

SITPRO

International Trade Guides

Financial

Letters of Credit Checklist and Guide for Export Sales Executives

Letters of Credit

Checklist and Guide for Export Sales Executives

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 exporter's guide is intended primarily for use in export sales and shipping departments. We strongly recommend you provide your customers with copies of these guides to back-up your own discussions with them.

This checklist is intended to help export sales representatives establish a letter of credit with the customer that is clearly understood. It also refers to less secure methods of payment and other responsibilities assumed on overseas visits. To ensure a letter of credit is workable, trouble-free and provides the security of payment for which it is requested in the first place, 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.

Preparation for Negotiations

In order to ensure you have all the information necessary for negotiating a sales contract you may wish to consider the following points:

Financial and credit management

- Individual customer credit limits, both "in house" and credit insurer if applicable - use of credit insurance should never be revealed to customers
- Efficiency of local banking system and customers' situations
- Methods of payment and terms, if other than letters of credit
- Acceptable currencies of sale
- Exchange control regulations and delays in transfers
- Import licence procedures

Legal and Administration

- Terms and conditions of sale
- Agency or distribution arrangements
- Retention of title
- Protest re unaccepted/unpaid bills of exchange
- Consignment stock: restrictions on repatriating unused stock
- Product liability insurance
- Situation re counterfeit supplies
- Settlement of disputes (jurisdiction, arbitration)

Production

- Delivery periods on standard items
- Delays in particular items
- Customer preference for "non-standard" quantity packing
- Pre-shipment requirements
- Third party suppliers and/or sub-contractors

Shipping

- Methods of transport available: direct, transshipment, multimodal
- Frequency of departures
- Approximate costs of alternative methods/routes
- Any complaints re previous shipments
- Type of packing
- Correct Incoterms 2000 term according to contract/transport mode
- Optimum delivery point
- Goods insurance

- Normal documentation
- Special documentation requirement such as...
 - Shipped on board or flight date
 - Shipment "on deck"
 - "Claused" transport documents, and which clauses
 - Delays for consular work or inspection formalities

After-sales service

- Local technical ability
- Spare part stocks

When Negotiating the Order or Contract with the Customer

Do you need to use a letter of credit?

- You may wish to do so: for some new customers; as security for unusually large amounts; or in developing countries where it may be essential to obtain an import licence and allocation of foreign exchange
- If a letter of credit is not needed, there are three other options: documentary collection open account and advance payment

Documentary collection

- If your payment terms are based on documentary collection, you should consider:
 - Local interpretation of "sight", e.g. after vessel's arrival
 - For term payments, bills of exchange to be accepted promptly? Protest action considered?

Open account

- Due date of payment is when funds are to be in the exporter's designated bank account, not payment locally
- Should documents be sent by courier instead of airmail?
- Avoid additional payment delays due to banking weekends - such as with the Middle East

Advance Payment

- Payment is expected by the exporter, in full, prior to the goods being shipped

Preparation for Letters of Credit

Where local regulations require, or where the exporter insists on a letter of credit, the following points should be discussed:

- The credit (irrevocable, even if there is no indication to that effect) may need to be confirmed by a major bank in the UK if political and/or economic conditions are considered a risk

- If unconfirmed, which local banks are acceptable as openers ("Issuing Bank"), bearing in mind a customer will wish to use his own bank
- Currency of payment
- Where payable, and whether paid immediately or after an agreed period. Clearly payment in the UK "at sight" is best, but the customer may want time to pay. Avoid credits payable outside the UK and requiring drafts drawn on the Applicant
- Who pays bank charges abroad and in the UK - this point is often overlooked
- Expiry date of the credit must allow time for production, shipment and presentation of documents to the banks
- Place of presentation of documents: any bank; a specified Nominated bank; or Issuing bank (UCP 600 Article 6)
 - If including transport documents as part of the documents presented UCP 600 permits a maximum of 21 calendar days after shipment for presentation, unless stipulated otherwise in the credit - the customer may prefer less, you may require more, but it must be made clear in the credit (Article 14(c))

In order to represent the sales contract properly, complete the bank application form with your customer, watching for points in the following list. Take a copy of the form to check against the credit when your company receives it.

Note: The L/C should be kept simple and refer to rather than recreate the sales contract. For example, it is preferable to state, "goods provided as per sales contract [number]" rather than reproduce the full goods description.

General

- All name and address details complete and correct
- Instructions given for confirmation where required
- Instructions as to preferred Advising bank in the UK - this may be determined by correspondent bank relationships, despite any exporter preference
 - A credit, however available, can under UCP 600 be available with any bank - this does not restrict you as the exporter to presenting documents to the Advising bank for settlement
- Presentation of documents in UK unless otherwise arranged
- Correct indication whether credit specifies payment, deferred payment, acceptance or negotiation

Price

- Delivery Terms (e.g. FCA Barking ICD - Incoterms 2000; CFR Mombasa - Incoterms 2000)
- Currency

- Tenor: period for payment (e.g. "on sight"; 60 days from date of transport document)
- Extra costs to be added to basic price such as freight, insurance, inspection, consular formalities, certificates of origin
- Final value in selected currency including extra costs
- Variations for value or quantities (e.g. "maximum £XXX"; "10% more or less")
- Allocation of bank charges in your customer's country and elsewhere
 - If the credit is in the currency other than sterling, check the customer understands about reimbursing banks charges

Insurance

- It is recommended that you and your customer should pin down in the contract of sale exactly what insurance provisions are needed
 - Can you obtain insurance cover for the risks specified?
 - 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 your customer has not asked you to arrange marine insurance on Incoterms CFR or CPT sales, for example, have you considered "seller's interest" or other CPT suitable cover for your own account, if available?

Production and Despatch Schedules

- Latest shipment date and subsequent credit expiry date should 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;
 - Documentation including obtaining shipping documents;
 - Whether partial shipments are involved; and/or
 - If the credit or import licence expiry dates are already determined by import regulations, can the production and dispatch schedule be met on time?

Presentation

- Will you need more than UCP 600 maximum allowance of 21 days for presentation of documents after date of transport document due to particular requirements?
- Where is the bank that the documents will have to be presented to obtain settlement (i.e. UK or abroad)?
 - Bear in mind that with presentation abroad, the exporter carries risk of loss/delay in post and has less time for correction of discrepant documents

Delivery to Customer

- What type of transport will be used? Match the type of transport documents to the method and delivery, particularly where container or groupage services are to be used
- For containerised goods:
 - Agree places of despatch and delivery (ignoring ports)
 - Avoid the terms "shipped" and "marine/ocean bill of lading" (especially "marine" or "ocean" for container or through transport documents)
- For all methods allow the use where necessary of transshipment, "on-deck" shipment and "claused" transport documents (agree "clauses")
- 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
- "Claused" transport documents: UCP 600 Article 27 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)
- "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))
- 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))

The Letter of Credit

- As a matter of routine, the vast majority of credits are communicated by teletransmission using the inter-bank SWIFT system
- Where a credit is issued by mail you may want a pre-advice

Detail - But Important

Ensure these detailed but vital points are settled before concluding discussions - you can save problems with discrepancies later.

- Agree what documents the credit should call for
 - It is recommended not to include the underlying sales contract, pro forma and the like
 - The documents called for should fulfil the requirements stated in the sales contract
- Avoid negotiable transport documents (documents of title) where a non-negotiable transport document fulfils requirements
 - Prevents goods (which are delivered at destination to a named consignee) from being held up waiting for the arrival of documents
- Ensure documents relate clearly to supply of the goods ordered - if no-charge goods or samples are to be sent at the same time, it must be stated in the credit

- Keep documents and the numbers of each to a minimum to avoid greatly increased risk of mistakes, rejection of the documents by the bank and consequent delay in payment and delay in the customer receiving documents to clear the goods
- Be sure the company can supply the documents and comply with the terms proposed by the customer, exactly as specified in the credit
- Check when completing the bank's application form with your customer (or make sure they will do so later) that any unnecessary instructions pre-printed on the form are deleted, such as:
 - "Documents produced by reprographic means not permitted"
 - "Short form bills of lading prohibited"
 - "Partial shipments prohibited"
 - "Transshipment prohibited"
 - "Bills of lading indicating goods may/will be carried on deck prohibited"
 - "Shipped on board/marine ocean bills of lading" (necessary for port-to-port shipments, but restrictive)
- Exchange the names, full titles, full addresses, telephone, email and fax details of the people in the customer's company, and your own, who are in charge of letter of credit shipments. Where you are not completing the form with your customer, make certain they have the full and exact spelling of your company name and address for the credit, and the correct description of the goods without unnecessary detail
- Even where you do complete the application form with the customer, give them a copy of SITPRO's **Letters of Credit Checklist and Guide for Importers** to use when applying for further credits - this will help to keep them as simple as possible
- If in doubt it is important to refer back to your company before making any letter of credit commitment. Ensure before leaving that you have noted the international direct dialling code, the time zone for each company you will be visiting, and important telephone, email and fax details, with individual home numbers as necessary