

Import finance

Many businesses find importing requires greater financial flexibility and reserves than buying from a UK supplier. Rather than buying on credit, you must often commit finance well before delivery. Negotiating the right agreement with your supplier can cut the cost and effort involved.

This briefing covers:

- key factors to consider when negotiating with your supplier
- terms of delivery
- payment methods and financing options
- handling VAT and duty.

1 The right balance

The terms you negotiate with your supplier must provide an acceptable balance, taking account of risks, costs and the need to arrange financing.

1.1 The payment method you agree will determine the **risks** you each carry (see **3**).

- Your supplier will want to reduce the risk of being paid late, too little or not at all.
- You will want to reduce the risk of paying for goods that are not as ordered, are faulty or damaged, or arrive late or not at all.

1.2 Both parties will face **costs** that would not apply to a transaction within one country. These will include:

- Transaction costs such as payment costs.
 - Administrative costs.
- All imports require documentation (see box, page 3).

- Transport and insurance costs — the terms of delivery will determine your share of these (see **2**).
- VAT and any duty or excise duty (see **5**).

1.3 Both you and your supplier may need to arrange **financing** (see **4**).

- The financing possibilities will depend on the payment method agreed.
- It may be appropriate for the party with access to cheaper financing to carry more of the financing burden. The financing burden you each assume can be reflected in the price you agree.

Directors' Briefing

a book in four pages

More than 160 briefings are
now available.

If you need further information or help,
ask the distributor of this briefing
about the services available to you.

2 Terms of delivery

2.1 The terms of delivery specify how **responsibility** and **costs** are shared between you and your supplier. They should cover:

- who is responsible for packaging and labelling of the goods
- who is responsible for arranging and paying for each stage of the delivery
- who is responsible for insuring the goods over each stage of the delivery
- when ownership of the goods passes from the supplier to you.

2.2 There is a range of internationally recognised **standard terms** known as Incoterms. The terms used will depend on how the goods are to be transported and what you negotiate with the supplier. They include:

- ex-works — where you arrange to collect goods from the supplier's premises, taking immediate ownership and responsibility

- delivered duty paid — where your supplier is responsible for delivery to your premises and pays any import duties and taxes
- several other terms are used where responsibility and costs are shared in specified ways.
For example, cost, insurance and freight (CIF), where the supplier pays for the delivery of goods to your port of destination. The risk of loss or damage to the goods passes to you, but the supplier must take out a minimum level of insurance cover against it.

Detailed information on all standard terms is published as 'Incoterms 2010' by the International Chamber of Commerce.

2.3 Taking more **control** over the delivery process may cut your overall costs and risks.

- It can be difficult to ensure that the exporter is handling things in the way you would like while delivery remains the exporter's responsibility.

Foreign currencies

A An established exporter will almost always be able to quote and invoice you in **pounds**.

- You may want to negotiate payment in a foreign currency, if it results in other concessions from your supplier.
- If you agree to pay in a foreign currency, you will be exposed to a foreign exchange risk.

B You can fix the exchange rate by entering into a **forward foreign exchange** contract with your bank.

- You agree to buy the foreign currency at a fixed price at an agreed future date. The cost of the transaction will be included in the rate you are quoted and depends on the current exchange rate and relative interest rates.

C A **euro bank account** will give you flexibility in sourcing products from the countries that use the currency.

- If you export to and import from the eurozone, euro sales can fund euro purchases and cut your exchange risks.
- Converting into and out of the euro remains an exchange risk as the value of pounds fluctuates against the euro.

3 Payment methods

3.1 **Open account** trading is common within the EU and for suppliers with whom you have an established relationship.

The supplier offers you credit (eg 30 days) in the same way as a UK supplier.

- Confirm exactly when the supplier expects to receive payment (eg 30 days after you assume control of the goods in accordance with the terms of delivery).
- You may be able to negotiate a discount by paying sooner.
- Open account trading may also be a possibility when you are acting as the supplier's agent (eg as a car dealer), particularly if goods are consigned to you or sold on a sale or return basis.

3.2 Suppliers may want to use **documentary collections** to reduce their risk or improve their financing position.

The supplier draws up a bill of exchange. You can negotiate the terms of the bill (eg payment 'at sight' or after 30 days) depending on how you and your supplier want to share the financing burden.

- For a bill that is payable at sight, payment becomes due when the bill and shipping documents are presented to you (usually through your bank).

- For a term bill (eg 30 days), you accept the bill on presentation, guaranteeing to make payment when due.
- Once you accept a bill, you have a contingent liability that will reduce the amount of credit available from your bank.
- Your supplier may be able to use an accepted bill as a means of raising finance.
- The responsibility for bank charges will be agreed in the contract with your supplier and noted on the bill of exchange.

Paperwork

You must have the right documentation to enable you to import goods.

A Goods in free circulation within **the EU** generally require minimal documentation.

However, if your annual imports exceed £600,000, you must provide Intrastat declarations to Customs for statistical purposes (visit www.uktradeinfo.com).

- It is good commercial practice to accompany goods with a commercial invoice that quotes the VAT numbers of all parties involved.
- Certain goods (eg agricultural or chemical goods, or goods subject to excise) require special documentation.

B For goods coming from outside the EU, your **supplier** must provide you with some of the documentation you need. This may include:

- An original invoice (plus three copies).
- A copy of the transport document.
- Any documentation required to prove the origin of the goods. You will need this if you are claiming preferential entry (reduced or zero rates of import duty for certain goods imported from certain countries).

C For imports worth **more than £6,500**, a valuation document is normally required. This is a declaration by the importer (ie you) or sometimes a third party.

D For goods from outside the EU, you may also need an **import licence**. Contact your trade association to find out which government department issues licences for your type of goods; for example, the Rural Payments Agency (RPA) issues import licences for agricultural products and plants and some food and drink.

3.3 Suppliers may want to use a **documentary credit** (or letter of credit) to minimise their risk. You apply to a bank to open a letter of credit. The bank agrees to pay the supplier once the conditions of the credit are met.

- The conditions will require delivery of the correct goods, on time, to the right place. Using a documentary credit allows you to ensure that your supplier provides the paperwork you need (see box).
- Your supplier will usually require a 'confirmed, irrevocable' letter of credit. This is the most secure form of payment. The banks guarantee to pay, even if you, the customer, default.
- Once the overseas bank is satisfied that the terms of the credit have been met, it will pay your supplier.
- A 'term' documentary credit lets you make payment after a set term, and usually involves the issue of a bill of exchange. The cost of the documentary credit will include interest charges to cover this.
- You have to pay your bank for issuing the documentary credit.
- Your bank will reduce the amount of other credit available to you.
- Your supplier can use the documentary credit as a means of raising finance.
- If your supplier requires the protection of a documentary credit but would otherwise be prepared to offer different terms, you can use a standby letter of credit.

3.4 Occasionally a supplier may ask for **payment in advance** for all or part of the order. This is most often used for one-off purchases of low value.

As well as carrying the financing burden, you are at risk from unscrupulous or incompetent suppliers.

- You have little or no protection if the goods are faulty or never arrive. Asking only for a deposit and never sending the goods is a common trick.

4 Financing your payments

There are several ways of financing payments.

4.1 You can use your **own overdraft** facility for small amounts.

4.2 For £100,000 or more, a fixed-term **commercial bill** drawn on your bank and then discounted by the bank can be more cost effective.

4.3 You can arrange financing in a **foreign currency**, typically if you are being invoiced or have other expenditure in that currency.

- You need to manage your exchange rate risk (see box, page 2).

4.4 For goods you plan to sell on, you may be able to arrange **bank finance** against the security of the stored goods.

4.5 If you use **freight forwarders** to handle delivery of the goods, you may be able to negotiate a credit line with them to cover their charges.

Specialist import finance companies can provide a range of financing options to suit your circumstances.

5 VAT and duty

Unless buying on delivered-duty-paid terms, importers are generally responsible for arranging customs clearance and paying any VAT and duty.

5.1 Import **VAT** of 20 per cent is raised on all imports of standard-rated goods.

You need only account for VAT for goods acquired within the EU. You account for input tax as soon as you take possession of the goods.

For goods imported from outside the EU, import VAT must be paid before the goods are released by Customs. You also need to pay VAT on any import duty. However, there are certain ways of deferring payment:

- If you import regularly, you can operate a deferment account, settling your VAT on a rolling basis. You will require a bank guarantee.
- If you need to store the goods before selling them on, you can store them in a customs warehouse. VAT (and duty) only become payable when the goods leave the premises.
- If you intend to re-export the goods after processing them, you can apply for Inward Processing Relief (IPR). VAT (and duty) only become payable if you decide to sell the goods in the UK.

VAT is based on the delivered-duty-paid value of the goods.

5.2 You may be required to pay import **duty**.

- There is no duty on goods that are in 'free circulation' within the EU. Goods are in free circulation if they originate from an EU country, or have already been imported with all customs charges paid, into an EU country.
- For goods that are imported from outside the EU, the rate of duty will depend on the product and the country of origin. Rates of duty can vary suddenly and without warning, and can have a significant effect on the value of goods.

Duty is based on the cost, insurance and freight (CIF) value.

6 Making payment

6.1 Electronic transfer systems are fast, straightforward and secure.

- You can usually arrange for a same day or overnight transfer. A typical transfer cost might be £20 for amounts up to £10,000.
- Your supplier's bank may delay crediting the funds to the supplier's account and may also charge the supplier.
- If you make regular small payments to suppliers in a particular country, you may want to open and maintain a bank account in that country (usually in the local currency).

You can periodically transfer funds from the UK to that bank account (if necessary, using a foreign exchange transaction to convert the funds to local currency).

6.2 Other payment methods can incur lower charges but take longer and are less secure.

The most common is a banker's draft, issued by your bank and payable to your customer.

- A banker's draft can be issued in any major currency. Your bank will charge you for issuing the banker's draft, typically starting at £10.
- You send the banker's draft to your supplier, who can cash it on receipt.

You can periodically transfer funds from the UK to that bank account (if necessary, using a foreign exchange transaction to convert the funds to local currency).

© BHP Information Solutions Ltd 2011. ISSN 1369-1996. All rights reserved. No part of this publication may be reproduced or transmitted without the written permission of the publisher. This publication is for general guidance only. The publisher, expert contributors and distributor disclaim all liability for any errors or omissions. Consult your local business support organisation or your professional adviser for help and advice.