Bank Payment Obligation

Combining the risk mitigation and working capital benefits of a letter of credit with the cost benefits and operational efficiencies of open account trade

There is a clear rationale for conducting trade on an open account basis: It is efficient, convenient and helps lower cost. However, there are challenges associated with the open account model, both for buyers and sellers, specifically related to liquidity and risk.

The Bank Payment Obligation (BPO) is an irrevocable undertaking of one bank to pay another bank upon the successful matching of predefined datasets using a data matching engine such as SWIFT's Trade Services Utility (TSU). The BPO enables companies to conduct open account trade with risk mitigation and liquidity benefits similar to that of a letter of credit (LC). At the same time, buyers and sellers retain the cost benefits and operation efficiencies by doing trade on a more integrated basis.

The solution is especially suited for companies that have a high volume or value of trade with established counterparties and are contemplating a move to open account in support of business process improvement and efficiency gains.

As of June 2013:

- 53 financial institutions, including 15 of the top 20 trade banks, have adopted the BPO.
- 30 corporates across various industries are already live or in the process of implementing the BPO instrument.

Understanding BPO

In order to utilize the solution, a company would first execute a BPO agreement with their bank, consistent with the process to initiate any other bank provided service. The buyer's bank would then communicate their obligation to pay the seller's bank – establishing the bank-to bank payment obligation.

The solution may also be used to streamline trade flows under a multibank scenario.

- The bank that issues a BPO (obligor bank) is usually the buyer's bank.
- The beneficiary of a BPO (recipient bank) is usually the seller's bank.
- The criteria required for a successful data match is set up within the TSU or other data matching engine using purchase order data. This is referred to as the "baseline".
- Like an LC, a BPO can be set up for "payment due" on a sight or time basis. For example, payment due "on match" or payment due "30 days from match".
- The data elements required for matching are extracted from relevant open account documents such as purchase orders, commercial invoices, bills of lading and insurance /certificate documents

How BPO works

Setup – establishing the baseline

1. Buyer submits purchase order data to its bank in order to setup a baseline.
2. The baseline is submitted to the seller's bank via the pre-agreed matching engine (e.g. TSU).
3. The seller's bank accepts the submission, typically after obtaining agreement from the seller. This establishes the baseline.
4. A BPO may be included on the original baseline submission or may be added as an amendment to an established baseline.

Payment – effecting the obligation

1. The seller submits the required data to their bank (recipient bank), or presents actual documents that the bank can use to create the dataset(s). The bank then submits the datasets to the TSU.
2. The TSU performs the data matching and provides results to the involved banks.
3. In the case of a mismatch, the obligor bank may choose to either accept or reject the discrepancies.
4. A successful match, or acceptance of a mismatch, binds the obligor bank to pay the recipient bank in accordance with the payment terms of the BPO.

J.P. Morgan can execute BPO transactions.

The International Chamber of Commerce ratified the Uniform Rules for BPO (URBPO) in the spring of 2013; these rules govern the relationship between financial institutions using the BPO.

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For more information, please contact your J.P. Morgan Treasury Services representative or visit jpmorgan.com/trade.

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A differentiated service that benefits buyers and sellers

For buyers

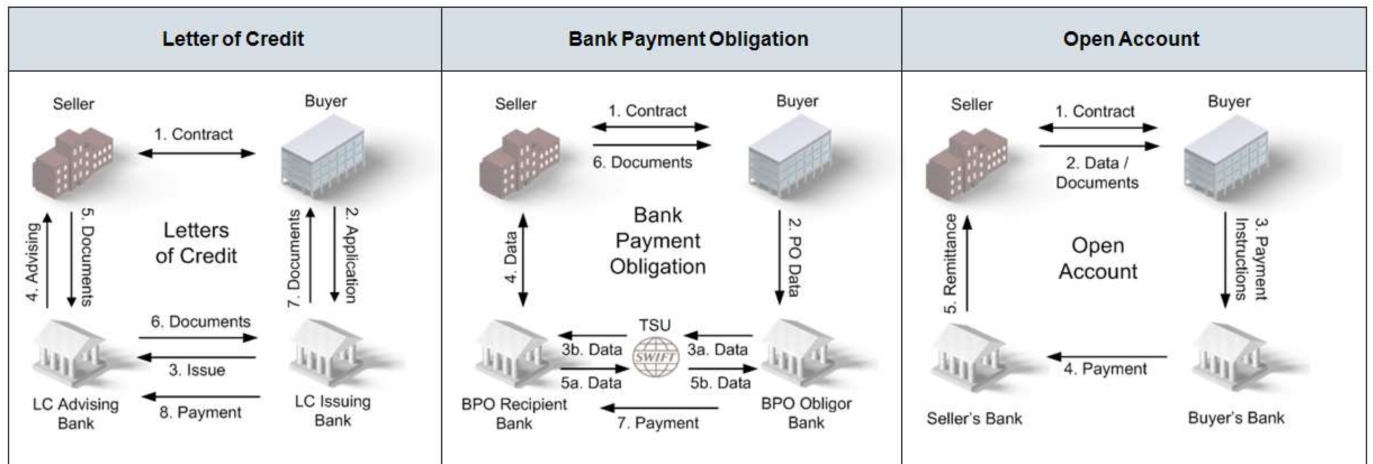
- Secure more favorable pricing, payment terms or higher credit limits from sellers
- Improve credit utilization
- Move to open account terms without the need for additional investment in technology and infrastructure
- Receive trade documentation more quickly
- Enable working capital benefits for sellers

For sellers

- Mitigate payment risk associated with open account trade
- Lower days sales outstanding (DSO)
- Mitigate issuing bank credit and country risk
- Reduce turnaround time and overall costs as compared to letters of credit transactions
- Move receivables off the balance sheet and increase sales by raising buyers' credit limits

Did you know?

J.P. Morgan has been a trade provider since 1800. Our global operating platform and multiproduct solutions are designed to benefit both buyers and their suppliers, providing innovative and effective tools for working capital optimization and risk mitigation. In 2012, J.P. Morgan was named Best Trade Bank in the World by readers of *Trade & Forfaiting Review*. Other Global Trade awards for J.P. Morgan include Best Supply Chain Finance Bank (*Global Trade Review*, 2012), Best Trade/ Online Platform Provider (*Trade & Forfaiting Review*, 2012) and Global Bank of the Year – Risk Management (*Treasury Management International*, 2012).



Process flow comparison between a letter of credit, a TSU bank payment obligation and an open account

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