

SITPRO

International Trade Guides

Financial

Letters of Credit Checklist and Guide for Exporters

Letters of Credit - Checklist and Guide for Exporters

SITPRO has produced a set of three **Letters of Credit Checklist and Guides** for Importers, Exporters and Export Sales Representatives. The checklist designed for importers is to be used by purchasing staff when applying to local banks for letters of credit. The export sales representative's guide advises on credits and some of the other responsibilities assumed on overseas visits. We strongly recommend you provide your customers with copies of these guides to back-up your own discussions with them.

This checklist is intended primarily for use in export sales and shipping departments. It will also be of assistance to those involved in financial and credit management and in production and supply. To ensure a letter of credit is workable, trouble-free and provides security of payment, it is essential to take simple yet effective precautions at the start. Working through the checkpoints set out in the various sections of the guide will help reduce discrepancies and associated unplanned costs.

Successive surveys by SITPRO and others have shown that well in excess of fifty percent of documents presented by exporters to banks for payment under letters of credit are rejected on first presentation. This can cause expensive delays for both the exporter and the importer and may even result in a lesser payment or no payment at all. A great many of those rejections could be avoided if more care was taken to ensure that the documents called for in the credit are properly completed.

The SITPRO **Letters of Credit Checklists and Guides** are designed to minimise unnecessary costs and risk when trading on the basis of letters of credit. They are aligned with and based on interpretation of Uniform Customs & Practice for Documentary Credits (UCP), produced by the International Chamber of Commerce (ICC). The current revision, UCP 600, is available from ICC UK (www.iccuk.net).

Any letter of credit requirements which are still not clear should be referred to your bank for clarification without delay.

Key Checks When the Letter of Credit is Received

Before going any further:

- Check that the letter of credit states that it is subject to the 2007 revision of the Uniform Customs and Practice for Documentary Credits (UCP) of the International Chamber of Commerce (usually referred to as UCP 600 or perhaps "current revision")
- Check the authenticity of the credit. Forgeries are comparatively rare, but dangerous. Credits are normally sent through an Advising/Confirming bank in the UK. Any departure from this routine should be viewed with suspicion, for example if it comes to you direct from overseas. If you do not recognise the UK Advising/Confirming bank, especially if it comes from a UK address asking you to send documents abroad, check its authenticity with your own bank
 - According to UCP 600 Article 9(b), the Advising bank shows it is satisfied that as to the apparent authenticity of the credit by advising the credit
- If you receive an unexpected credit from a buyer unknown to you, even under cover of a seemingly genuine advice from a UK bank, check with the bank that everything is in order - particularly if it calls for goods to be shipped direct to the buyer with only a PO Box number

Having assured yourself on these points, proceed with the key checks. Bear in mind, as mentioned, that over half of credit documents are rejected on first presentation to the banks. The main reason for this is matters that could have been put right, had the credit been checked early enough, were not put right. Making these key checks on the day the credit arrives, consulting other departments accordingly and carrying out the more detailed checks immediately afterwards, will enable difficulties to be spotted in better time to take action.

Check that the type of credit gives you the level of payment security you sought

- A bank in the UK may not state it but credits issued under UCP 600 should be irrevocable

Check that you will be paid at the time you planned

- The credit may specify payment some time after shipment or after documents and/or drafts have been deemed compliant by the paying bank (Nominated or Issuing bank). Additional delays and other problems may arise if payment/acceptance is to take place abroad

Check that both your company name, address and full title and those of the buyer are correct and consistent with all other documents

Check that you can produce the goods, ship them, assemble the documents required and deliver them to the bank, all by the expiry date and within the time limit for presentation of transport documents

- The bank has no discretion under UCP 600 and is not in a position to treat as compliant either documents presented after expiry dates or documents not completely in order

If the credit has been sent electronically to a UK bank ("teletransmitted") check that it provides details of the credit that you can act upon and that is not just a pre-advise

- Unless it says otherwise, and provided it refers to UCP 600, the teletransmitted credit: can be taken as the operative credit; can be safely acted upon; and overrides any later mailed advice. Unless a pre-advise states otherwise, the Issuing bank is bound to follow up the pre-advise by issuing the credit

Check that only those bank charges you agreed to pay are stated to be for your account

- Be careful over bank reimbursing charges with a credit not expressed in sterling

If an alteration or extension is required, complete the detailed checks below to see if there are any other errors, and:

- Contact the buyer without further delay and then ensure that any necessary amendments are received in time
 - If an import licence must be extended, this can take some time
 - If the licence cannot be extended and a new one has to be obtained the delay may well go beyond the expiry date of the credit
- Contact the Advising bank
 - It is unlikely that the Advising bank would make an error or omission: under UCP 600 an Advising bank signifies by advising a credit, that the advice accurately reflects the terms and conditions of the credit

At an early stage, it will be in your best interests to send a copy of the credit to your forwarder or whoever will obtain the transport documents. Similarly with your insurers if insurance is to be covered by you. Telephone instructions alone may easily result in misspellings or other errors and consequent rejection by the bank, or even a wrong type of transport or insurance document may be provided.

Detailed Checks Immediately on Receipt of the Credit

When checking your credit under the headings below, remember that UCP 600 will apply fully unless you have agreed different terms, which are reflected in the credit. One or more of the following checkpoints may thus be overridden by conditions stipulated in your particular credit. If you are still unclear as to what the wording of the credit implies check what UCP 600 has to say on the point and with the UK bank.

Note: It is recommended that the details of the credit be recorded at this point so that a progress check can be updated right through to presentation of the final documents to the bank for payment. The Documentary Letter of Credit Exporters Validation Form available from Chancellor Formecon Ltd provides a convenient way for doing this.

Does the type of credit give you the security of payment you want?

- Irrevocable but carrying only the undertaking of your customer's bank in their country
- Irrevocable and confirmed, carrying the extra and separate undertaking of a second bank, usually in the UK

Is it payable when you want it?

- At sight, when correct documents are presented to the paying bank
- At a later date, such as 90 days after the date of the transport document

Is it payable where you want it?

- In the UK with little or no delay after reasonable time for checking by the paying bank; or
- Abroad, with possible lengthy delays and some risk
 - If you were not expecting payment to be made abroad but are prepared to consider it, be sure you understand your position, i.e. that you are responsible for postal delays in presenting documents overseas within the time limits set by the credit. It also gives less time for replacing non-compliant documents with compliant ones

Note: Under UCP 600, whether a credit is available by sight payment, deferred payment, acceptance or negotiation, a credit can be available with any bank.

Is the value of the credit correct?

- Does it allow for:
 - Any extra agreed costs such as freight or inspection fees
 - Planned variation: "about" or "approximately" in a credit permits up to a $\pm 10\%$ variation in the amount stated of the credit, quantity or the unit price (see Article 30(a) of UCP 600)
 - Unplanned variations: UCP 600 Article 30(b) allows a tolerance of $\pm 5\%$ provided a stipulate number of packing units or individual items is not stated in and the total amount of the drawings does not exceed the credit

Are the terms of delivery the same as you quoted (e.g. FOB, CIF, CIP) and do they match the price properly?

- You will need to specify if you want the delivery terms to form part of the credit terms
 - For example, if you quoted "£10,000 FOB Southampton –Incoterms 2000" and the credit states "£10,000 CIF Hong Kong –Incoterms 2000" you will naturally not be able to recover the freight and insurance
- The paying bank will refuse your documents if you exceed the credit amount or alter any unit price quoted in the credit
- Inconsistent delivery terms are discrepancies and the L/C will be rejected

Company names, addresses and other details

- All details should be correctly spelt and consistently reproduced on all the documents
- Following UCP 600 Article 14(j), addresses need not be the same as stated in the credit, but must be within the same country as the respective addresses mentioned - except when the Applicant's contact details appear as part of the consignee or notify party details on a transport document

Are partial shipments expressly prohibited?

- If not, they are allowed (UCP 600 Article 31(a))

Can you meet the expiry date and also present documents within the transport document time limit?

- You will need to allow for:
 - Production and packing
 - Inspection, if required, and obtaining any inspection certificate or clean report of findings
 - Obtaining other certificates (e.g. certificate of origin)
 - Chamber of Commerce and/or consular work
 - Shipment against availability of transport
 - Assembling and checking documents
 - Presenting documents to the bank
 - The presentation of documents must be completed within 21 days of the date of shipment evidenced by the transport document, unless the credit curtails or extends the period - a credit will more frequently curtail the period
 - The expiry date stipulated in the credit must be adhered to - it is not overridden by the 21-day rule
 - It might be in your interest to ask for an extension on the 21 days - provided it falls within the validity of the contract

Has the export or import licence been obtained with adequate validity?

Are the goods described consistently?

- Descriptions in the L/C should be brief and correspond with the invoice (UCP 600 Article 18(c))
- Details in other documents do not need to be identical to, but should not conflict, with that stated in the invoice and credit (UCP 600 Article 14(d) and (e))

Does the credit restrict the way in which documents are prepared?

- Documents, howsoever prepared, are deemed to be originals provided they are properly authenticated (Article 17 of UCP 600 gives details)

Can you provide the transport document called for?

- "On deck": a clause stating goods may be loaded on deck is acceptable, but it must not state that goods are or will be loaded on deck (UCP 600 Article 26(a))
- "Claused" transport documents: Article 27 of UCP 600 states that banks will only accept clean transport documents (i.e. bearing no clause or notation expressly declaring a defective condition of the goods or packaging)
- The places of acceptance and delivery and, if a bill of lading is called for, the ports of loading and discharge should be checked - the UCP 600 transport articles (Articles 19-24) are precise on this point
- Transport documents may be issued by any party, including freight forwarders, other than a carrier, owner, master or charterer (see UCP 600 Article 14(l))
 - Check that the requirements for the mode of transport are satisfied
- Short form or blank back transport documents are acceptable
- "Intended vessels" and "intended ports of loading" are acceptable in certain circumstances (see UCP 600 Articles 20 and 21 sections (a)(ii) and (iii))
- "Received for carriage" or "received for shipment" documents are not acceptable under UCP 600
 - For Road, Rail and Inland Waterway the transport document can indicate the date of receipt for shipment, dispatch or carriage (UCP 600 Article 24)
 - For Courier and Post, a courier receipt may indicate a date of pickup, and a post receipt or certificate of posting can indicate a date of receipt for transport (UCP 600 Article 25)
- Transshipment: the prohibition of transshipment is inappropriate
 - Under UCP 600 Articles 19-24 (the transport articles), transport documents may indicate goods may or will be transhipped provided the entire carriage is covered by one and the same document, even if the credit prohibits transshipment

Insurance

- Can you obtain insurance cover for the risks specified? If "all risks" is stipulated, banks will accept any "all risks" notation or clauses on insurance documents (UCP 600 Article 28(h)) - remember that "all risk" does not mean all risk
 - Does your quotation cover the cost of insuring the risks specified?
 - Can you provide the right type of insurance document, for example if the credit calls for a policy rather than a certificate? Cover notes are not acceptable
- If you are not asked to arrange marine insurance, for example on Incoterms CFR or CPT sales, have you considered obtaining "seller's interest" or other suitable cover for your own account, if available, outside the terms of the credit?

Can you supply all other documents in the way called for?

- Remember that some documents, such as inspection certificates or consular documents, may take some time to arrange

Interpretation of common business language

- For example, words such as "promptly" and "immediately" are disregarded under UCP (refer to Article 3 of UCP 600 for further information)

What if the credit is wrong or ambiguous on any of the above points?

- Prompt decision and action is necessary on:
 - Whether you can change your plans or paperwork to meet the requirement
 - Whether to ask the customer to amend the credit and who pays for the amendment
 - Whether to let things stand and risk non-payment
 - If in doubt, always consult your own bank and/or the paying bank for advice and make a record of the time, date and outcome of the contact
 - Remember that only the Applicant can authorise amendments, i.e. alterations or extensions, through his bank

When Compiling Documents for Presentation to the Bank

Ensure that:

- Documents presented in the credit are presented as separate documents
 - For example, if a packing list and weight list are required and you have a combined packing and weight list, two original copies of this document will need to be presented
- You have the correct number of originals and/or copies of each; they carry the information called for; the title of each is correct and it is issued by the party specified in the credit
- They do not conflict
 - For example, the shipping marks, quantities/weights, transport details, references, and in general terms the descriptions, must tally so that they clearly relate on their face to the same shipment
- The description of goods is correct
 - They may be described in general terms (not conflicting with the credit) in all documents except the invoice, where the exact contract description should be reproduced
 - Contract details should preferably not be repeated in full in transport documents and some carriers will refuse to enter more than the minimum necessary information. This may cause a discrepancy if the information conflicts with that in the credit or other documents
- Documents are authenticated where necessary - import regulations in some countries still make it essential to sign manually and possibly witness documents and any alterations or additions to them

- Any restrictions in the credit are catered for, for example if short form bills of lading are prohibited

Check each document to ensure that it is in order

Transport Document

- Type of transport document, e.g. sea, air, road, rail, inland waterway, multimodal, courier or postal despatches
- The document should:
 - Indicate the name of the carrier and be signed by the carrier, master (for sea shipments) or named agent
 - Indicate the goods have been dispatched, taken in charge or shipped on board (as appropriate) at the place stated in the credit
 - Indicate the place of dispatch, taken in charge, ports of loading and discharge, and/or the final destination (as appropriate) stated in the credit
- Date of issuance - deemed to be the date of dispatch, taking in charge or shipment, unless otherwise indicated
- Consignor - can be different from beneficiary
- Consignee - can differ from buyer
- Endorsed as may be stipulated in the credit

Insurance Document

- Correct type, e.g. a certificate or policy, and number of documents as stipulated in the credit
- Correct amount stated for insured coverage - the amount must be at least 110% of the CIF or CIP value of the goods (UCP 600 Article 28(f)(ii))
- Same currency as the credit
- Risk covered in the credit
- Date of insurance document no later than date of shipment - unless cover takes effect from date of shipment (UCP 600 Article 28(e))
- Endorsed, if necessary, exactly as required by the credit

Invoice

- Must not contain merchandise not called for in the credit, even if they are stated to be free of charge
 - Invoices listing no-charge goods or samples not included in the credit will be refused
- Invoice heading containing your company's name
- Made out in name of Applicant, expressed and spelt exactly as in the credit
- Same currency as the credit

- Description of goods, including import licence or pro-forma details, price, terms of delivery, and any no-charge goods or samples, worded and spelt exactly as set out in the credit
- Clauses or statements word for word identically spelt and the use of any foreign language specified
- Value not more than the credit permits and the same as any bill of exchange - under certain conditions you may be able to underdraw by up to 5% (see below)
- Quantity: a \pm 5% tolerance is sometimes permitted. Alternatively, the credit may permit a specific variation, e.g. an 'about' amount is equivalent to a \pm 10% tolerance (see Article 30(a) and (b) of UCP 600)
- Produced, signed and authenticated as necessary in a way allowed for by UCP and in the credit (UCP 600 Article 17)

Other Documents

- Correct issuer
- Correct wording or content - avoid unnecessary wording which might confuse the bank checker
- Clearly relate to the goods invoiced
- Tele-transmissions to the Applicant and/or insurer correctly set out, addressed and dated
- Certificates to cover any other credit requirement only where a specific certificate is called for (note UCP 600 Article 14(h))
- Signed, authenticated or endorsed as necessary
- Do not enclose any documents not required by the credit

Bills of Exchange, if any

- Date
- Signature identifies signatory
- Endorsement
- Clause
- Letters of Credit reference number
- Term - sight or usance dates
- Amount and currency
- Words and figures tally
- Drawn on correct party
- Correct document e.g. "sole" or "1st and 2nd of exchange"

Covering note/letter to Nominated bank

- List the documents, preferably in the same order as they appear in the credit
 - Give the name, address, telephone, email and fax details of the correct contact in your office and back-up contact in case of absence
 - Indicate how to pay - cheque or direct to bank account (in which case show bank, branch, sort code, account name and account number)
 - If you have a forward currency contract for a letter of credit payable in foreign currency, provide contract details

Present documents to the bank without delay and within the expiry date and transport document time limit

- All documents must be completed and delivered to the bank by close of business on the expiry date and within the presentation of transport documentation time limit, whichever is earlier; or, if the bank is normally closed on that day, on the next business day
 - Obtain a time/dated receipt where appropriate
- Check the transport document presentation time limit very carefully: presentation must be completed within 21 days of the date of shipment, unless the credit specifies a different period - this may well be earlier than the expiry date of the credit itself or any specified "last date for presentation/negotiation" (Article 14 of UCP 600)
- The import licence expiry date is equally important and it may not be possible to extend this
- If any discrepancies are found and they can be put right, the corrected documents must still be presented to the bank by the original expiry date and within the time permitted from date of shipment evidenced by the transport document
- Check and send any specified documents to the Applicant if required to do so under the terms of the credit, enclosing a copy of your documents schedule as sent with your credit documents when making presentation to the bank for payment

If There Are Discrepancies

Unless you can correct discrepancies in time you will lose your right to payment under the credit and all the cost and effort to obtain security will have been wasted.

What are the options?

- Correct the documents within the original expiry date and within the period allowed after the shipment evidenced by the transport document
- The Issuing bank may approach the Applicant for a waiver of the discrepancy (UCP 600 Article 16(b)) - not normally done at the request of the exporter
- Ask the paying bank to contact the Issuing bank for authority to honour/negotiate the documents despite the discrepancies

- An indemnity, either your own undertaking or one issued by or joined-in by your bank, may be acceptable
 - In such a case you are paid promptly but are still at risk and if the Issuing bank decides not to pay, the money must be repaid to the paying bank with interest
 - Indemnities are often casually issued and financial directors are frequently unaware that a massive contingent liability is building up. (If an indemnity is decided upon, try to arrange a validity of six months maximum)
- The bank may offer to pay under reserve - this has the same practical effect as payment under an indemnity though without the paperwork, but there is normally no time limit applicable
 - Money received has to be paid back with interest if the Issuing bank rejects the discrepant document
- Documents can be sent on an "approval basis" (also called "in trust" or "on collection") to the Issuing bank under the protection of the credit
 - Can seriously hinder cash flow and an unscrupulous buyer may try to take advantage by offering a reduced price for a quick settlement against documents "as presented"
 - With documents "on collection" the Remitting bank (paying bank) should be requested to instruct the issuing bank that release of the documents to the buyer is to be only against payment being authorised in accordance with the credit terms

If the transport document involved is a full set of negotiable bills of lading, these measures normally retain your control over the goods as the buyer cannot take delivery without the documents, which are still in your control. However, in other circumstances, the buyer can obtain the goods without the presentation of documents. Nevertheless, the buyer is in effect being asked whether, after all, they still want the goods and is prepared to accept the discrepancies in the documents. They are quite free to refuse.