services. Proceeds of these loans do not go directly to the foreign borrower but are used to pay the United States exporter.[60] The purpose of the direct lending program is to supplement private sources of funds where they are unwilling or unable to completely finance the sale. Generally, direct loans are granted only on a long term basis, i.e., for terms greater than five years.

It is the policy of Eximbank to require private participation in the direct lending program in order to encourage the private expansion of export credit, to insure that Eximbank does not compete with private capital, and to broaden the impact of Eximbank's cash resources. To induce participation, Eximbank will fully finance the portions of the loan that mature later in time. Therefore, the private lender can recoup

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[57] 12 U.S.C. § 635 (Supp. 1975).

[58] NEW TRENDS, *supra* note 7, at 55; *see also* Streng, *Export Financing*, 11 SAN DIEGO L. REV. 104 (1973); Report to the President by the Committee on International Trade and Investment (July, 1971).

[59] The availability of export credit is as important a competitive tool as price, quality or service. NEW TRENDS, *supra* note 7, at 55.

[60] In cases where the importer has already paid the exporter, Eximbank will reimburse the importer.

his investment before Eximbank recovers its own funds. Moreover, Eximbank will guarantee[61] repayment of the private lender's portion of the total loan against both political[62] and commercial risks.[63]

Three criteria must be satisfied before Eximbank will agree to make the direct loan and financial guaranty available to the exporter.[64] First, the borrower, in this case the importer, must be financially capable of performing his repayment obligations.[65] Moreover, the transaction must be financially, economically, and technically sound both for the borrower and for the country of the borrower. Finally, consistent with the goal of increasing United States exports, the goods or services sold must be of United States origin. The legislation does not specify the types of projects that the bank should finance. Eximbank policy, however, is to finance projects which will directly contribute to the economic well-being of the buyer's country. This policy translates into the rule that Eximbank will finance projects which increase productive and earning capacity in the buyer's country, but it will not finance social service projects.[66]

In order to develop greater private financial support for domestic exporters who are forced by foreign competition to provide deferred credit terms, Eximbank will guarantee repayment of medium term (six months to five years) export debt. The guarantee again covers both political and commercial risks. As a general rule, the guarantee is available only to domestic banking institutions, although the exporter who has been financed by the bank may be a corporation, a partnership, or an individual. The guarantee is issued upon notification to Eximbank that the bank involved has purchased the importer's notes without recourse to the exporter. There are only two limitations on the availability of the guarantee: it is available only for domestic goods and services, and repayment terms cannot exceed terms customary in international trade for the type of goods exported.[67]

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[61] *See* text accompanying note 67, *infra*.

[62] Political risks include war, expropriation and inconvertibility of currency.

[63] Commercial risks include default and insolvency.

[64] Eximbank will make preliminary commitments to assist the exporter in the marketing phase of his operations.

[65] 12 U.S.C. § 635(b) (Supp. 1975). The statute states that there must be "reasonable assurance of repayment."

[66] J. LOPMIS, INTERNATIONAL FINANCE: OFFICIAL AGENCIES AND U. S. BUSINESS 23 (1970). Examples of projects financed by Eximbank are power production, transportation and steel refining.

[67] The terms and conditions of the guarantee are contained in the Master Guarantee Agreement between Eximbank and the private bank. Two provisions are of particular importance to the exporter. First, he must receive ten percent of the price on or before delivery and take the balance in promissory notes providing for payment in dollars. Second, the exporter must retain at least ten percent (two percent for agricultural commoditeis) of the loan at his own risk. NEW TRENDS, *supra* note 7, at 58-61.

Eximbank, in conjunction with an association of private insurance companies,[68] also provides credit insurance to exporters. Various types of policies are available, but the goal is to insure short and medium term loans (up to five years) against political and commercial risks. Under this program, exporters are required to self-insure as much as ten percent of the loan. These policies have a further advantage to the exporter (beyond the value of the insurance) in that the policies may be assigned, along with the notes insured, as collateral on a loan.

While these programs are perhaps the most important from the exporter's point of view, they do not exhaust the services and facilities provided by Eximbank to assist exporters. Through its Cooperative Financing Facility (CCF), Eximbank makes credit available to small and medium-sized purchasers of United States goods and services through banks in the importer's country.[69] Eximbank also provides counseling services which assist exporters in solving problems relating to financing exports. Finally, in an effort to make more private capital available for export financing, Eximbank will discount export loans in much the same way that the Federal Reserve Bank will discount domestic loans.

Although Eximbank is the principal government agency for assisting the exporter in financing his sale, other government agencies may be of some assistance. For example, the Commodity Credit Corporation of the Department of Agriculture has an Export Credit Sales Program to support the exporting of agricultural commodities by purchasing the exporter's accounts receivable. Moreover, several agencies such as the Overseas Private Investment Corporation (OPIC) and the Agency for International Development (AID) will assist exporters financially in connection with their programs of financing direct foreign investment.

Conclusion

Selling goods abroad, while potentially profitable, is unavoidably complex, legally and commercially. The complexity is not only a function of the risks involved but also a result of the various economic policies a given nation may pursue in an effort to further its own economic goals. The exporter must be aware of the problems posed by this economic, legal and political environment in order that he might attempt to control or to eliminate as much uncertainty as possible. The available financing methods offer the exporter flexibility in resolving the basic conflict[70] between his goals and those of the buyer, and a reduction of much of the uncertainty involved in the payment aspect of the transaction.

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[68] Foreign Credit Insurance Association (FCIA). *Id.* at 61.

[69] Under this program Eximbank will participate with foreign financial institutions to extend credit to United States exporters. NEW TRENDS, *supra* note 7, at 88.

[70] *See* text accompanying note 9, *supra*.