Letters of Credit

Security of payment and protection against non-performance

A letter of credit is a promise by a bank on behalf of the buyer (customer/importer) to pay the seller (beneficiary/exporter) a specified sum in the agreed currency, provided that the seller submits the required documents by a predetermined deadline.

- Advantage for the seller: The security that the supply of goods will be paid.
- Advantage for the buyer: The security that payment will be effected only against delivery of the agreed documents.

Procedure for a Letter of Credit

Opening

Upon opening a letter of credit the bank undertakes an obligation on behalf of the buyer to pay the seller. To this end the buyer must have sufficient assets/credit with the issuing bank.

Credit Suisse provides a special order form to facilitate the formulation of the order for the letter of credit.

Notification/confirmation

Upon receipt of the notification the bank sends the letter of credit to the seller without incurring any liability for its part. However, the bank must take reasonable care to check that the credit appears authentic.

When confirmation is requested the bank sends the letter of credit to the seller with its own promise to pay.
Amendment
If the wording of the letter of credit does not reflect the requirements of both parties, the letter of credit can be adjusted by means of an amendment.

Using and Honoring Letters of Credit
Before they can be submitted, all required documents must be available and must comply with the UCP (Uniform Customs and Practice for Documentary Credits) and documentary credit terms and conditions, and be consistent amongst each other.

Credit Suisse provides a special remittance form (DE) for the seller’s convenience to facilitate the submission of the documents.

If the document submission is compliant with the letter of credit, it is honored in accordance with the conditions set out in the letter of credit.

Types of Letters of Credit

Sight
Under a sight letter of credit, payment is made to the seller immediately after the required documents have been submitted to the authorized bank, provided the conditions in the letter of credit have been met. Banks are, however, allowed a reasonable period of time for checking purposes (not more than five working days after they receive the documents).

Deferred Payment
In the case of a letter of credit with deferred payment, the payment to the seller is not made when the documents are submitted, but instead at a later time defined in the letter of credit.

In the Far East, this kind of documentary credit is also known as a “usance L/C.”

Acceptance
In the case of an acceptance credit, the payment to the seller is not made when the documents are submitted, but instead at a later time defined in the letter of credit.

The seller can request a discount from the bank that accepted the bill of exchange, or from another bank, and thus draw the amount of the bill minus the discount at any time after the documents have been submitted.

Negotiable Credit
Under UCP 600 (Uniform Customs and Practice for Documentary Credits, 2007 revision, article 2) negotiation means the purchase by the nominated bank of drafts (drawn on a bank other than the nominated bank) and/or documents under a complying presentation, by advancing or agreeing to advance funds to the beneficiary on or before the banking day on which reimbursement is due to the nominated bank.

Unfortunately, the term “negotiable credit” is understood and applied in different ways in different parts of the world.

Particular Types

Transferable L/C
Transferable letters of credit are particularly well adapted to the requirements of international trade. They allow an intermediary to transfer a letter of credit to a supplier, thus enabling the intermediary to reduce the extent to which it uses its own funds to process business transactions.

Standby L/C
Standby letters of credit are similar to guarantees. Due to their documentary nature, they fall under the UCP (Uniform Customs and Practice for Documentary Credits). Standby letters of credit can also be issued under ISP98 (International Standby Practices).

If the guaranteed service/payment is not provided, the seller can invoke the bank’s obligation to pay by submitting, together with any other documents that the letter of credit might require, a declaration stating that the letter of credit customer has failed to meet his obligations/payment.

Revolving L/C
If the buyer requests partial deliveries of the ordered goods at specific intervals (contract for delivery by installments), payment can be made under the terms of a revolving letter of credit that covers the value of each consecutive installment. The bank is normally liable for the total value of all agreed partial deliveries.

However, the second partial payment is not effective until the first installment has been paid, and so forth.
Red Clause L/C
In the case of a red clause credit (letter of credit with advance payment), the seller can request an advance for an agreed amount (defined in the terms and conditions of the letter of credit) from the correspondent bank. This advance is basically intended to finance the manufacture or purchase of the goods to be delivered under the letter of credit. The advance is normally paid against receipt and a written undertaking from the seller to subsequently deliver the transportation documents before the credit expires.

Green Clause L/C
Unlike the red clause letter of credit, in the case of a green clause letter of credit, the advance is normally paid not only against receipt and a written undertaking from the seller to subsequently deliver the transportation documents before the credit expires, but also against receipt of an additional document providing proof that the goods to be shipped have been warehoused.

Forms of Letters of Credit
Unconfirmed
In the case of an unconfirmed letter of credit, the correspondent bank merely notifies the seller that a letter of credit has been opened. In this case, it makes no promise to pay and is therefore not required to honor documents presented by the seller. As a result, the seller may rely exclusively on the issuing bank (letter of credit bank) and therefore bears the collection risk of the issuing bank and the country risk – according to their domicile – as well as the transfer risk.

Confirmed
If the correspondent bank confirms the letter credit (on behalf of the issuing bank), then it is committing itself towards the seller to honor documents that are in compliance with the documentary credit terms and presented on time. In this case, the seller receives not only an obligation by the issuing bank but also a legally equivalent and independent promise of payment on the part of the correspondent bank. The seller then bears the collection risk of the confirming bank and, if this bank is not domiciled in his country, the corresponding country risk – according to its domicile – as well as the transfer risk.

Revocable
All letters of credit subject to the current "Uniform Customs and Practice for Documentary Credits" (UCP 600), which is effectively the norm nowadays, are regarded as irrevocable. It is possible in theory to open a revocable letter of credit, but this is no longer done in practice for various reasons (difficult wording/insufficient security [revocation]).

Irrevocable
An irrevocable letter of credit is a firm commitment by the issuing bank to make payment if the documentary credit conditions are fulfilled. It may not be amended or canceled without the consent of the seller and all obligated banks.

If the seller wishes to amend or cancel individual conditions of the letter of credit, then he must ask the buyer to issue an instruction to the issuing bank in this respect.

Transport Documents and Other Documents
Bill of Lading (B/L)
The bill of lading is a transportation document issued by the carrier, or by the carrier’s authorized agent, for the consignment to be shipped. This document states the main shipping terms for the consignment.

There Are Three Different Kinds of Bills of Lading
- The on-board bill of lading is issued after the consignment has been loaded onto the ship. It states the loading date and the name of the ship.
- The received-for-shipment bill of lading merely confirms that the carrier has received the goods designated for shipping.
- The through bill of lading covers the entire journey of the goods, whether they are transshipped or carried by different means of transport.

A Bill of Lading Is a Security
Only the holder of the bill of lading can take possession of the goods. The bill of lading can be issued (addressed) as follows:
- To the order of a natural or legal person (order bill of lading): Entitlement to the goods can be transferred by endorsement.
- A “straight consignment” to a natural or legal person ("straight bill of lading"): Transfer can be effected only by assignment.
- An “order” (bearer bill of lading): Whoever has possession of the original bill of lading is entitled to the goods. The bill of lading is transferred on the release of the document.

Commercial Invoices
The commercial invoice is the accounting document which shows the financial claim of the seller against the buyer. A customs invoice is often required in addition to a commercial invoice to document the value of the goods for import clearance.
Packings, weight lists, and official accompanying documents or permits required by certain countries for export and/or import (such as EUR, ATR, “Clean Report of Findings”) are not covered in the UCP (Uniform Customs and Practice for Documentary Credits); they must be issued under the conditions stipulated by the letter of credit.

Certificates
Certificates of quality, analysis and inspection, etc., are not covered in detail in the UCP (Uniform Customs and Practice for Documentary Credits); they must be issued under the conditions stipulated by the letter of credit. Certificates must be signed by the issuer.

Certificate of Origin
A certificate of origin is a document that confirms the origin of the goods. It may be issued by an official organization, such as a chamber of commerce, or by the beneficiary or the manufacturer (but always as per the terms and conditions of the L/C).

Insurance Documents
If the agreed delivery terms are CIF or CIP, it is up to the seller to arrange insurance. The insurance document (policy or certificate) is the proof that he has done so. According to UCP (Uniform Customs and Practice for Documentary Credits), the insurance document must cover a minimum of 110% of the CIF value of the goods and the risks defined in the letter of credit, unless stated otherwise.

Forwarder’s Certificate of Receipt
A document issued by a forwarding agency confirming receipt of the goods for shipment/dispatch and dispatch instructions. The forwarder’s certificate of receipt (FCR) does not fall under the UCP (Uniform Customs and Practice for Documentary Credits) and is not recognized as a valid transportation document.

Sea Waybill
A non-negotiable sea waybill certifies that goods have been loaded on board a ship, but the document itself does not have the properties of a security. It is not necessary to present this document in order to take possession of the goods.

Courier Delivery Slip
This certifies that goods have been accepted and forwarded by a courier service.

Air Waybill
An air waybill confirms the conclusion of a contract between carrier and consignor, and sets out the conditions with respect to handling, flight route and delivery of the goods.

Road Waybill
This certifies that a contract has been signed between the consignor and the carrier concerning the transportation of goods by road (by truck).

Inland Waterways B/L
This certifies that a contract has been signed between the consignor and the carrier concerning the transportation of goods by inland waterways.

Postal Delivery Slip
This certifies that goods have been accepted and forwarded by a postal service.

Special Constructions for Letters of Credit
An intermediary may wish to transfer his claim based on a letter of credit to a supplier, even if the terms of the letter of credit do not allow a transfer, or if a transfer would contravene article 38 of the UCP (Uniform Customs and Practice for Documentary Credits).

He then has two available options, neither of which necessarily provides the same security as the transferred credit, and which banks will only carry out under certain circumstances.

Back-to-Back Credit
The intermediary’s bank issues a back-to-back letter of credit in favor of the supplier, based only on the security of an existing letter of credit in its own favor.

The UCP (Uniform Customs and Practice for Documentary Credits) contain no specific rules on back-to-back credits. This type of documentary credit consists of two independent letters of credit, which constitute a unit only in a commercial, but not a legal sense.

Assignment of Proceeds from Letters of Credit (Cession)
The beneficiary of the letter of credit can assign (cede) the credit proceeds entirely or in part to a third party. The beneficiary of the assignment then receives a declaration from the bank by order of the letter of credit beneficiary, authorizing the payment of a specified sum from an amount made available under the terms of the letter of credit, provided that the docu-
ments complying with the letter of credit have been submitted. Unlike a transferable letter of credit, the responsibility for submitting the documents rests solely on the beneficiary of the letter of credit.

**Commissions and Charges for Letters of Credit**

Commissions are charged for services rendered in order to offset credit and settlement risks, and to cover the cost of providing collateral.

Unless stipulated otherwise in the letter of credit, these commissions are charged to the seller. If the letter of credit stipulates that the charges are to be borne by a party other than the buyer and if these charges cannot be collected, the buyer is ultimately held liable for their payment (Article 37 of UCP – Uniform Customs and Practice for Documentary Credits).

Exception: Under a negotiable credit the negotiation commission (interest) is charged to the seller unless the letter of credit explicitly states otherwise.

### Standard conditions for letters of credit

#### Export
- **Notification**
  - 0.10%, min. CHF 200, max. CHF 1,500
- **Confirmation commission including period for deferred payment or acceptance**
  - In addition to the notification commission, depending on the actual risk profile of the issuing bank in the respective country min. CHF 300 per transaction
- **Prepayment of a deferred payment under-taking (in addition to the interest) if applicable**
  - CHF 200
- **Assignment of proceeds**
  - 0.10%, min. CHF 200, max. CHF 1,500
- **Pre-advice**
  - CHF 100

#### Import
- **Liability commission including period for deferred payment**
  - Min. 0.20% per quarter
  - Min. CHF 250 per quarter or fraction thereof, min. CHF 500 per transaction
- **Release of goods**
  - CHF 100

#### Additional commissions and charges
- **Utilization (Examination of documents) incl. payment**
  - 0.20%
  - Min. CHF 300 per set of document(s)
- **Deferred payment/acceptance Monitoring of due date(s)**
  - CHF 200
- **Amendment**
  - CHF 200
- **Discrepancies in the documents**
  - CHF 100
- **Cancellation or Expiry without utilization**
  - CHF 100
- **Query/Tracer**
  - CHF 50
- **Postage and telecommunication**
  - Actual costs, min. CHF 25
- **Special handling e.g. Structuring and Advisory – time and effort**
  - CHF 200 per hour, min. CHF 100

All commissions and charges are due on performance of the service.

Prices in effect from January 1, 2013
Prices and services are both subject to change.
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