Chapter 2
Cash-in-Advance

With the cash-in-advance payment method, the exporter can eliminate credit risk or the risk of non-payment since payment is received prior to the transfer of ownership of the goods. Wire transfers and credit cards are the most commonly used cash-in-advance options available to exporters. With the advancement of the Internet, escrow services are becoming another cash-in-advance option for small export transactions. However, requiring payment in advance is the least attractive option for the buyer, because it tends to create cash-flow problems, and it often is not a competitive option for the exporter especially when the buyer has other vendors to choose from. In addition, foreign buyers are often concerned that the goods may not be sent if payment is made in advance. Exporters who insist on cash-in-advance as their sole payment method for doing business may lose out to competitors who are willing to offer more attractive payment terms.

Key Points

- Full or significant partial payment is required, usually via credit card or bank or wire transfer or escrow service, before the ownership of the goods is transferred.
- Cash-in-advance, especially a wire transfer, is the most secure and least risky method of international trading for exporters and, consequently, the least secure and an unattractive method for importers. However, both the credit risk and the competitive landscape must be considered.
- Exporters may select credit cards as a viable cash- in-advance option, especially for small consumer goods transactions.
- Exporters may also select escrow services as a mutually beneficial cash-in-advance option for small transactions with importers who demand assurance that the goods will be sent in exchange for advance payment.
- Insisting on cash-in-advance could, ultimately, cause exporters to lose customers to competitors who are willing offer more favorable payment terms to foreign buyers.
- Creditworthy foreign buyers, who prefer greater security and better cash utilization, may find cash-in-advance unacceptable and simply walk away from the deal.

CHARACTERISTICS OF CASH-IN-ADVANCE

Applicability

Recommended for use in high-risk trade relationships or export markets, and appropriate for small export transactions

Risk

Exporter is exposed to virtually no risk as the burden of risk is placed almost completely on the importer.

Pros

- Payment before shipment
- Eliminates risk of non-payment

Cons

- May lose customers to competitors over payment terms
- No additional earnings through financing operations

Wire Transfer: Most Secure and Preferred Cash-in-Advance Method

An international wire transfer is commonly used and is almost immediate. Exporters should provide clear routing instructions to the importer when using this method, including the receiving bank's name and address, SWIFT (Society for Worldwide Interbank Financial Telecommunication) address, and ABA (American Bankers Association) number, as well as the seller's name and address, bank account title, and account number. The fee for an international wire transfer can be paid by the sender (importer) or it can be deducted from the receiver's (exporter's) account.

Credit Card: A Viable Cash-in-Advance Method

Exporters who sell directly to foreign buyers may select credit cards as a viable cash-in-advance option, especially for small consumer goods transactions. Exporters should check with their credit card companies for specific rules on international use of credit cards. The rules governing international credit card transactions differ from those for domestic use. Because international credit card transactions are typically placed using the Web, telephone, or fax, which facilitate fraudulent transactions, proper precautions should be taken to determine the validity of transactions before the goods are shipped. Although exporters must tolerate the fees charged by credit card companies and assume the risk of unfounded disputes, credit cards may help the business grow because of their convenience and wide acceptance.

Escrow Service: A Mutually Beneficial Cash-in-Advance Method

Exporters may select escrow services as a mutually beneficial cash-in-advance option for small transactions with importers who demand assurance that the goods will be sent in exchange for advance payment. Escrow in international trade is a service that allows both exporter and importer to protect a transaction by placing the funds in the hands of a trusted third party until a specified set of conditions are met. Here's how it works: the importer sends the agreed amount to the escrow service. After payment is verified, the exporter is instructed to ship the goods. Upon delivery, the importer has a pre-determined amount of time to inspect and accept the goods. Once accepted, the funds are released by the escrow service to the exporter. The escrow fee can either be paid in full by one party or split evenly between the exporter and the importer. Cross-border escrow services are offered by international banks and firms that specialize in escrow and other deposit and custody services.

Payment by Check: A Less-Attractive Cash-in-Advance Method

Advance payment using a check drawn on the importer's account and mailed to the exporter will result in a lengthy collection delay of several weeks to months. Therefore, this method may defeat the original intention of receiving payment before shipment. If the check is in U.S. dollars and drawn on a U.S. bank, the collection process is the same as it would be for any U.S. check. However, funds deposited by non-local checks, especially those totaling more than $5,000 on any one day, may not become available for withdrawal for up to 10 business days due to Regulation CC of the Federal Reserve (§ 229.13 (ii)). In addition, if the check is in a foreign currency or drawn on a foreign bank, the collection process can become more complicated and can significantly delay the availability of funds. Moreover, if shipment is made before the check is collected, there is a risk that the check may be returned due to insufficient funds in the buyer's account or even because of a stop-payment order.

When to Use Cash-in-Advance Terms

- The importer is a new customer and/or has a less-established operating history.
- The importer's creditworthiness is doubtful, unsatisfactory, or unverifiable.
- The political and commercial risks of the importer's home country are very high.
- The exporter's product is unique, not available elsewhere, or in heavy demand.
- The exporter operates an Internet-based business where the acceptance of credit card payments is a must to remain competitive.