

# ***SAMPLE CASE STUDIES – International Business***

## **Case Study 1 - Documentary Credit**

### **M/S Auto India**

#### **Introduction**

M/S Auto India is a public limited company; they manufacture SUVs (sports utility vehicle), in technical collaboration with General Motors of USA. The company has established their manufacturing base at Ranjangaon in Pune. They have acquired an area of 250 acres and the total project cost is estimated at Rs 1500 crores. As per the projections, the company is slated to achieve a 25% market share in the Indian market, within a period of two years.

Out of the total project cost, 49% is brought in by General Motors and the rest is tied up with financial institutions, international banks and Indian banks. The working capital is financed by a consortium of banks in which Global bank, Pune branch, is the leader. The company imports many parts of the car engine in a CKD (completely knocked down) condition from General Motors, Detroit, after establishing import letters of credit through its main bankers, Global Bank, Pune Branch.

M/S Auto India approached Global Bank, Pune for opening of import letter of credit as per UCP ICC 600 for USD 100,000, on sight basis, in favour of General Motors, Detroit.

Type of credit	- Irrevocable negotiable
Application	- UCP ICC 600
Applicant	- M/S Auto India, Pune, India
Beneficiary	- M/S General Motors, Detroit, USA
Issuing Bank	- Global Bank, Pune, India
Advising Bank	- The American Bank, New York
Negotiating Bank	- The American Bank, New York
Reimbursing Bank	- International Bank, New York
Availability	- Negotiable at sight
Expiry	- At the counters of The American Bank, New York
Amount	- USD 100,000
Merchandise	- Car engine parts
Quantity and price	- 50 units @ USD 2000 per unit

#### **Circumstances**

##### **Issuing Bank**

Global Bank, Pune issued its irrevocable negotiable credit through its head office in Pune since Global Bank co-ordinated all its accounting and communication functions at its head office. The Bank's head office transmitted the credit through Swift network as

instructed by its Pune branch to General Motors, Detroit, through The American Bank, New York.

### **Advising Bank**

The American Bank, New York advised the credit to General Motors, Detroit on receipt of the swift transmission.

### **Credit**

Along with other conditions, the credit clearly stated that the negotiating bank was to forward the documents directly to Global Bank's head office at Pune.

### **Beneficiary**

After export of the consignment, General Motors, Detroit presented the documents under the credit to The American bank, New York.

### **Negotiating Bank**

The American Bank, New York, examined the documents presented by General Motors and determined that they were in compliance with the terms and conditions of the credit. The American bank negotiated the documents and forwarded the documents, as per the credit terms, to the HO of Global Bank in Pune and claimed reimbursement from International bank, New York.

### **Reimbursing Bank**

International Bank, New York honoured the reimbursement claim by crediting the current account of the American Bank, New York and debiting the account of Global Bank, Pune, in its books.

### **Issuing Bank Head Office**

Global Bank's Head Office, at Pune, received the documents and after internal registration of the documents, forwarded the documents to its Pune Branch by inter-office mail.

### **Issuing Bank Branch**

On receipt of the documents by the Pune branch of Global Bank, they examined the documents and determined that they were discrepant. They were (a) 60 units were shipped instead of 50 units, thereby overdrawing the credit value by USD 2000 (b) Inspection certificate by Auto Inspection Council, USA is not submitted, as per credit terms. Global Bank contacted Auto India for waiver of the discrepancies.

### **Applicant**

Auto India requested for copies of the documents to be forwarded by fax and after reviewing the same, they refused to waive the discrepancies.

**Issuing Bank Branch**

Global Bank, Pune Branch instructed its HO to transmit an authenticated swift to The American Bank, New York stating that Global Bank had rejected the documents for the noted discrepancies, requesting the American Bank's instructions as to disposal of the documents, and demanding a refund of the funds reimbursed.

**Issuing Bank Head Office**

The HO of the Global Bank sent the authenticated swift message to the American Bank, New York, as instructed by its Pune Branch.

**Negotiating Bank**

On receipt of the swift notification advising that Global Bank had rejected the documents for the stated discrepancies, the American Bank informed Global Bank that it did not accept the rejection of the drawing since the Global Bank did not comply with UCP 600 *sub-article 14* for standard examination of documents. Therefore, Global Bank was said to be stopped from dishonouring its irrevocable obligation.

**Issuing Bank**

Global Bank, Pune Branch responded by stating that they acted in accordance with UCP *article 14*, since their action did not exceed five banking days following the day of receipt of the documents at their branch counters after which they scrutinised the documents and determined to refuse them. They maintained that as per *article 14* of UCP 600, they notified about the rejection of the documents, by swift, not later than the close of the fifth banking day following the day of receipt of the documents. They had pointed out all the discrepancies and had informed American Bank, New York that they were holding the documents at the latter's disposal.

**Negotiating Bank**

The American Bank, New York replied as follows:-

We disagree with your position that you acted in accordance with UCP 600 *article 14*. Documents were delivered by courier to your HO as per the terms of the credit, on Monday, January 7, 2008. Your swift notifying rejection of the documents was not sent until Wednesday, Jan 16, 2008 that is, on the eighth banking day after receipt of the documents by your bank.

**Issuing Bank**

Global Bank, Pune Branch, responded by stating that even though its HO received the documents on January 7, 2008; the Global Bank's Pune Branch did not receive the documents until the following Thursday, January 10, 2008, and the swift advice rejecting the documents was sent within the time period permitted in UCP *article 14*.

**Negotiating Bank**

The American Bank, New York, replied that it was not their concern how Global Bank's operational policy impacted on their inability to comply with UCP. The American Bank, New York stated that in accordance with the credit terms and conditions, documents were negotiated by them and forwarded to Global Bank's HO by courier. The documents were

received by Global Bank on Jan 7, 2008, and any notice of rejection of the documents should have been given within the close of the fifth banking day following receipt of the documents. Global Bank's Pune Branch failed to do so. Therefore, the American Bank, New York's position was firm relative to UCP 600 *article 14* and they would not refund the funds reimbursed.

### ***Questions***

- 1) Was Global Bank, Pune Branch correct in its argument, as the credit issuing bank?
- 2) Was the stand taken by The American Bank, New York correct, as the negotiating bank?

### ***Possible Solutions***

1) Global Bank, Pune was incorrect in its interpretation of UCP 600 *article 14*. The credit clearly stated that it expired at the counters of the negotiating bank and that the documents were to be sent to the head office of Global Bank. The credit did not contain any indication that presentation at the counters of Global Bank's head office was for administrative purposes only, and that effective presentation to the issuing bank would only be considered when the issuing bank had received the required documents. UCP 600 *article 6* states that presentation of documents must be made to issuing bank, or the confirming bank, if any, or any other nominated bank. The beneficiary presented the documents to the nominated negotiating bank and American Bank, New York presented the documents to the issuing bank as instructed. Therefore, Global bank's Pune Branch had a duty to determine the number of days remaining in the five banking day period after presentation of the documents at their head office in order to comply with *article 14* of UCP 600.

2) Yes, the stand taken by American Bank, New York, as the negotiating bank, is correct. As per the terms and conditions of the credit, they have negotiated the documents and forwarded the same to Global Bank's head office. The American bank, New York should have received the notice of rejection of the documents within five banking days following the day of receipt of the documents at the counters of the head office of the Global bank. The stand of The American Bank, New York is in concurrence with the *article 14* of UCP 600.

\*\*\*

## **Case Study 2 - Foreign Trade**

### **M/S Taneja Exports, Mumbai**

#### **Introduction**

Mr. Gurmeet Taneja and Mr. Rahul Khatri are partners of M/S Taneja exports, Mumbai. Both of them qualified from IIFT, New Delhi in the year 2002. They declined lucrative corporate job offers, since they have decided to plunge into the world of international business.

M/S Taneja Exports is registered as a partnership firm, with Mr. Gurmeet Taneja and Mr. Rahul Khatri sharing the profits in the ratio of 60: 40.

The partners had conducted in depth market survey in the domestic as well as international markets regarding the demand of women's apparels in cotton and hosiery. They have taken the assistance of Apparel export promotion council and the marketing agencies in various countries of European Union.

On account of their knowledge in foreign trade, they were able to quickly assess that Indian exporters have not succeeded in penetrating into the huge apparel market of Europe. They found out that the main reasons were ineffective marketing, improper quality control and non adherence to the shipping schedules. Mr. Gurmeet concentrated on marketing of the cotton and hosiery apparels abroad and Mr. Rahul ensured on the procurement of the raw materials and timely execution of shipments.

The firm had taken an industrial gala, measuring 700 sq ft, at 501, Mangal Das market, Lower Parel, Mumbai. They were paying a monthly rent of Rs. 35,000/- for the office premises and the stock of garments was kept in a godown in the same gala area, for which the rent payable was Rs. 15,000/- pm

The firm was sourcing their raw materials from the south Indian towns of Tirupur and Coimbatore. As per the export orders, they were providing the raw materials for job works in Mumbai and subject the samples to rigorous quality and specification checks. The firm had employed 2 accounts staff and 3 contract workers to attend to daily office and godown activities.

The firm was able to achieve steady improvement in export sales due to the stringent quality control measures and timely execution of shipment schedules. The following were the credit facilities enjoyed from M/S International Bank of India, Fort branch, Mumbai.

<b>Facility (Amount in Lakhs)</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
<b><i>Fund based</i></b>			
a) Export packing credit	5.00	7.00	10.00
b) Foreign bill purchased/Foreign bill negotiated	5.00	7.00	10.00
<b><i>Non Fund based</i></b>			
a) Performance guarantee	2.00	5.00	7.00
<b><i>Export sales</i></b>			
	20.00	30.00	40.00

Towards the security of the credit facilities, the firm had mortgaged the residential house, valued at Rs 85 lakhs, belonging to Mr. Vikram Taneja, father of Mr. Gurmeet Taneja, and stocks valued at Rs 15 lakhs was also hypothecated to the Bank. Mr. Vikram Taneja stood guarantee for the facilities sanctioned to the firm.

M/S Taneja exports used to avail the export packing credit facility from International Bank of India and adjust the same by purchase or negotiation of the export bills drawn on their European buyers. Generally the bills carried a tenor period of 60 days. Most of the export bills were drawn and send for collection through international Bank of India, Mumbai Fort Branch, to the foreign buyer's bankers, based on the confirmed purchase order of the buyer. The bills were paid on the due dates and the conduct of the account on the bank's books was quite satisfactory. Based on the past history and the increase in sales turnover achieved by the firm, the bankers were happy to increase the credit limits from Rs 7 lakhs in 2003 to Rs 17 lakhs in 2005.

On June 17, 2005, the firm submitted an export document to International Bank of India, Fort Branch, for Euro 53000.00, drawn on M/S St Lurn Fashions, Paris. The documents were drawn on 60 days DA terms as per the contract. The merchandise under the export were ladies garments in cotton and hosiery. In the covering letter of the firm to the bank, they had instructed the bank to present the documents to St Lurn, Paris, through their bankers viz, Credit Lyonnais, Paris. The exporter had submitted bills of exchange, bills of lading, commercial invoice, packing list, inspection certificate, certificate of origin and in the bill of exchange it was typed as 'to be co-accepted by credit Lyonnais'.

The International Bank of India took the documents in its books and sent the documents for collection to Credit Lyonnais, Paris. In due course, they received communication from Credit Lyonnais that the documents were accepted by St Lurn and due date of the documents were August 25, 2005. The bankers informed the due date of the bill to Taneja exports. On August 30, 2005, Taneja Exports informed the bankers that they are yet to receive the payment of the bill for Euro 53000.00 in their books. The bank sent a swift message enquiring about the fate and payment of the bill. Two days later the bank received a message from Credit Lyonnais saying that the importer, St Lurn, had become bankrupt and they were unable to pay the bill. International Bank of India informed the same to Taneja Exports. They argued with the bank that they had clearly mentioned in the bills of exchange that the documents were to be released against the co-acceptance of the

French bank only. Immediately the Indian bank send a message to Credit Lyonnais that since the bill of exchange contained the co-acceptance clause by the French bank, they are liable to pay even though the importer had become bankrupt. The French bank refuted the claim of the Indian Bank and intimated that the bank's collection instruction did not contain any co-acceptance clause by the French bank and they had acted as per the provisions in the uniform rules for collection in the ICC publication No 522.

Since payments were not forthcoming, Taneja Exports filed a suit with the National Consumer Forum, New Delhi for deficiency of services by International Bank of India, Mumbai, on November 10, 2005. They put forth the argument that the bank was deficient in not mentioning about the co-acceptance clause in their covering letter to the French bank and in case of non-coacceptance by the French bank they would have returned the documents to India and the exporter could have arranged for an alternate buyer or re-import of the merchandise. This negligence on the part of the bank had caused them total financial loss. After hearing the arguments of both the parties, The National Consumer Forum gave the judgement, on February 6, 2006, that the International Bank of India was deficient and negligent in their services and ordered them to compensate the value of the export bill of Euro 53000.00 (approx Rs 24 lakhs) along with 15% interest, till the date of payment.

The bank went on appeal against the order of the consumer forum in the Supreme Court on March 20, 2006. After hearing the counsels of both sides, the Supreme Court gave the judgement that since the original agreement between the exporter and importer do not have any co-acceptance clause by the importer's banker, the co-acceptance clause on the bill of exchange cannot be binding on the French Bank as well as on the Indian Bank. The bankruptcy of the importer is the reason for loss to the exporter and not the deficiency of service by the bank. The Supreme Court set aside the judgement of the National consumer forum and passed the judgement in favour of the bank, with costs, on March 15, 2007.

### *Questions*

- 1) Elaborate the deficiency of service on the part of the bank, pointed out by the National consumer redressal forum, in the light of the uniform rules for collection ICC publication No.522.
- 2) Advise the firm about the precautions they should have taken to avoid such a colossal business loss.
- 3) Discuss the remedial measures the bank in India should take to avoid such damaging judgements by the consumer forums.
- 4) Elaborate the Supreme Court judgement in the context of the international banking rules and practises, as guided by the ICC publications.

### *Possible Solutions*

1) All the export documentary collection bills are governed by uniform rules for collection ICC (International chamber of commerce) publication No. 522. As per article 4a (1) of URC ICC 522, 'All documents sent for collection must be accompanied by a collection instruction indicating that the collection is subject to URC 522 and giving complete and precise instructions. Banks are permitted to act upon the instructions given in such collection instruction, and in accordance with these rules'. We cannot find fault with the French bank since they have acted according to the instruction contained in the covering letter of the remitting bank, which contained no instructions regarding the co-acceptance of the documents by the collecting bank (French Bank). In this case, the remitting bank had failed to undertake proper scrutiny of the collection documents received by them.

2) The exporter should not invent and provide any unilateral directions without the underlying agreement and concurrence of the importer and his bank. The co-acceptance of the documents was not agreed upon by the importer and his banker, viz Credit Lyonnais, Paris. The exporter should have taken ECGC's (Export Credit Guarantee Corporation of India) buyer wise credit limit, which would have come to his help in the case of default due to bankruptcies of the buyer.

3) The Bank's trade finance desk should be manned by qualified and trained personnel. The person handling the export document can find out the discrepancy (the clause of co-acceptance by the French bank on the bill of exchange) and inform the exporter either to amend it or call for the underlying agreement. This simple step would have saved the reputation, monetary loss and mental agony suffered by the exporter and the bank officials.

4) As per article 4a (2) of URC ICC 522, 'Banks will not examine documents in order to obtain instructions'. The International Bank of India (remitting bank) need not take into account the instructions contained in the body of the documents. Hence, the clause of co-acceptance on the bill of exchange is not binding on the remitting bank as well as collecting bank. There were no express instructions by the exporter to the bank regarding the co-acceptance by the importer's bank in France. Also, there was no express undertaking by the French bank to co-accept the documents. On the forgoing, deficiency of service cannot be charged against the bank.

\*\*\*