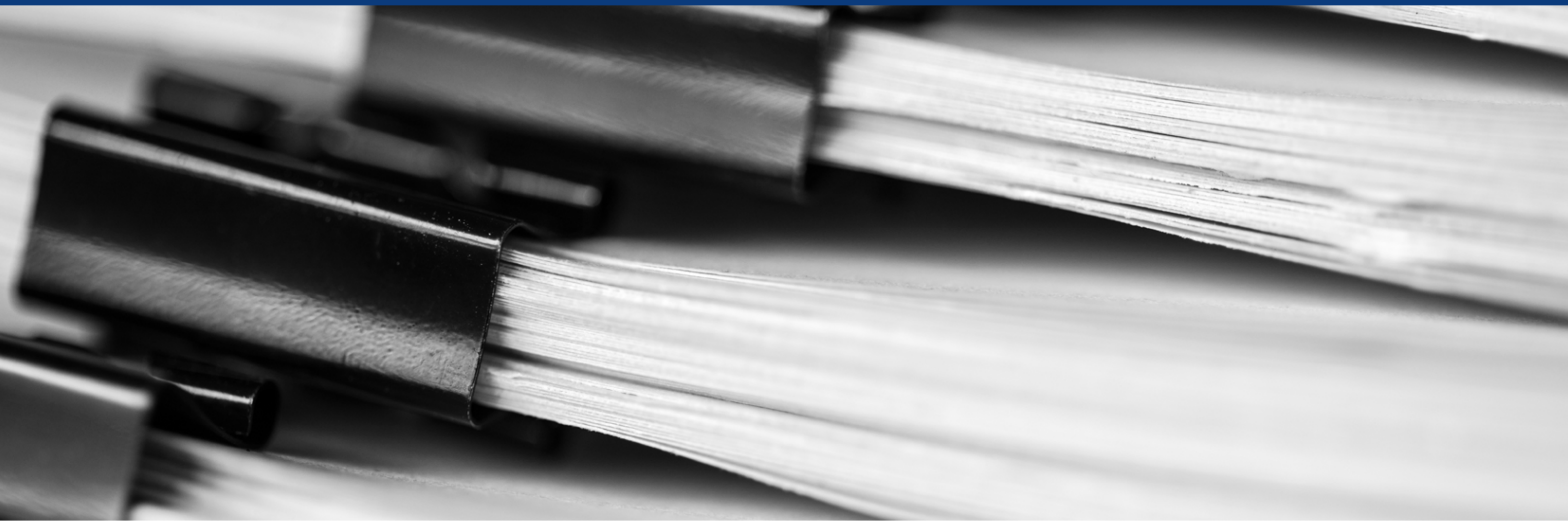


# LETTERS OF CREDIT, THE UCP600 AND DOCUMENTARY REQUIREMENTS

**Letters of credit (LCs) are one of the most common methods of payment for goods in international trade.**

An LC is a contract by which a bank agrees to pay the beneficiary upon the happening of a specific event or, in connection with the export of specific goods, against the presentation of specified documents. The use of LCs to effect payment is widespread in international trade. This is because they offer security of payment for and receipt of goods to contractual counterparties who may be in different jurisdictions to each other – and who may be contracting to buy and sell goods which are located in a third jurisdiction, or which are in transit.

LCs are standalone contracts, separate from the sale contract, and banks are concerned only with the LC contract, not the sale contract. (Article 4 UCP 600). A feature common to all types of LCs is that money is raised on the documents, not on delivery of the goods (Article 5 UCP 600).

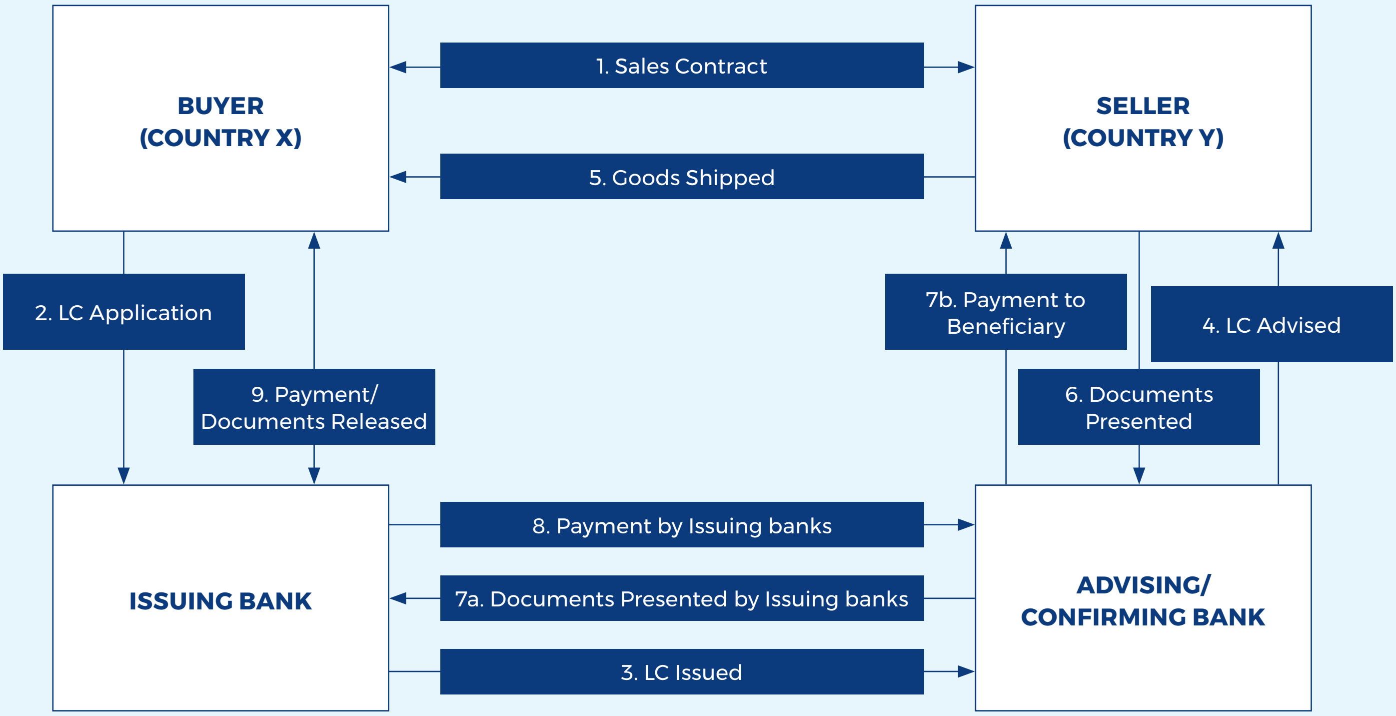
### UCP 600 – What are they and why do they matter?

The Uniform Customs and Practice for Documentary Credits ("UCP") 600 are international rules published by the International Chamber of Commerce (ICC) with the aim of standardising international banking practice in relation to LCs. The UCP 600 are only applicable if they are expressly incorporated (and there is provision for including them at field 40E in the SWIFT MT700). However, although a voluntary code, the majority of LCs are governed by the UCP 600. They are trans-national in application and comprise of 39 articles setting out detailed requirements which govern the scope of a bank's obligations and which reflect universal custom and practice. It is possible to amend their application to an LC by modification or exclusion. The UCP 600 replaced the UCP 500 in July 2007, with the aim of reducing ambiguity and the possibility of rejecting documents.

### Other rules

- ISBP (International Standard Banking Practice) 745: to be read in conjunction with UCP 600 but not incorporated into the LC. This defines terms not defined in UCP 600, such as "shipping documents" and "shipping marks".
- URDG (Uniform Rules on Demand Guarantees) 758: covers demand guarantees and counter guarantees.
- ISP (International Standby Practices) 98: intended to be the standard reference for Standby LCs and more specialised than UCP 600.

## Structure of a Typical Documentary LC Transaction




1. Seller and Buyer agree sales contract – with payment to be made by LC.
2. Buyer requests Issuing Bank to issue the LC – this is the Bank's own irrevocable undertaking to pay the Beneficiary on compliance with conditions. Buyer agrees to indemnify Bank and gives pledge over documents.
3. LC issued and sent to Seller's local bank (known as Advising Bank).
4. Advising Bank examines LC and informs Seller (and adds own undertaking if it is also Confirming Bank).
5. Seller ships goods to Buyer.
6. Seller presents documents under LC to Advising Bank (also called Nominated Bank if nominated as paying bank).
7. (a&b) Documents are checked. If they are in order, payment is made and documents are forwarded to Issuing Bank.
8. Documents are checked and reimbursement is made to Confirming Bank.
9. Documents are released against payment from Buyer (or other arrangements).
10. Buyer uses documents to obtain possession of goods.

### Different Types of LC

- **Documentary** – an obligation by the issuing bank to pay the agreed amount to the beneficiary (usually the seller) on behalf of the applicant (buyer) upon receipt of the specified documents.
- **Standby** – this operates more like a demand guarantee. It is a secondary rather than a primary obligation to pay, usually triggered by non-performance. It does not have to be issued by a bank. The issuer undertakes to pay in the event of default by the applicant and presentation of conforming documents by the beneficiary.
- **Irrevocable/revocable** – A revocable LC can be changed or cancelled by the issuing bank at any time and for any reason. An irrevocable LC offers more security as it cannot be changed or cancelled unless all parties agree.
- **Transferable** – this is an LC with an added provision permitting the bank to transfer the sum specified by the LC to another party at the request of the original beneficiary.
- **Back-to-back** – two LCs, one issued by the buyer's bank to an intermediary and the next issued by the intermediary's bank to the seller, usually to conceal the ultimate seller's identity from the ultimate buyer.
- **Revolving** – a single LC which can cover multiple shipments, so the credit can be renewed either as to the amount or as to the time it is available. These are often used where regular shipments are made from the same seller over a period of time.
- **Sight Credit or Usance Credit** – generally LCs are paid "at sight" of the compliant documents by the bank. A usance credit is not paid at sight but at a future date,

- **Confirmed L/C and Silent Confirmed L/C** – Confirmation is usually requested if the seller is concerned about the creditworthiness of the issuing bank and/or the buyer's country risk. The advising bank adds its confirmation to the LC at the issuing bank's request The advising bank then becomes the confirming bank and undertakes to pay the beneficiary if the LC is complied with (this is a separate undertaking from the one given by the issuing bank and so offers extra security to the seller). Silent confirmation happens when the seller, not the issuing bank, requests confirmation, which is not disclosed to the other parties in the transaction.

### Requirements for documents presented under an LC:

**All documents required under the LC must be submitted.**

**Description:** the description of the goods in the commercial invoice must correspond with that appearing in the LC (Article 18 UCP 600) but other documents may contain a description in general terms provided that it does not conflict with the LC.

**Date:** transport documents and insurance documents must be dated.

**Originality:** original documents are required (Article 17 UCP 600).

**Strict Compliance:** documents must conform strictly to the terms of the LC unless the misdescription or typing error is regarded as trivial.

**Timing of presentation:** documents must be presented to the confirming or issuing bank (as the case may be) within the time limits stated in the LC and within 21 calendar days after the shipment date. (UCP 600 Article 14(c))

**Consistency:** *"Data in a document, when read in context with the credit, the document itself and international standard banking practice, need not be identical to, but must not conflict with, data in that document, any other stipulated document or the credit"*. (UCP 600 Article 14(d))

Some documents carry specific requirements:

- Commercial invoice:
    - The description of the goods must be full and accurate.
    - The amount must not exceed the amount of the credit – but the bank may pay the maximum amount of the credit (UCP 600 Article 18(b)).
    - The name of both beneficiary and applicant must appear.
    - The currency must match the credit.
    - It need not be signed.
- Transport documents (e.g. bill of lading):
    - These must be "clean".
    - They must indicate the name of the carrier
    - They must be signed.
    - There must be full coverage from the place of loading to place of discharge.
    - There must be a full set of originals.
    - A charterparty B/L cannot be used.

Specific requirements also apply to other documents such as insurance documents and certificates.

### Bank's obligations: standard of examination:

The Bank must decide, on the basis of the documents alone, whether the documents appear on their face to be compliant (UCP 600 Article 14(a)). A complying presentation is one that meets the requirements of the credit and the applicable provisions of the UCP 600 and international standard banking practice (UCP 600 Article 2). The Bank has a maximum of 5 banking days following the day of presentation to determine if a presentation is complying. (UCP 600 Article 14(b)). The UCP600 imposes a doctrine of strict compliance – the documents must comply - there is no "de minimis" rule.

### Discrepancies

Documents which comply in all respects will trigger payment under the LC. Where documentary presentations do not comply strictly with the requirements, they are known as discrepant. If the advising bank accepts non-conforming documents it may not be reimbursed by the issuing bank.

#### Ten common examples of discrepancies include:

1. Invoice value exceeds the amount available under the LC.
2. Bills of lading are not clean - meaning they bear notations that call into question the condition of the goods.
3. Bills of lading are not endorsed.
4. Bills of lading are made out "to order" (shipper's order, blank endorsed) but the LC stipulates "straight" (direct to consignee) bills of lading, or vice versa.
5. Not all documents required by the LC are presented.
6. Documents are "stale dated" that is, not presented within a reasonable time after issuance.
7. The invoice does not specify the shipment terms (CIF, FOB, etc.) as stated in the LC.
8. The invoice is not signed as the LC requires.
9. Late shipment.
10. Shipment to/from incorrect ports.

### Treatment of discrepancies

UCP 600 Article 16 deals with discrepant documents, waiver and notice. Where documents do not comply, the bank may:

- Refuse to honour the credit.
- In its sole discretion, approach the applicant for a waiver of the discrepancies.
- If the bank refuses to honour the credit, it must give a notice stating this and listing each discrepancy. It must state:
  - that the bank is holding the documents pending further instructions from the presenter; or
  - that the bank is holding the documents pending a waiver from the applicant; or
  - that the bank is returning the documents; or
  - that the bank is acting in accordance with instructions previously received from the presenter.

If an Issuing or Confirming bank fails to follow this procedure, it will be prevented from claiming that the documents presented are not compliant.

Notwithstanding the doctrine of strict compliance, courts will ignore trivial defects. These have been held to include listing a buyer's telex number with one digit incorrect. Trivial defects were found not to include:

- Referring to goods as "Any Western Brand-Indonesia (Inalum Brand) instead of "Any Western Brand".
- Certifying courier charges at issuing bank's cost rather than at beneficiary's cost.
- Specifying minimum protein content as 67% rather than 70% required.
- Omission of an ampersand ("&") or the word "and" from the name of a company.

**Published: March 2018**

**This client guide was produced by Andrew Williams. Should you require any further information or assistance with any of the issues dealt with here, please do not hesitate to contact him or your usual HFW contact to discuss.**


**ANDREW WILLIAMS**
Partner, London
**T** +44 (0)20 7264 8184
**E** brian.perrott@hfw.com


**Should you be interested in any of our other client guides please contact:**


**CLAIRE MCNAMARA**
Director of Knowledge Management
**T** +44 (0)20 7264 8021
**E** claire.mcnamara@hfw.com



**AMANDA RATHBONE**
Professional Support Lawyer
**T** +44 (0)20 7264 8397
**E** amanda.rathbone@hfw.com