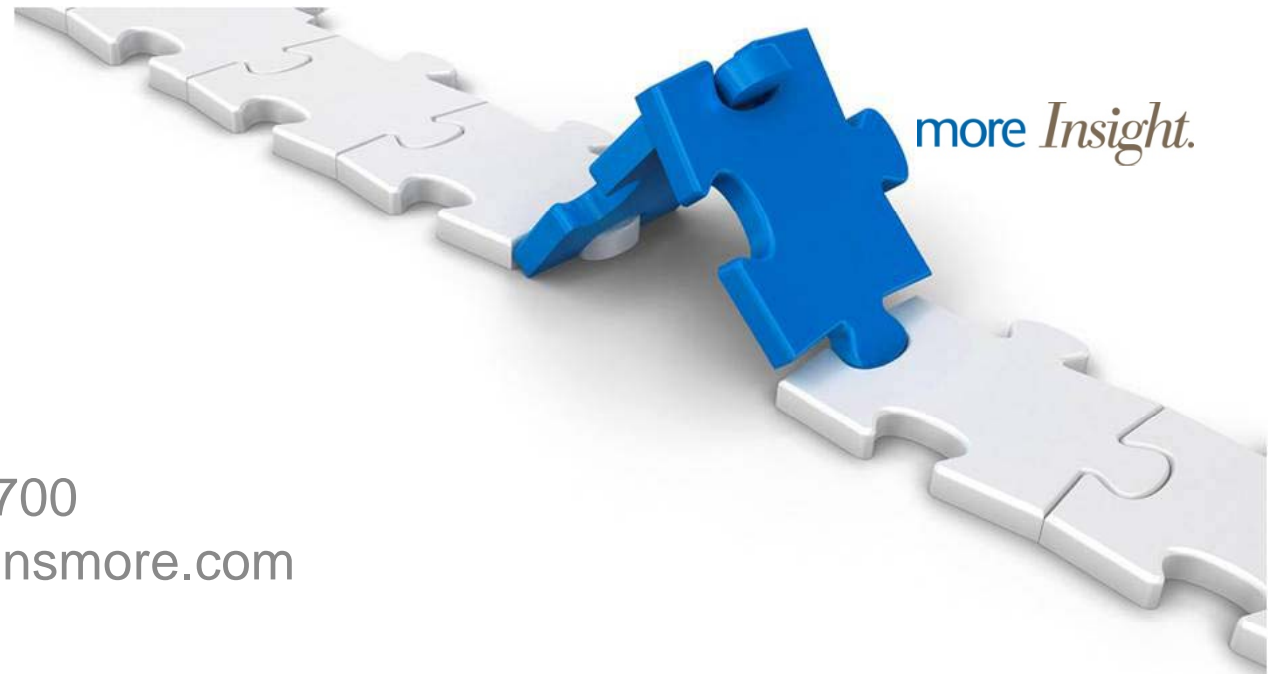




more *Insight.*

Letters of Credit

Tips for Getting Paid



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Presenter

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We will be covering

- What are letters of credit?
- Benefits of use in international trade
- Tips for Getting Paid
- Bank Payment Obligations

Terms

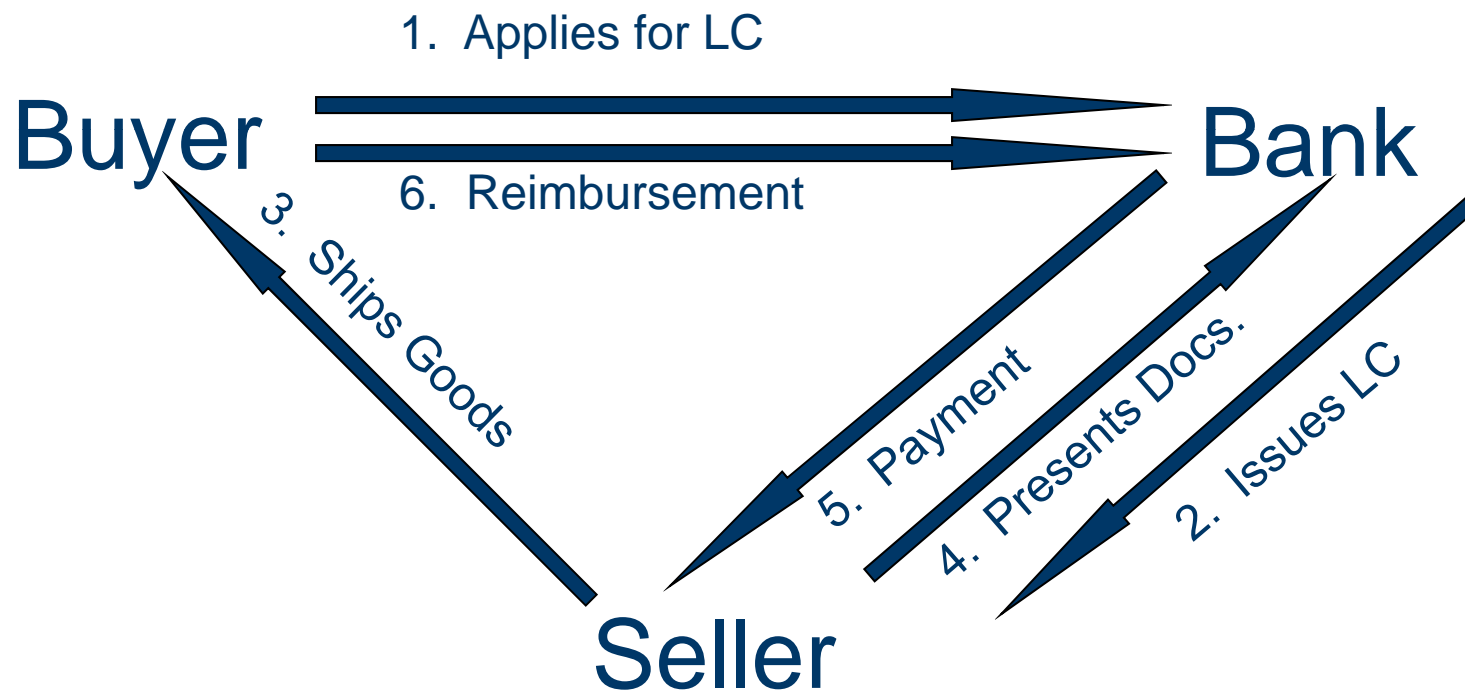
▶ Letter of Credit

- ▶ Bank undertakes to pay a named beneficiary upon the timely presentation of complying documents

▶ Commercial Letter of Credit

- ▶ Bank undertakes to pay to Seller the purchase price of the goods upon receipt of Seller's invoice or other documents evidencing Seller's right to payment of the purchase price
- ▶ Other documents may be transport, insurance, customs, inspection, etc.

Commercial Letter of Credit

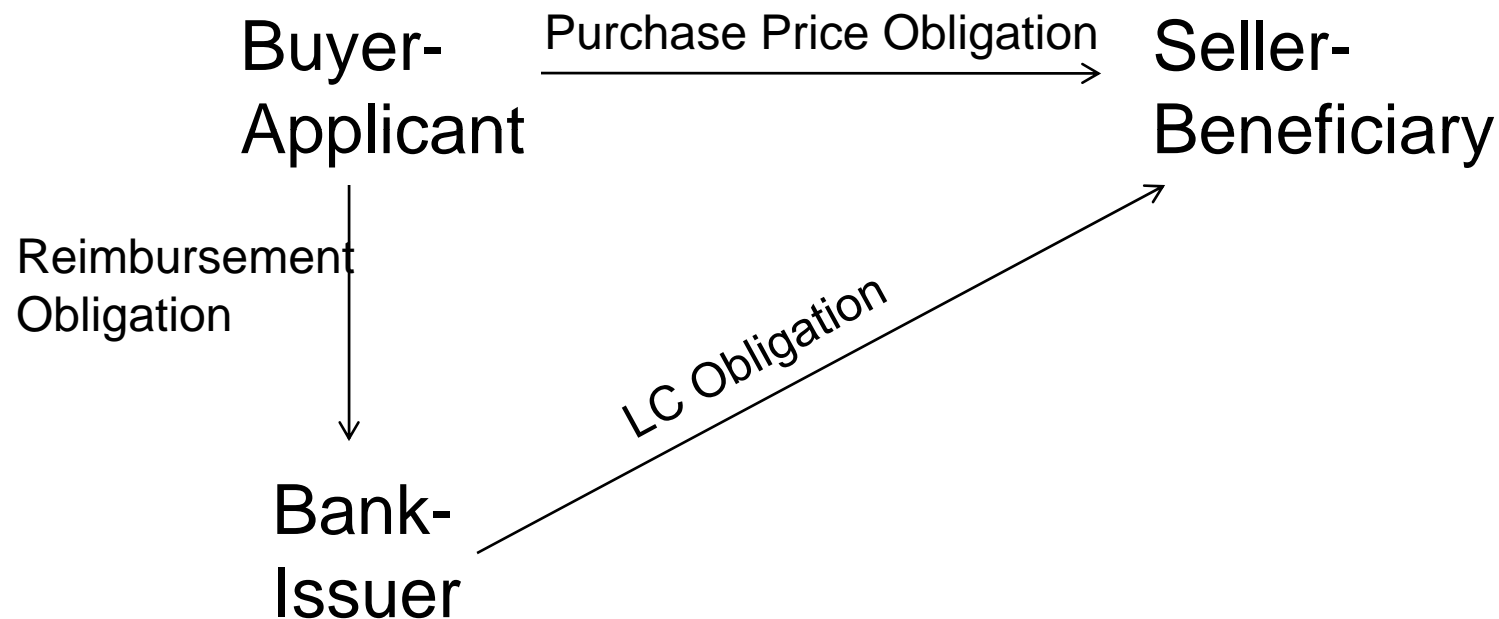


Terms (cont.)

- ▶ “Applicant” applies to “Issuer”, which issues the letter of credit to “Beneficiary”
- ▶ Beneficiary “presents” complying documents to Issuer (or Confirmer, or Nominated Bank)
- ▶ Issuer must “honor” a complying presentation and pay Beneficiary or “dishonor” a non-complying presentation

Commercial Letter of Credit

- ▶ Three independent obligations:

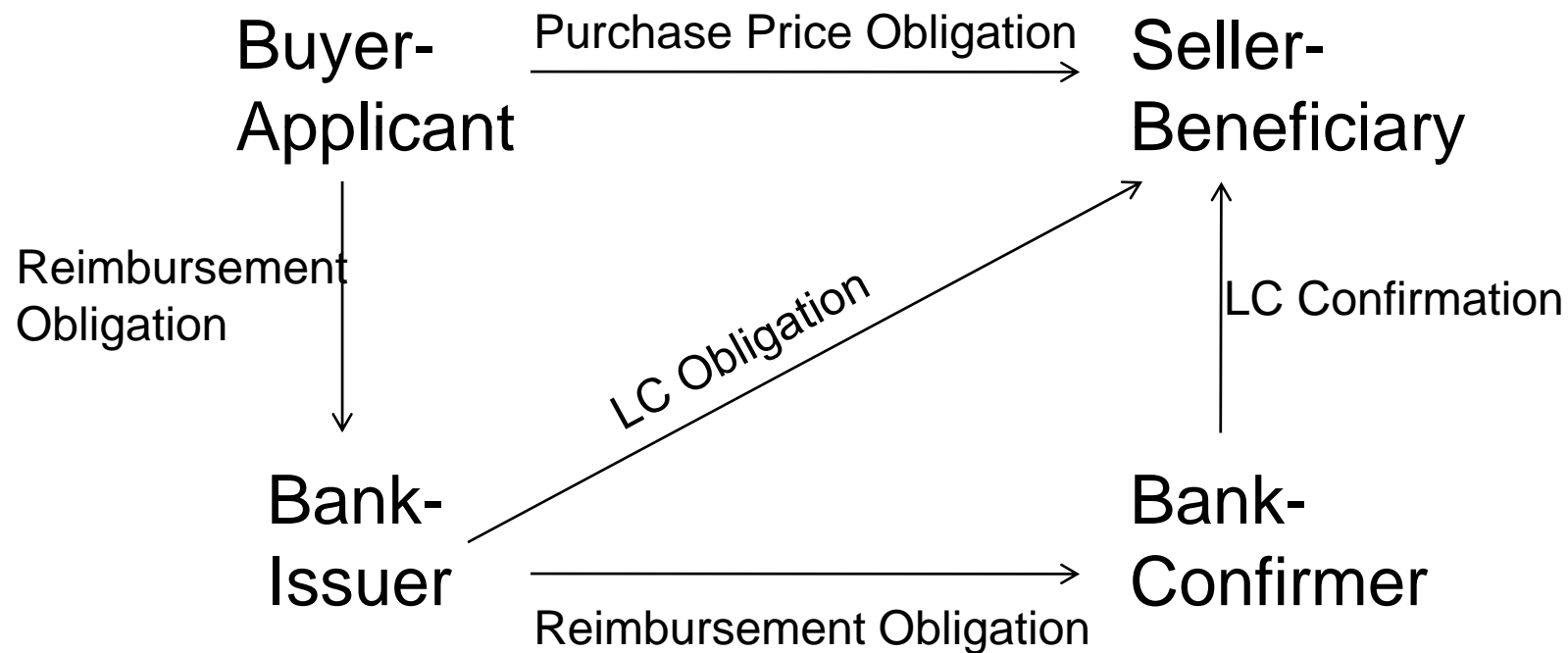


Confirmation

- ▶ If Seller is unfamiliar with Buyer's Bank or cannot trust the letter of credit practice or law in the country where Buyer's Bank is located, the Buyer's Bank may authorize a local bank to confirm the letter of credit
- ▶ Confirming Bank in effect issues a parallel letter of credit to Beneficiary and seeks reimbursement from Buyer's Bank

Confirmation

- ▶ Two additional obligations:



Terms (cont.)

▶ Nominated Bank

- ▶ Issuing Bank may authorize another bank to receive documents and pay Beneficiary
- ▶ Nominated Bank is not authorized to confirm the letter of credit and may not pay until it examines documents and obtains recourse against the Beneficiary
- ▶ Nominated Bank obtains reimbursement from Issuing Bank

Terms (cont.)

▶ Advising Bank

- ▶ Issuing bank may authorize another bank to notify the Beneficiary that the letter of credit has been issued, confirmed, or amended
- ▶ No authorization to pay Beneficiary or seek reimbursement

▶ Negotiating Bank

- ▶ Issuing bank may authorize another bank to purchase documents from the Beneficiary (usually at a discount)

Terms (cont.)

- ▶ Standby Letter of Credit
 - ▶ Obligations are the same: Bank undertakes to pay upon the timely presentation of complying documents
 - ▶ Often used in transactions other than the sale of goods
 - ▶ Beneficiary typically presents a demand with a statement that Applicant is obligated to pay Beneficiary the stated amount

Benefits to Seller

- ▶ Assurance of timely payment
 - ▶ Possibly even before goods manufactured
- ▶ Bank takes risk of insolvency or refusal to pay
- ▶ Payment upon presentation of documents
- ▶ In the event of dispute, Seller is already paid
- ▶ Almost cash advance

Benefits to Buyer

- ▶ Not a cash advance
- ▶ Buyer's bank assesses creditworthiness
- ▶ Can bargain for assurances of quality

Tips for Getting Paid

- ▶ Anticipate issues in the contract
 - ▶ Many problems avoided at this stage
 - ▶ More than just 'letter of credit'
 - ▶ Terms can address
 - ▶ Issuers
 - ▶ Confirmation
 - ▶ Rules
 - ▶ Irrevocable
 - ▶ Terms
 - ▶ Expiration
 - ▶ Law and Forum

Tips for Getting Paid

- ▶ Issuer
 - ▶ Good international reputation
 - ▶ Solvency
 - ▶ LC expertise
 - ▶ “Satisfactory”

Tips for Getting Paid

- ▶ Confirmation
 - ▶ Close to home
 - ▶ Additional undertaking
 - ▶ Added cost

Tips for Getting Paid

▶ Rules

- ▶ Commercial—UCP600
- ▶ Standby—ISP98

▶ Irrevocable

- ▶ Assumed/Default Rule
- ▶ Revocable only if stated

Tips for Getting Paid

▶ Terms

- ▶ Documents

- ▶ Timing

 - ▶ Last day for shipment or presentation

▶ Expiration

- ▶ Meaning

- ▶ Extension

- ▶ Force Majeure

Tips for Getting Paid

▶ Law and Forum

▶ Significance

▶ Options

▶ Local

▶ US

▶ UN Convention on Independent Guarantees and Standby Letters of Credit

Tips for Getting Paid

- ▶ Consider LC as an exhibit
- ▶ Negotiate in advance

Tips for Getting Paid

- ▶ Advising Bank
 - ▶ Authenticate terms
 - ▶ Accuracy of documents
- ▶ Negotiating Bank
 - ▶ No undertaking to act
 - ▶ Buy documents
 - ▶ Silent confirmation

Tips for Getting Paid

▶ Commercial versus Standby

▶ Standby

- ▶ Can be used in ongoing trade
- ▶ Pay in case of default
- ▶ Can save on fees (issuance, amendment, discrepancies)
- ▶ Higher cost than single commercial LC

▶ Commercial

- ▶ Single transaction
- ▶ Sales price to be paid by bank
- ▶ Lower cost on single LC

Tips for Getting Paid

- ▶ Applicant-Controlled Conditions
 - ▶ Veto power
 - ▶ LC banks will enforce

Tips for Getting Paid

- ▶ Discrepancies and Waivers
 - ▶ 60-80% of new presentations are discrepant
 - ▶ Can cure but before expiration?
 - ▶ Verify on all documents:
 - ▶ Descriptions of goods
 - ▶ Names and addresses of parties
 - ▶ Any quoted language

Tips for Getting Paid

▶ Difficult countries

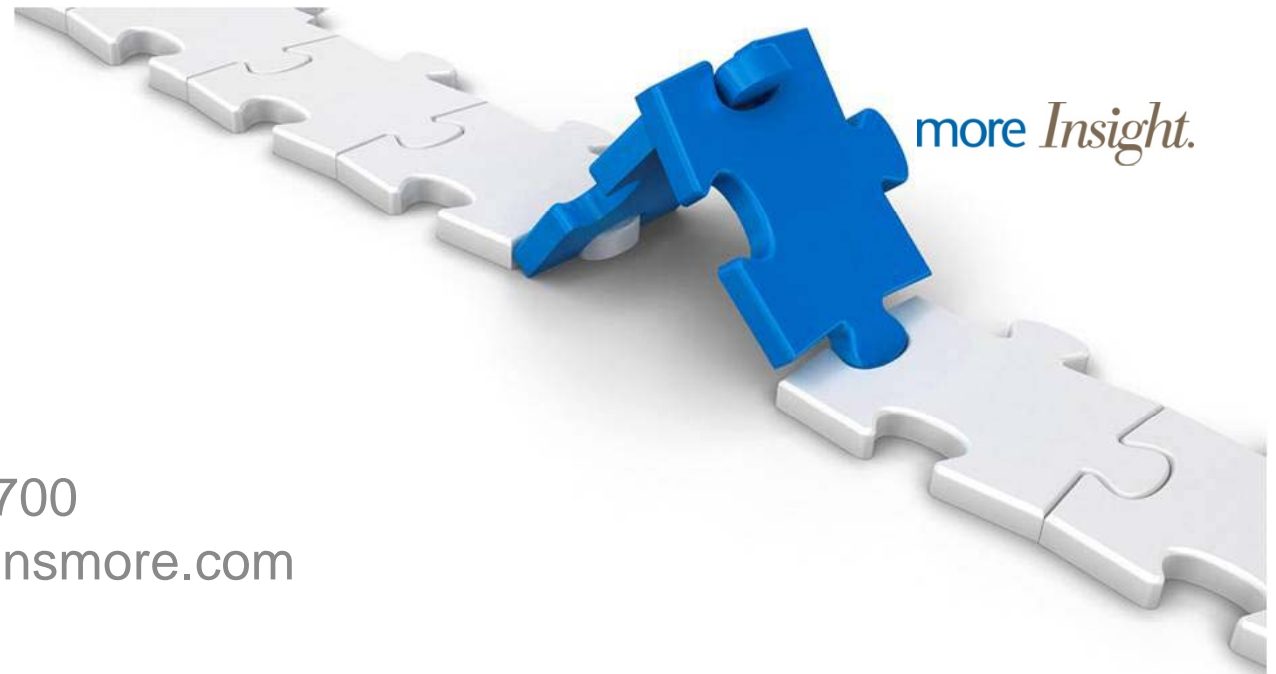
- ▶ Examples (not exhaustive): China, Korea, India, Taiwan, Pakistan
- ▶ Deal with major offices of the banks—not rural
- ▶ Scrutinize documents
 - ▶ If documents in English, notice typical English variations
- ▶ Maintain control over goods
- ▶ Use nominated US bank if possible

Tips for Getting Paid

- ▶ If no payment
 - ▶ Can protest, sue
 - ▶ Jurisdiction may be provided for
 - ▶ Arbitration
 - ▶ Can recover costs under US law
- ▶ Injunctions
 - ▶ Excessively used in some countries
 - ▶ Reserved for LC fraud

Bank Payment Obligations

- ▶ Product of SWIFT (Society for Worldwide Interbank Financial Telecommunication) and ICC
- ▶ To be used in and support open account trade
- ▶ Electronic issuance and presentation
- ▶ Questions
 - ▶ Is it a letter of credit?
 - ▶ Rules/Law?



Questions?

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