

# SITPRO Briefings

*Letter of Credit*



## Checklist and Guide for Importers



#### Introduction

This is one of three SITPRO letter of credit checklists available on our website ([www.sitpro.org.uk](http://www.sitpro.org.uk)). Of the other two, one is designed for export sales executives - for use by executives when visiting customers' countries. The third checklist is designed for UK export departments.

This checklist and Guide is specifically to assist importers. UK exporters may also wish to send copies to overseas buyers as part of their overall customer relations. It details the recommended procedures to be followed, including an item-by-item reference to completing the application form provided by the importer's bank. A simple specimen form is included at the end of this guide and while only an example, will not be found significantly different from those used by banks themselves.

Successive SITPRO and other surveys have shown that well in excess of 50 percent of documents presented by exporters to banks for payment under letters of credit are rejected on first presentation. This risks expensive delays for both the exporter and the importer. A great many of those rejections - possibly as many as half of them - could be avoided if more care were taken to ensure credits properly represent the sales contract.

The purpose of this Checklist is to guide the importer through the process of opening a credit to help in keeping rejections to a minimum. Nevertheless, any requirements of a credit opened using the recommendations outlined here which are still not clear to the supplier should be referred to the advising bank for clarification without delay, or to the importer if the advising bank is unable to assist.

The recommended checks take into account the ICC Uniform Customs & Practises for Documentary Credits (UCP 500). These "rules" reflect worldwide practice and incorporate many years of ICC operational experience to avoid, as far as possible, delays for the importer receiving his documents and for the exporter being paid.

## Arranging for the Letter of Credit

When negotiating the order or contract with your supplier, you should only be thinking of using a letter of credit if your country's exchange control regulations require it or if your supplier insists on it as the means of payment. Otherwise, you should try to avoid the procedure, which as mentioned earlier, can quite often cause problems both for you and your supplier.

If a letter of credit is unavoidable, check with your bank that they are prepared to open one for the value of the intended transaction and on the terms of settlement proposed (i.e. payable at sight or later), and whether it is to be confirmed by a bank in the supplier's country.

Ask the bank to obtain a status report on your supplier, mentioning that a letter of credit will be used.

#### Make sure that you:

- Have exchange control approval for the importation;
- Will be able to obtain any necessary import licence;
- Can pay import deposits and Customs duty on time;
- Check whether forward exchange cover or a foreign currency account is advisable for letters of credit in a currency other than your own.

**Consult other departments in your company** to ensure that the terms of the sales contract and letter of credit meet their requirements.

#### Obtain a copy of your bank's application form for opening a letter of credit to see how your supplier's instructions can best be entered on your bank's form.

In the absence of pre-arranged instructions, try to discuss the sales contract and any requirements for the credit with your supplier's representative to agree how your bank's form should be completed.

However if a representative cannot visit, then read the sales contract very carefully and apply the conditions to your bank's form as appropriate - consult your bank if you have any doubts whatsoever, as UCP 500 requires that they will open the credit according to your instructions.

#### Points to agree with your supplier:

- Who pays the charges for opening (and possibly confirming) the credit; for amendments and or extensions, and subsequent payment charges. Unless you specify otherwise, all those charges will be payable by you as the opener, including those in the supplier's country. If the credit is in a foreign currency, check with your bank on the matter of reimbursing commission.
- The type of letter of credit and its terms. If in doubt discuss them with your bank before you proceed.

#### Should it be:

- Irrevocable, where your bank gives a binding undertaking to the supplier provided all the credit terms and conditions are fulfilled;
- Irrevocable and confirmed, where a bank usually in the supplier's country, adds its own undertaking for which it will charge. Once issued, an irrevocable credit can only be amended by joint agreement of your bank and your supplier and, if confirmed, agreement of the confirming bank as well;

#### When is it to be payable:

- At sight when your supplier presents the correct documents to the paying bank within the time allowed  
or
- At a later date, for example, 90 days after the date of the transport document, but only against

a correct presentation.

**Where it is payable:**

- At the bank in the supplier's country (making it easier for him to deal with any queries over the document)  
or
- At your own bank

Are there any special provisions, such as a transferable letter of credit. Make sure you fully understand any special requirements see UCP 500 Article No. 48 regarding transferable credits.

**Which documents the letter of credit needs to call for** and which, if any, need to be sent direct to you. The paying bank will ignore vague requirements in the credit where a supporting document is not specified.

**What type of transport is available:** Sea, air, road, rail or perhaps a combination of two of more - or possibly post or courier. Include the type of transport document that will be used and who will issue it. Especially check:

- If the goods will be packed in a container;
- If your supplier intends to use a freight forwarders groupage service for small consignments;
- Where the goods will go from and to, and whether there is a direct service;
- If there are any dangerous goods, long lengths, heavy lifts, or awkward pieces which may have to be shipped on deck;
- If the type of product usually attracts claused bills of lading (for example superficial rust on steel products).

All such contingencies have to be allowed for in the letter of credit.

**The expiry date of the letter of credit** must allow time for your supplier as the beneficiary to receive the credit, obtain or manufacture goods, complete arrangements for packaging and transport and to assemble documents prior to presentation. Issuing bank charges are normally levied on a 3 monthly basis, so an expiry date of 3 months from issue or a multiple thereof will be normal in most cases. If the validity proves too short this will likely involve amendments and also lead to delay in despatch. Do not work to the supplier's "ex works" date, but allow further time for shipment, inspection or consular work, assembling documents and presenting them to the bank.

**Check that you have on file the names, full addresses, telephone, email and fax numbers** of the people responsible in both the supplier's company and your company for the day to day handling of letter of credit operations.

**When the letter of credit is to be opened.** If it is to be opened after you have placed your order, ensure your supplier knows as soon as possible what the letter of credit will call for. Possibly by a copy of your application to the bank (although that is no authorisation for him to proceed with manufacture/supply) or by a copy of the actual credit when you receive it from your bank, sent to him directly by you.

**When applying to your bank for a letter of credit**

- Give your bank clear and precise instructions and avoid unnecessary requirements. If a latest shipment/despatch date is to be quoted, this should precede the expiry date by the number of days allowed for presentation of documents. If no latest shipment/despatch date is indicated it will be taken to be the same as the expiry date, which can cause problems for the supplier in presenting documents. (Note UCP 500 Article 42).

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#### State clearly:

- What type of letter of credit has been agreed;
- Who pays what charges, commissions and any other costs;
- The correct value (see item 4 under “Completing the Application Form”). Ensure that it covers the value as laid down in the sales contract, including any agreed variations in quantity, price, or other costs such as freight and insurance, inspection fees etc. (“About” and similar expressions used in conjunction with the credit amount or the quantity of goods or the unit price allows a difference of up to 10% more or 10% less).
- The delivery terms (see item 14 under “Completing the Application Form”) for example £25,000 CFR Singapore (Incoterms 2000). Remember to match documents to delivery terms, e.g.
  - Stipulate “freight paid” on transport document where appropriate
  - Do not call for a certificate of insurance for CFR (C&F) or CPT purchases.It is essential to refer to the appropriate Incoterms 2000 in all sales contracts to establish without doubt the responsibilities of the seller and the buyer during the transit of the goods.
- The beneficiary’s (supplier’s) name and address. Check the spelling, company title (whether Limited, plc and Inc, GmbH etc), and address, exactly as on the supplier’s letterhead or proforma (see item 3 under “Completing the Application Form”).

#### Points to check carefully

- Describe the goods simply, briefly and accurately. You only need enough detail for basic identification, no more (see item 13 under “Completing the Application Form”).
- Do not state “part shipments prohibited” or “transshipment prohibited” unless you have agreed this with your supplier. Note UCP 500 Articles 23(d), 24(d), 26(b) and 27(c) for transshipments and article 40(a) for partial shipment.
- Ensure the expiry date allows time for shipment and presentation of documents to the bank (see item 5 under “Completing the Application Form”).
- Do not use expiry dates as a way of putting pressure on your supplier to improve delivery times.
- Call for the agreed minimum documentation only. The bank’s application form for letters of credit may have a pre-printed list of documents - this is only a guide. Be sure to delete what is not necessary and amend it as appropriate to meet your requirements, as items left on the form may cause problems for your supplier. Banks should in any event discourage excessive detail, in accordance with UCP 500.
- Avoid asking for the same information twice. For example, packing list details are often included in the commercial invoice and weight certificates can be included as stamps on transport documents. The credit must nevertheless be specific as to what is required (see item 11 under “Completing the Application Form”).
- Call for a certificate of insurance not a policy, where the supplier is effecting insurance on your behalf i.e. on CIF or CIP terms. State which risks are to be covered. If “all risks” is stipulated, banks will accept any “all risks” notation or clause on the document and in the UK, the London Institute Clauses “A” will be applied unless requested otherwise. If you wish for more specific cover, give details (see item 10 under “Completing the Application Form”).
- Avoid stating “photocopies are not acceptable”. UCP 500 provides for documents produced by copier or computer methods, and banks will accept them if marked as originals and, where necessary, authenticated. This should be an adequate safeguard.
- Transport Document. The following points on transport documents should be checked carefully and, if necessary, discussed with your bank. They refer to transport documentation practices as recognised in the UCP 500 (Section D. Documents), which may indicate loading on board, despatch or taking in charge.

**Call for the type of transport document you need.** This may not be a “traditional” ocean or marine bill of lading, especially with through container transport. UCP 500 provides the flexibility which you, the carrier and your supplier need. It clearly defines what banks will accept as meeting the requirements of the transport document you call for (see item 8 under “Completing the Application Form”).

- Determine if a freight forwarder’s or a ‘house’ transport document is to be used for the particular method of transport selected - state that this is acceptable.
- Do not state “Short form transport documents are not acceptable”, if your import regulations permit them.
- If you require an “on board” notation to be properly authenticated, stipulate this in the credit.
- Permit “on deck” shipment for dangerous, heavy or awkward sized goods.
- State that “claused” transport documents are acceptable if they are usual in your trade, and say what type of clauses are acceptable.

#### **Especially with through container transport:**

- Specify the place of despatch and the place of delivery, without specifying ports of loading or discharge.
- Do not prohibit transshipment when the goods are being shipped in container or by air.

#### **Other points:**

- State how the letter of credit has to be sent to your supplier’s country: by airmail or, if urgent, by courier service (fast but usually more expensive), or by electronic transmission. If sent electronically, state who pays any extra cost and whether the transmission itself is to be the effective letter of credit (see item 1 under “Completing the Application Form”).
- To help control interest cost within your facilities with your bank, ask them to instruct the overseas bank to confirm on the day they pay your supplier. In the knowledge that the overseas bank has checked and found documents to be in order, you can then decide whether to pay your bank before it receives them.
- Request all documents to be sent from the bank overseas by fastest means, preferably registered express mail or courier service. Even if this costs more, it can be much less than demurrage and other costs caused by delayed documents.
- Ask your bank to telephone you on the day they receive the documents. Give your bank the name of the right person to contact, and if possible arrange to collect the documents rather than having them posted to you.
- If there is still doubt about any terms or documents, contact your supplier and refer to your bank for advice before you ask them to open the letter of credit.
- If the checks and suggestions on this Checklist mean that you decide to change some of the practices you have operated with your bank previously, discuss them with the bank first.
- As soon as you receive your copy of the letter of credit from your bank, check it carefully and in particular watch for any additions or omissions to your original instructions, which may not be workable for your supplier. If anything is in doubt, contact your bank immediately.
- If it is correct, send a clear photocopy of it and of any covering instructions from your bank, direct to your supplier. That may give him advance information possibly several days before getting the formal letter of credit through the banking system. It may also enable him to identify points with which he cannot comply and to advise you immediately thus avoiding problems later.

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## Completing the Application Form

(A specimen of the Application Form is included at the end of this document and may assist in completing your own bank's form).

### (1) Method of Issue

- To avoid any possibility of delay it is advisable to request issue by electronic transmission. An electronic pre-advise with the effective credit following by air mail is sufficient, where the supplier (beneficiary) merely requires advance notification of a credit to come and there is no immediate urgency to ship goods and present documents. (Note that under UCP 500 Article 11(c) the pre-advise must be followed up by an issue of the credit - unless the pre-advise says otherwise).

### (2) Applicant

- This is you, the customer at whose request ABC Bank is to issue the credit. Your correct company title and full address should be entered here. It is important that this be complete and accurate in every detail.

### (3) Beneficiary

- The supplier, or exporter in whose favour the credit is to be issued. Full and exact details should be entered here, in the same way as for the applicant.

### (4) Currency and Amount

- The amount should be expressed in figures and words ensuring that both are expressed in the correct and the same currency. In the event of a variation in amount being permitted, this should be expressed in the appropriate terms e.g. "£10,000 - 3% more or less".
- Care should be taken with both your and your supplier's exact requirements. Variation can be ambiguous e.g. there may be a tolerance in the unit price, quantity of goods and credit amount by the use of 'about' and similar wording - eg '10% more or 10% less'.

**NB:** UCP 500 Article 39(c) - which allows a tolerance of 5% less in the amount of the drawing, even if the credit prohibits partial shipments, provided that any stated quantity of goods is shipped in full and that any

stated unit price is not reduced. This provision for short-drawing may result from over-estimating freight charges at the time of concluding the sales contract months before actual despatch.

### (5) Expiry

- The expiry date must allow time for the beneficiary to receive the credit, produce or manufacture goods, complete arrangements for packaging and transport etc. and to assemble documents prior to presentation under the credit. Issuing bank charges are normally levied on a 3 monthly basis so that an expiry date of 3 months from issue or a multiple thereof would seem appropriate in most cases. If the validity proves too short this can cause problems with amendments and lead to delay in despatch.
- The place of expiry should be the country of the beneficiary. If it is not, he will have to rely on your bank to effect settlement upon receipt of documents. This is unsatisfactory and also defeats the object of establishing a letter of credit, while making it very difficult for your supplier to correct any errors in the documents.

### (6) Availability

- The availability of the credit will depend upon the terms agreed - normally by means of sight payment with documents accompanied by sight draft
- Alternatively, settlement may be by means of acceptance, when drafts will be drawn at a term (or usance) e.g. or 60 days from the date of the transport document.
- In the event of a deferred payment being arranged no draft will be called for, and settlement will be stipulated at a specified or determinable future date.
- As the issuing bank will have correspondent banking relationships in the beneficiary's country, the choice of correspondent should be left to them. If the beneficiary insists on a bank other than the issuing bank's choice as advising bank, this can lead to delay and additional costs.

### (7) Documents and Presentation Period

- Unless specific documents are required by government regulations, only documents essential to the banking transaction should be stipulated. All other documents can be

sent direct to you and, if necessary, a statement to this effect shown as required under the credit. Essential documents are those listed in items (8), (9) and possibly (10) below.

- UCP 500 stipulates 21 days as the normal cut-off period for presentation of documents after the date of issue of the transport document, but it concerns only how quickly the documents can be obtained and presented by the supplier. The period may be curtailed or extended depending on circumstances. Whatever period is selected does not alter the requirement for documents to be presented within the validity of the credit.

#### **(8) Transport Documents (Carefully note UCP 500 Articles 23-30)**

- Transport may be by sea, air, road or perhaps inland waterway or a combination of these, or by post or courier. It is unlikely that the average importer will have a knowledge of all the different types of transport involved. Specialist advice should be sought from a local freight forwarder, carrier or his agent.
- However, thought should be given to the advantages of stipulating a non-negotiable sea waybill instead of the traditional marine bill of lading. In such circumstances, the appropriate wording would be: "A full set of 1/1 on board non-negotiable sea waybills stipulating goods to be released at destination to the importer (consignee) and claused to the effect that the shipper had surrendered the right to change the name of the delivery party during the course of transit".
- Normal practice for defining marine bills of lading would be: "A full set of on board marine bills of lading issued to order and blank endorsed marked 'freight paid' (if CFR or CIF) or 'freight payable at destination (if FOB) and notify (name and full address of consignee)".
- For despatches by air the wording would be "Air Waybill (original No.3 for shipper) evidencing goods consigned to (name and full address of consignee)" marked "freight paid" or "freight payable at destination" indicating flight number and date of despatch". In some cases house airwaybills

(HAWBs) may also be used against a letter of credit.

- International road transport is covered by another non-negotiable document (as is the airwaybill) known as the CMR note. A forwarder's certificate or receipt for transport (FCR or FCT) is only acceptable if specifically stipulated in the credit.
- Railway authorities belonging to the rail international convention use the CIM consignment note.
- It is obviously very important that you and your supplier should agree on the exact method of carriage, as it is essential that you give your bank precise details as to what is to appear in the credit.

#### **(9) Commercial Invoice**

- Details should be kept as simple as possible. Where they are required to be signed, certified or legalised precise instructions should be given.

#### **(10) Insurance**

- If insurance is to be covered by the supplier i.e under CIF or CIP, then a Certificate of Insurance should be called for covering the necessary risks e.g. London Institute Cargo Clauses 'A'

#### **(11) Other Documents**

- Documents other than the above should be avoided or arranged to be sent direct outside the credit. However it is often necessary to provide Weight Notes, Packing Lists, Certificates of Origin (issued by either the beneficiary or by a Chamber of Commerce and certified or legalised depending upon country regulations) and Inspection Certificates (usually issued by independent bodies to indicate that the goods shipped are as described and of the right quantity and quality, and possibly price). In the event a condition is stated in the credit e.g. "Goods to be shipped on a vessel not more than 20 years old" without the requirement of a document to substantiate this, banks will ignore it (see UCP 500 article 13c). Great care should be taken therefore to ensure that all required documents are stipulated.

#### **(12) Insurance Effectuated**

- If the supplier is covering the insurance then a Certificate will be presented under item 10 above. If you are covering the insurance

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then this should be indicated here.

**(13) Goods**

- This should be kept as simple as possible to avoid both actual and typographical errors. A simple description may also avoid dishonour under the credit if certain items (unstated in a general description of goods) are not available at the time of shipment and need to be replaced by others.

**(14) Terms**

- The 'traditional' terms for break- bulk i.e. non-containerised cargoes, are FCA, CFR (C&F) and CIF. These days, other terms are more appropriate for multimodal and containerised traffic, such as FCR CPT and CIP, and the advantages of referring to the appropriate term from the ICC Incoterms 2000 should be remembered. There are also special terms covering delivery through to your premises or other preferred location.

**(15) Transport Details**

- Ports and airports of shipment or despatch are best left in general terms such as "any UK port" or "any UK airport". To be specific e.g. "despatch from Norwich" can cause difficulties. If a latest shipment/despatch date is to be quoted, this should precede the expiry date by the number of days allowed for presentation of documents. If no latest shipment/despatch date is indicated it

will be taken to be the same as the expiry date.

**(16) Part Shipment/Transshipment**

- Part shipments should normally be allowed particularly in view of short drawings within the tolerance allowed (see item 4 under "Completing the Application Form".)
- Credits relating to container shipments should not prohibit transshipment and it is not always possible to despatch goods by air without transshipment.

**(17) Special Conditions/Other Instructions**

- Back charges and who is responsible for payment of these should be entered here. Although it will depend contractually on who had agreed to pay charges, it is normal banking practice for the beneficiary to pay all banking charges in his country and for you to pay those in your own.

**NB:** If reference to charges is omitted banks will assume that all bank charges are for your account as the applicant. If confirmation by the advising bank is required, this should also be entered here; again an additional charge will be made and it should be agreed as to who pays this charge. Any other specific instructions such as 'credit to be transferable' should be entered, as appropriate.

A.B.C. Bank plc

Application Form For A Documentary Credit

1. PLEASE ISSUE AN IRREVOCABLE DOCUMENTARY CREDIT

- BY AIRMAIL
- BY AIRMAIL PRE-ADVISE BY TELE-TRANSMISSION
- BY TELE-TRANSMISSION FULL PARTICULARS

3. BENEFICIARY

IN FAVOUR OF (full name and address)

2. APPLICANT (full name and address)

4. CURRENCY AND AMOUNT (in figures and words)

5. EXPIRY DATE

In \_\_\_\_\_ (Country)

6. AVAILABLE BY DRAFT(S) AT  SIGHT  DAYS SIGHT  DAYS FROM DATE OF \_\_\_\_\_ FOR \_\_\_\_% OF INVOICE DRAWN ON YOU/YOUR CORRESPONDENTS OR BY DEFERRED PAYMENT AT \_\_\_\_\_

7. DOCUMENTS REQUIRED WHICH MUST BE PRESENTED NOT LATER THAN \_\_\_\_\_ DAYS AFTER THE DATE OF THE ISSUANCE OF THE TRANSPORT DOCUMENT

8. TRANSPORT DOCUMENT

9. COMMERCIAL INVOICE

10. INSURANCE

11. OTHER DOCUMENTS

12. INSURANCE TO BE EFFECTED BY \_\_\_\_\_ (BUYERS/SELLERS)

13. COVERING (GOODS DESCRIPTION)

14. TERMS OF SHIPMENT (CIF, FOB, ETC.)

15. SHIPMENT/DISPATCH/TAKING IN CHARGE AT/FROM \_\_\_\_\_ TO \_\_\_\_\_ NOT LATER THAN \_\_\_\_\_

16. PART SHIPMENTS ALLOWED/NOT ALLOWED    TRANSHIPMENT ALLOWED/NOT ALLOWED

17. SPECIAL CONDITIONS/OTHER INSTRUCTIONS

EXCEPT AS OTHERWISE EXPRESSLY STATED THIS DOCUMENTARY CREDIT IS SUBJECT TO UNIFORM CUSTOMS AND PRACTICE FOR DOCUMENTARY CREDITS PROVISIONS OF THE INTERNATIONAL CHAMBER OF COMMERCE PUBLICATION NO. 500.