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BAFT-IFSA Product Definitions for Open Account Trade Processing and Open Account Trade Finance

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Section 1: Introduction

Banks have provided trade finance services such as processing purchase orders and managing shipping information and associated documentation and have provided financing through traditional trade finance products (namely letters of credit) for centuries. With the advent of the internet and new technologies, the way buyers and sellers interact has evolved. More and more, trade transactions are handled on Open Account terms yet the need for Open Account Trade transaction processing, servicing and financing (that build on the core trade services that banks have long provided) remains.

Open Account Trade is a common term generally used by buyers to pay their suppliers for the purchase of goods without necessarily requiring 3rd party payment guarantees from the buyer. New technologies facilitate collaboration among supply chain partners and provide more precise information, and thus allow banks to provide processing and financing services at various points throughout the life cycle of a trade transaction. These products and services are beneficial to buyers and sellers who have been developing deeper and more collaborative relationships to strengthen their supply chains to gain competitive advantage.

Given the rapid growth of Open Account Trade there is a need for common understanding of the terminology used in these transactions. BAFT-IFSA, as part of its mandate to evaluate and guide standardization, improve risk management and enhance the role and relevance of financial institutions, has established the following definitions to provide clarity on Open Account Trade-related products and services. They describe Open Account Trade life cycles and identify related trade service processing and financing services a bank may provide. Additionally, these definitions provide the necessary flexibility to encourage service customization and differentiation, factors critical to ongoing trade services and trade finance evolution and development.

The definitions herein largely reflect a buyer-centric flow of Open Account Trade. Based on market feedback, BAFT-IFSA will build upon these definitions, including additional seller-centric flows. BAFT-IFSA believes these definitions will help further international standards and documentation to govern Open Account Trade transactions among financial institutions.

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Section 2: Processing/Servicing Definitions

Open Account Processing leverages the existing trade services processing capabilities of financial institutions. It can include purchase order upload to create transactions, document examination and/or data matching, tracing and follow up for payment and payment services. An important activity in Open Account transaction Processing is the exchange and sharing of documents and document data which can be sent to a bank via a number of methods, including paper documents and electronic records hereafter referred to collectively as documents.

These processing activities which are further defined below can trigger Supply Chain Finance opportunities. A bank may engage in some or all of these activities and/or financing opportunities.

1. Purchase Order Advice

A purchase order specifying the goods and terms is created by the buyer. The seller is then notified of the purchase order and other shipping instructions through a collaboration platform, fax, email, portal or other method. Once notified, the buyer may require the seller's acknowledgement.

2. Document Presentment and Data Matching

Documents are created and presented by the seller. Matching criteria under Open Account are defined by the buyer. They may consist of simple checking for the presence of all the required documents or detailed checking of specific data values within or among documents in an automated, semi automated, or manual fashion as defined in the Purchase Order Advice.

3. Discrepancy Handling/Dispute Resolution

If the matching results include discrepancies between the buyer's matching criteria and the presented document data, the buyer is typically notified to determine if the documents will be rejected or approved. For efficiency purposes, the buyer can preauthorize the bank to pay documents where there are no discrepancies. Dispute resolution enables buyers and sellers to resolve disputes related to Open Account activity on-line or via other methods of communication.

4. Management of Approved Invoices/Drafts

The bank manages the approved documents process with respect to potential financing and the scheduling of transaction settlement and/or the collection of invoice proceeds.

5. Document Payment

The buyer pays at maturity (usually the document due date) and the seller is paid or seller's financing (if any) is repaid with any remaining proceeds going to the seller.

6. Documents/Payment Reconciliation

When payment is received, the bank may, on behalf of the buyer and the seller, reconcile payment to the documents' value (usually the invoice/draft value) and keep track of PO balances.

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Section 3: Open Account Trade Finance Definitions

Supply Chain Finance

As applies to Open Account transactions, Supply Chain Finance (SCF) solutions encompass a combination of technology and services that link buyers, sellers, and finance providers to facilitate financing during the life cycle of the Open Account trade transaction and repayment. The below financing opportunities fall within the overall definition of Supply Chain Finance.

1. Purchase Order Commitment to Pay

The buyer's bank issues its commitment to pay the seller (at sight or at maturity) once the seller ships and makes available the required documents that match the purchase order and other stipulated conditions. This service allows the seller to take the risk of the bank issuing its commitment to pay instead of that of the buyer.

2. Pre-Shipment Finance

Pre-Shipment Finance, also known as Purchase order financing, is made available to a seller based on a purchase order received from a buyer. This financing can cover all the related working capital needs of the seller including raw materials, wages, packing costs and other pre-shipment expenses. Once the goods are ready, refinancing or repayment can occur.

3. Warehouse Finance

Warehouse financing is a form of trade finance in which goods are held in a warehouse for the buyer, usually by the seller, until needed. At a minimum, warehouse receipts are commonly required as evidence for the financing. Some banks may only do this under structured trade transactions.

4. Post-Shipment Finance

Post-shipment financing is provided to a seller using the receivable as collateral. The seller presents shipping documents as evidence of a receivable and the bank may also require a bill drawn on the buyer for the goods exported. The bank may prefer to purchase and discount a bill drawn on the buyer for the goods exported.

5. Approved Payables Finance

Approved Payables Financing allows sellers to sell their receivables and/or drafts relating to a particular buyer to a bank at a discount as soon as they are approved by the buyer. This allows the buyer to pay at normal invoice/draft due date and the seller to receive early payment. The bank relies on the creditworthiness of the buyer.

6. Receivables Purchase

Receivables Purchase allows sellers to sell their receivables/drafts relating to one or many buyers to their bank to receive early payment. The bank may require insurance and/or limited or full recourse to the seller to mitigate the risk of the pool of receivables.

7. Flexible Due Date

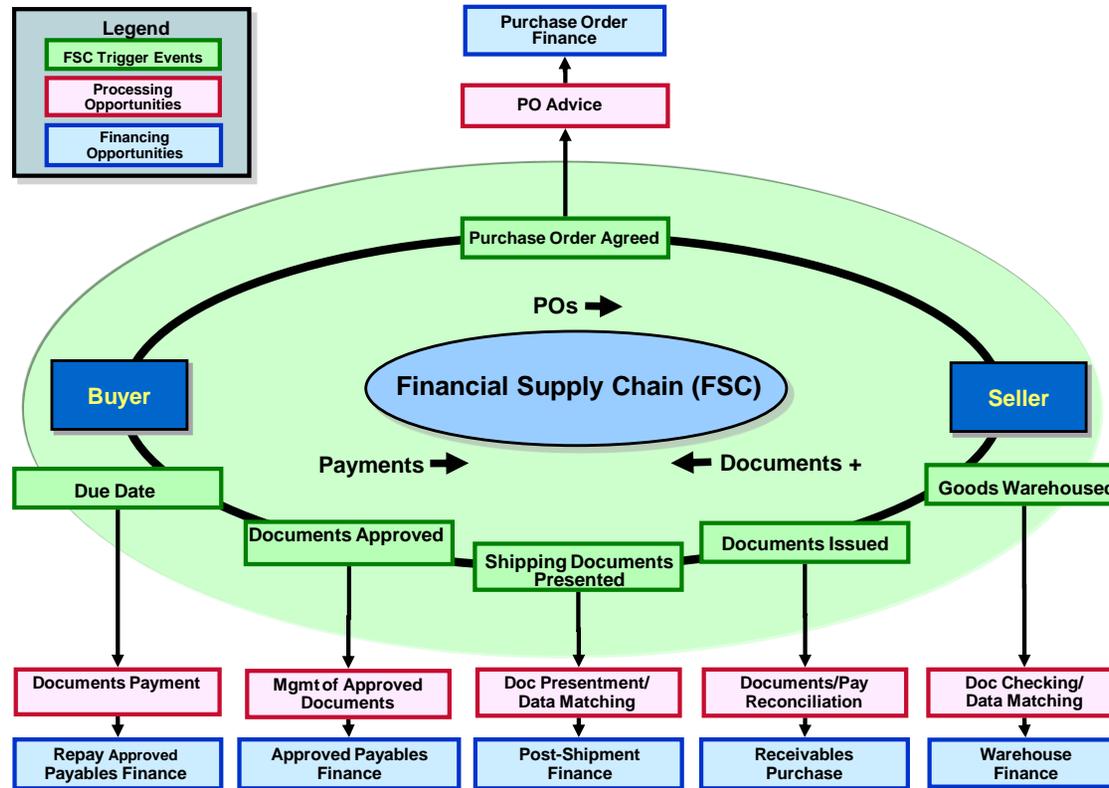
As an alternative to payment on the scheduled repayment date, customers may request payment prior to or following the scheduled due date. Repayment prior to the scheduled date would result in expected prepayment discount, while extensions of due date would equate to additional financing.

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Section 4: Opportunities Diagram

Open Account Processing and Financing Opportunities



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Section 5: Opportunities Matrix

| Supply Chain Finance Trigger Events | Bank Processing Opportunity | Bank Financing Opportunity |
|-------------------------------------|---|---------------------------------|
| Purchase Order Agreed | Purchase Order Advice | Pre-Shipment Finance |
| Goods Warehoused | Document Checking/Data Matching | Warehouse Finance |
| Documents Issued | Documents/Purchase Order Reconciliation | Receivables Purchase |
| Documents Presented | Document Checking/Data Matching | Post-Shipment Finance |
| Documents Approved | Management of Approved Documents | Approved Payables Finance |
| Due Date | Document Payment | Repay any outstanding financing |