UCP 600 rules – changing letter of credit business for international traders?

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Abstract: A letter of credit (L/C), in international trade may be described as an instrument of finance carrying a conditional guarantee of payment from the overseas (buyer's) bank to the seller. Consequently, a L/C is desirable in high value and/or high risk transactions. The guarantee is conditional upon the seller complying 100% with the documentary requirements of the L/C, an issue of particular concern to exporters, as the International Chamber of Commerce (ICC) estimates worldwide documentary discrepancy rates of 70%. L/C transactions are governed by ICC rules, and whilst these provide an international standardised process, the differing interpretations of what constitutes documentary compliance create difficulties for sellers in particular. The new rules: UCP 600, supposedly have simpler and clearer wording, to reduce ambiguity and differences in interpretation, and hopefully reduce documentary discrepancy rates and the associated financial risks. This article examines the major changes introduced by the UCP 600 and comments on their likely impact on future L/C business. Whilst acknowledging some improvements were introduced in the UCP 600, the article concludes that a number of issues have been ignored to the detriment of traders.

Keywords: export finance; international banking regulations; international trade finance; letters of credit; UCP 600.

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1 Introduction

It is commonly accepted that there are four traditional methods of payments used in international trade. These are:

- Prepayment or Clean Payment in Advance. Under this payment arrangement, the buyer[1] pays the seller prior to the dispatch of the goods. The expression Clean Payment indicates that banks are not involved in the method of payment, other than in the transfer of funds under instructions (if applicable). Although this method of payment carries virtually no risk to the seller, it is typically limited to low value transactions, or new relationships with no prior trading history, as "in most cases the buyer is not likely to favour this method" (Australian Institute of Export, 2005, p.265).
- Open Account, or Clean Payment. This is the opposite of Prepayment. Under this payment arrangement, the exporter dispatches the goods against the buyer's promise to pay at a future predetermined date, although the exporter enjoys no payment guarantee. This is another clean payment method, used in mature relationships with a relatively long trading history and "where the trading partners have the utmost confidence in each other" (Jimenez, 1997, p.129).
- Bill of Exchange – B/E or Draft. Under this payment arrangement, the exporter dispatches the goods to the buyer and subsequently seeks payment through the buyer's bank, via the B/E, although this bank does not provide any payment guarantee. It is important to note that the B/E "does not guarantee payment and the seller has lost control of the goods to some extent as they are out of his country" (Branch, 2000, p.244). Under this payment arrangement the bank, under instructions, releases the documents required for the import of the goods to the buyer either against the promise of payment in the future, or against the immediate outright purchase of these documents. The operations of B/E are subject to a specific set of rules issued by the International Chamber of Commerce (ICC) – the Uniform Rules for Collections, ICC Publication 522, commonly referred to as the URC 522. This method of payment is used in situations where the level of trust has developed beyond the prepayment and letter of credit (L/C) options, but not quite yet to warrant the open account option.
- L/C or Documentary Credit. Although globalisation has influenced patterns of world trade, L/C continue to be "the most widely used mechanism for effecting payments required under international trade transactions" (Burnett, 2004, p.170). L/C are estimated to account for "more than USD 1 trillion of trade annually" (Klein, 2006, p.1), and their importance has been recognised by some English judges that referred to L/C as 'the lifeblood of international commerce' (D'Arcy, Murray and Cleave, 2000, p.166). Under L/C payment arrangement, the exporter is provided with a conditional guarantee of payment from the buyer's bank, prior to the shipment of the goods. By using a L/C the seller relies on the buyer's bank "to provide sound financial backing to the buyer's undertaking to pay" (Edwards and Weston, 1986, p.41), and this is affected by that bank issuing the L/C. Under such conditions, therefore, the seller effectively substitutes the credit risk of the buyer with that of his bank (Nelson, 1999). Consequently, exporters may use the L/C as a risk management

tool, particularly in situations where the country/customer risk may be unacceptable for bill of exchange or open account terms; or where a high transaction value is involved; or where there is little trading history between the parties, and therefore the level of trust has not yet developed. The L/C is the most complex of the four payment terms, but arguably the safest for both sellers and buyers. L/C operations worldwide adhere to a specific set of rules issued by the ICC – the Uniform Customs and Practice for Documentary Credits, commonly abbreviated to UCP. The ICC updates these rules in response to changes in international banking and business practices.

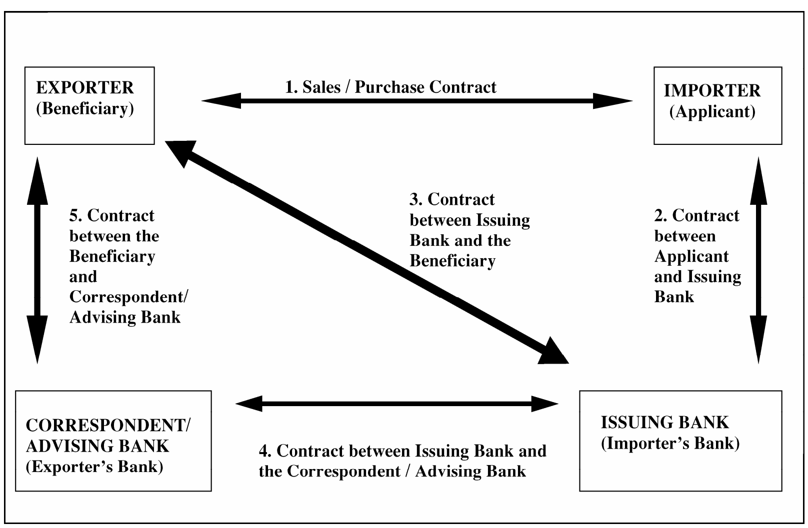
This article concentrates only on L/C transactions in the context of the UCP 600, the latest revision to the rules, effective from 1 July 2007. First, the article provides an explanation of the contracts that are derived from using a L/C, then an explanation of the operational mechanism of the L/C. These are followed by a commentary on the UCP 600 (and related rules), and the major changes and challenges of this revision for exporters, importers and the banks alike, before reaching the conclusion.

2 Contracts arising from the use of a letter of credit

The decision to use a L/C as the payment method in a commercial transaction gives rise to a number of separate contracts, as shown in Figure 1 and explained below.

Contract number 1 creates the business relationship between the seller and the buyer, and specifies the payment subject to a L/C. Because the L/C is an instrument of payment issued by the buyer's bank – the issuing bank, the buyer – applicant – will need to request his bank to set up this payment arrangement in favour of the seller – beneficiary, and this gives rise to the next contract.

Figure 1 Typical contracts arising from a letter of credit transaction



Source: Bergami (2006, p.415).

Contract number 2 creates a business relationship between the applicant (buyer) and the issuing bank (buyer's bank). The applicant is seeking his bank (issuing bank) to establish a conditional guarantee of payment in favour of the beneficiary (seller), via the L/C instrument. Under these conditions, the bank is underwriting the credit risk of the applicant by providing an undertaking to pay the beneficiary, subject to certain conditions specified in the L/C – these are discussed at contract number 3. As the issuing bank is assuming the credit risk of the applicant, a commercial risk assessment on the applicant will be performed and if the bank agrees, the application will be accepted and the L/C issued. It should be noted that it is common practice for banks to avail themselves of security from the applicant prior to issuing the L/C. Depending on the results of the commercial risk assessment, the applicant may need to provide 100% security to the issuing bank, or a lesser amount, as the case may be. The form by which the security is provided is a matter decided between the bank and the applicant, and is not limited to cash amounts only.

Contract number 3 gives rise to the payment undertaking contract between the issuing bank and the beneficiary; however, this is a conditional undertaking. The issuing bank "guarantees payment to the exporter if all documents are presented in exact conformity with the terms of the L/C" (Nelson, 2000, p.91). As banks are neither a party to the contract nor do they deal in the trading of goods, the requirements of the L/C are documentary. That is, the issuing bank will pay the beneficiary as long as the specified documents, with particular data contents, are provided by the beneficiary within the stipulated time frames of the L/C. As L/C are typically channelled through the banking system, and not sent direct from the issuing bank to the beneficiary – a practice developed to reduce possible fraudulent activities – the issuing bank enters into another contract.

Contract number 4 establishes a service and agency contract between the issuing bank and its correspondent bank in the exporter's country, the advising bank – usually the exporter's bank. The role of the advising bank is to act, as instructed, on behalf of the issuing bank. The actions taken by the advising bank are, at minimum, to advise the L/C to the beneficiary; and to accept and check the documents tendered to it by the beneficiary; and advise the issuing bank as to their compliance or otherwise. However, the role of the advising bank may also include, by agreement, a number of additional roles, such as: paying bank – paying the beneficiary and claiming reimbursement from the issuing bank; or confirming bank – underwriting the issuing bank's payment guarantee by substituting it with its own guarantee of payment. Because the advising bank performs functions designed to link it with the beneficiary, the last contract is formed.

Contract number 5 establishes a relationship between the advising bank and the beneficiary. The advice of a L/C only happens when the advising bank is satisfied as to the genuineness of the L/C. A number of security and verification checks are conducted by the advising bank prior to the release of the L/C to the beneficiary. This is simply a matter of practice developed to counteract fraudulent activities. There is nothing preventing an issuing bank and a beneficiary from dealing directly with each other, thereby by-passing the involvement of an advising bank. The problem with this approach, however, is that the beneficiary cannot check the validity of the L/C, simply because the beneficiary does not have access to the banks' security systems. Therefore, a beneficiary acting in good faith against a L/C received directly from a bank in a foreign country may unwittingly become the victim of fraud. Thus, from a risk management perspective, a L/C received directly should be treated with caution and suspicion, at least until due diligence checks have been conducted and the genuineness of the L/C verified.

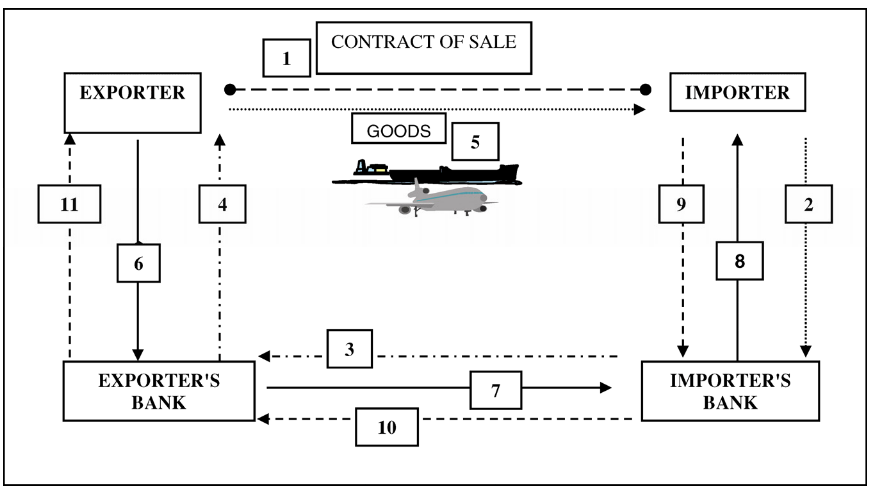
The contracts discussed above provide a contextual background for an explanation of the operational mechanics of the L/C cycle, and this is discussed in Section 3.

3 The mechanics of letter of credit operations

A L/C is subject to a set of rules, devised by the ICC. These rules were firstly codified in 1929 and revised in response to changing business and banking practices in 1933, 1951, 1962, 1974, 1983 and 1993 – UCP500, and 2007, with the UCP 600, effective 1 July.

The operations of L/C transactions are complex by their very nature. Partly, this is due to the fact that at least four parties are involved in the L/C cycle, and partly also because of the requirements of the UCP rules that govern these transactions. Figure 2, discussed below, shows the typical cycle for a L/C transaction that is drawn with a deferred payment option, that is, where the seller is allowing payment at a future predetermined date.

Figure 2 Typical letter of credit transaction with a deferred payment option (see online version for colours)



Source: Bergami (2006, p.442).

(1) Contract of sale between the parties – L/C is the method of payment chosen; (2) importer lodges L/C application with issuing bank; (3) issuing bank issues L/C to advising bank; (4) L/C advised to exporter; (5) goods despatched; (6) required documents lodged by exporter to the bank; (7) documents sent to issuing bank for acceptance; (8) documents released to importer; (9) funds transferred from importer on due date; (10) funds transferred from issuing bank; (11) funds transferred to exporter; L/C Application (2) ··········►; L/C Transfer —·—·—► (3, 4); Documents ————► (6, 7, 8); Funds - - - - - -► (9, 10, 11).

It can be observed that Steps 1, 2, 3 and 4 in Figure 2 reflect the contracts 1, 2, 3 and 4 shown in Figure 1 and discussed above. Before Step 5 is activated, the beneficiary checks the most important requirements of the L/C for consistency with the original intentions of the sales contract. This is an important issue, as banks only check for documentary compliance to the L/C, and because they are not a party to the contract of sale they are not bound by it. Indeed, the UCP rely on the 'independence principle' to separate the contract of sale from banking operations – this is discussed in Section 4. Issues important for the beneficiary to check include the:

- Description and quantity of goods to be supplied.
- Currency and price.
- Delivery terms – Incoterms.
- Payment period.
- Latest shipment and documentary presentation dates.
- Types of documents required – internal: beneficiary issued, such as invoices and packing lists; or external: third party issued, such as transport documents and certificates of origin.
- Data content requirements on documents to be presented for payment.

Should the exporter find any discrepancies between the original agreement and the L/C, an amendment prior to the dispatch of the goods may be required. Should this be the case, usually the beneficiary will request one from the applicant. The amendment follows the same route of the original L/C, that is, from Steps 2–5 of Figure 2. If the L/C is consistent with the contract, the beneficiary proceeds to supply the product/s, as shown in Step 5.

Steps 5 and 6 are probably the most crucial for the beneficiary. The dispatch of the goods is linked to the instruction given to the carrier in caring for the goods en route, but importantly in the context of documentation, these instructions also determine the type of document issued by the carrier and the data content such documents contain. Data not conforming to the L/C requirements may result in a payment delay or, in a worse case situation, non-payment. This is a matter of real concern, as it appears that beneficiaries lodge discrepant documents at an estimated rate of up to 70% on first presentation (ICC Thailand, 2002), thus, losing the very credit risk protection they seek through the L/C in the first place. This matter is discussed further in Section 4. Once the cargo has been sent, as shown is Step 5, the beneficiary obtains transport and other third party documents, as applicable. As shown in Step 6, the beneficiary lodges the L/C with all the required documents at the counters of the advising bank. Typically, the L/C will stipulate a presentation period the beneficiary must adhere to. This is the time allowed from the transport document date to the date of documentary presentation at the counters of the advising bank. This is an attempt to avoid documentation delays that may result in cargo being held up at the arrival port, causing storage charges to be borne by the applicant.

The advising bank, on receipt of the documents, checks same for compliance and advises the beneficiary accordingly, as per Step 7. It should be noted that non-compliant documents are not accepted by the bank rather, the bank notifies the beneficiary of errors and it is up to the beneficiary to decide whether to change the documentary data, if possible, or accept to proceed with incorrect documents and run the risk of non-payment. Where possible, such as in the case of errors on internally produced documents – for example invoice or packing slips, the beneficiary can easily provide amended documents; however, in the case of third party documents, this may not always be possible. For example, seeking a post-shipment change to the shipment date on a bill of lading so it complies with the L/C is "tantamount to the perpetration of a fraud in that … such a practice is a deception on the receiver" (Springall, 2007, p.19), consequently, the shipping line ought to refuse such a request, and therefore, a discrepancy of this calibre may not be rectifiable. On completion of the checking procedures, the advising bank sends the document to the issuing bank for acceptance.

At Step 8, the issuing bank checks the documents and releases these to the buyer, unless errors are found, in which case the bank will follow specially prescribed procedures as laid out by the UCP rules. This may necessitate the applicant to provide a waiver to the issuing bank, agreeing to accept discrepant documents before these are released to the applicant.

Steps 9, 10 and 11 show the flow of funds from the applicant to the issuing bank, through the advising bank, to eventual deposit into the beneficiary's account. The transfer of funds is actioned strictly in accordance with the stipulations found on the L/C. Unless documentary discrepancies are found that may cause delays in remittance of funds, the beneficiary is assured of timely payment in a L/C transaction, and this is particularly good for cash flow planning purposes.

Against the background to the contracts and the operations of L/C transactions, it is now possible to discuss, in Section 4, the application of the UCP rules in greater detail in the context of the major changes the revised UCP rules – UCP 600 – introduced.

4 The new letter of credit rules: UCP 600

This section considers only the major changes introduced by the Uniform Customs and Practice for Documentary Credits, 2007 Revision (International Chamber of Commerce 2007a), effective from 1 July 2007, and commonly referred to as simply the UCP 600, as it is beyond the scope of this article to examine word-for-word changes from the previous version of the rules: the UCP 500 (International Chamber of Commerce, 1993). As the UCP 600 makes reference to other sets of rules, these are also commented on, as appropriate, as part of the discussion in this article.

As with any set of rules, the issues surrounding their implementation is the interpretation given to them and this varies between banks and beneficiaries. Whilst a considerable body of knowledge has developed over the use of L/C rules, and this has particularly been the case for the UCP 500, the same cannot be claimed for the current set of rules, UCP 600 as, at the time of writing this article, these are still in a transition phase and little has been written about them to date. The UCP 600 has been in force for less than two years since their official application date of 1 July 2007. As business is conducted on an ongoing basis, and as the UCP 600 does not have retrospective application, the use of UCP 600, in reality, has been less than a year. This is evidenced by the fact that a number of L/C would have been issued prior to 1 July 2007 (under UCP 500), but would have been transacted after 1 July 2007, when the UCP 600 became effective. No doubt, as in the past, the ICC will continue to play an important steering role in clarifying the application of these rules in response to queries. In the meantime, an analysis of the major changes to the UCP 600 should contribute to a greater understanding of their practical implications. The UCP 500 is comprised of 49 articles, whereas the UCP 600 comprises only 39 articles. The UCP 600 has not just simply removed ten articles; rather it has considerably rewritten, combined and added some articles, attempting to simplify the overall meaning of the new rules.

The UCP 600 applies to L/C transactions in accordance with Article 1 (International Chamber of Commerce, 2006, p.17) that makes the UCP 'rules' for the first time in their life. Whilst this article states that the rules are 'binding on all parties' to the L/C transaction, it also states 'unless expressly modified or excluded by the credit'. The general position of the ICC in relation to the modification of the rules has not changed, as under the UCP 500 this was also possible (Wickremeratne, 2007), but arguably the UCP 500 text perhaps carried a less explicit message as their equivalent wording was 'unless otherwise expressly stipulated in the credit' (International Chamber of Commerce, 1993, p.10).

> "Even though, in UCP 500, one could always exclude or modify any provision, this had not been so obvious and openly suggested. Users considered UCP 500 to be tight rules and did not interfere with them, except in the case of a few and well-understood and necessary modifications (as was the case with standbys for example). Any exclusion of modification of the UCP 600 must be well thought through. I have even heard of a case where an issuing bank excluded the whole of article 7!" (Dobas, 2008, p.4).

Article 7 is the UCP 600 article that deals with the issuing bank's undertaking. Excluding or attempting to exclude this article would make a mockery of the whole L/C transaction, because the beneficiary would not therefore be able to rely on the issuing bank to make good the payment against complying documents. It will be interesting to see whether, in the future, the more explicit wording of UCP 600 Article 1 will result in an increased propensity to modify or exclude articles against individual L/C transactions, and if this is the case, then beneficiaries will need to exercise particular care to ensure that the credit risk protection afforded by the L/C has not been diluted or lost altogether as a result of these modifications or exclusions. This may necessitate the beneficiary to acquire a more intimate knowledge of the UCP 600.

New definitions have been inserted via Article 2 of the UCP 600, "which provides the meaning of the main phrases used throughout the rules" (Wynne, 2007, p.45), such as banking day, credit, hour and negotiation. Article 2 also provides the meaning of complying presentation, which is defined as "a presentation that is in accordance with the terms and conditions of the credit, the applicable provisions of these rules and international standard banking practice" (International Chamber of Commerce, 2006, p.17). The reference to international standard banking practice raises a number of issues. By way of background, the UCP 500 Article 13 also made reference to international standard banking practices, however, no codified set of practices existed when the UCP 500 became effective, in 1994. Indeed, the first publication of these practices, referred to as ISBP by the ICC, did not take place until 2003 (International Chamber of Commerce, 2003). This meant that for nearly ten years banks were checking documents against a set of practices that had never been published. To their credit, the ICC did not repeat this mistake with the release of the UCP 600. The updated – not revised – ISBP were made available in June 2007, just in time for the UCP 600 effective date of 1 July 2007 (International Chamber of Commerce, 2007b), but as it turns out, only minimal changes were made to the ISBP to bring them in line with the UCP 600. It is argued here that in relation to the ISBP, there are significant issues of concern: the lack of authority; and the adoption of the ISBP. The ISBP have not been defined as rules, but rather as a set of 'principles' that explain "how the practices articulated in UCP 600 are applied by documentary practitioners" (International Chamber of Commerce, 2007b, p.12). Article 14d of the UCP 600 links the standard for examination of document to international standard banking practice with the words "data in a document, when read in the context with the credit, the document itself and international standard banking practice" (International Chamber of Commerce, 2006, p.27). However, it should be noted that "in this context it does not mean the ICC publication containing the ISBP" (Andrle, 2007, p.18), as apparently "the practices are broader than what is stated in this publication" (International Chamber of Commerce, 2007a, p.16). The concern with this statement is that it would be possible for an alternate set of international standard banking practices to appear and that may produce unexpected results. The lack of authority of the ISBP or a similar set of standards, stems from the fact that these are principles and not rules and in accordance with UCP 600 Article 16cii., the responsibility of a bank in the face of discrepant documents is to notify the presenter with a single notice that "must state … each discrepancy in respect of which the bank refuses to honour or negotiate" (International Chamber of Commerce, 2006, p.29). This requirement means that the bank must rely on the UCP 600 alone to advise on the discrepancies, and therefore, the ISBP carries no authority of its own. As different practices may exist and different codes may arise, the ICC has not been able to mandate the adoption of the ISBP. Testament to this is the recognition by the ICC itself that the ISBP do not cover all international standard banking practices. Although the ICC has attempted to influence banking procedures by referring to international standard banking practices, the fact of the matter is that it will be up to banks to voluntarily adopt such practices, and indeed, voluntarily embrace the ISBP. It is argued here that this situation of uncertainty is not good for the beneficiary, as the interpretation of the UCP rules, as influenced by banking practices, no doubt will impact on the acceptance or otherwise of a set of documents and may result in a differential, rather than standard treatment of documentary acceptance decisions that will vary from bank to bank and country to country. Hopefully this will not happen, but there is no evidence that the UCP 600 can prevent this situation from developing.

To the defence of the UCP 600 though, Article 14d does state, in part, that "data in a document … need not be identical to, but must not conflict with, data in that document, any other stipulated document or the credit" (International Chamber of Commerce, 2006, p.27). This follows the principles of the doctrine of materiality, supporting the acceptance of documents in light of minor and inconsequential differences on the documents. The change in the words from the comparable UCP 500, Article 13 indicates that "a clear attempt has been made to seek to reduce rejection of documents on presentation on the basis that the documents are inconsistent or in some way non-compliant" (Wynne, 2007, p.45). Article 14b reduces the time that a bank has to check the documents for compliance from seven to a maximum of five banking days. This is a positive step for the beneficiary, in particular when dealing with L/C drawn at sight, as it means that payment may be forthcoming up to two days earlier than was previously the case.

Under the UCP 500, L/C could either be irrevocable or revocable. A revocable credit is one that, after it is issued, may be changed without reference to the beneficiary. Under such conditions, it is not difficult to imagine that the beneficiary has a potentially weakened position in documentary compliance, because there is no certainty that the original L/C requirements will remain unchanged until the completion of the transaction. The irrevocable credit, instead, is one that after having been issued requires the agreement of all parties for changes to take effect. The irrevocable L/C, therefore, is preferred by the beneficiary, because there is certainty of requirement until the end of the transaction, or an amendment has been agreed to. The default L/C type under the UCP 500 Article 3 was irrevocable, unless the parties expressly indicated the use of a revocable credit. Revocable credits, not surprisingly, have lost their appeal in modern day L/C transactions and the UCP 600 reflects this through Article 3 that states in part that "a credit is irrevocable even if there is no indication to that effect" (International Chamber of Commerce, 2006, p.19) and "this is a significant change in that the option of revocability … is not required" (Wickremeratne, 2007, p.19). This is a positive change for both the seller and the buyer, as it provides stability in the L/C transaction.

The UCP 600 has not altered the long established 'principle of independence', that is, the separation of the L/C from the underlying contract, insofar as banking operations are concerned, and this is reflected in Article 4. Article 5 also reinforced that separation by specifying that "banks deal with document and not with goods, service or performance to which the document may relate" (International Chamber of Commerce, 2006, p.20).

One area of contention with the UCP 500 was the requirement for data content on commercial invoices, via Article 37c that stated, in part, "the description of the goods on the commercial invoice must correspond with the description in the credit" (International Chamber of Commerce, 1993, p.44). This approach is based on the doctrine of strict compliance that is unforgiving of inconsequential differences and contributes to, rather than reduces discrepancies. This requirement fostered a documentary check environment enabling the practice of 'manufacturing discrepancies' to be developed. The invention of discrepancies was known to occur in situations where the issuing bank, having taken considerably less than 100% security from the L/C applicant, was provided with documents that seemingly complied. Upon enquiry, the issuing bank would find that the applicant had insufficient funds to cover the L/C payment. Unwilling to make the payment as due, the issuing bank would suddenly 'find' mistakes in the documents. This practice was simply designed to 'buy time' while the banks argued amongst themselves as to whether these discrepancies were real, or not, in accordance with the UCP 500. Payment would ultimately ensue, but the beneficiary would incur a time delay with consequential cash flow implications and costs. Unfortunately, the now corresponding Article 18 in the UCP 600 has remained substantially unaltered, thus the practice of manufacturing discrepancies may be allowed to exist in the future.

The responsibility of the advising bank has been clarified by Article 9 of the UCP 600. "By advising the credit … the advising bank signifies that it is has satisfied itself as to the apparent authenticity of the credit … and that the advice accurately reflects the terms and conditions of the credit" (International Chamber of Commerce, 2006, p.23). This is an improvement over the comparable Article 7 of the UCP 500 that merely required the bank to show reasonable care in checking the apparent authenticity of the credit.

Discrepant documents were discussed above, but in the context of the notice to be given to the presenter of the documents. However, Article 16 also addresses the process that may be followed in the presence of discrepant documents and their disposal. Under the UCP 500, in accordance with Article 14, the issuing bank would seek a written waiver from the applicant before accepting discrepant documents. Often this process resulted in the buyer seeking to acquire some gain from the seller, by way of a discount or extended time to pay, in return for accepting the discrepant documents. Where discrepant documents exist now, an additional option for the presenter has been introduced by Article 16iii (a). The presenter of the documents may instruct the issuing bank to hold the documents pending further instructions, and not seek a waiver from the applicant. This may be a good option in a situation where the price of the goods has increased, and the seller may be able to gain an additional price for the goods.

Finally, there is another concern that has not yet been resolved. Article 28h refers to ‘all risk’ insurance, but because of differences in liabilities between countries, it is unclear as to what the article intended. Indeed, the ICC itself is now suggesting that “a documentary credit should not call for an insurance coverage against ‘all risks’ because there are various types of ‘all risks’ coverage in different markets” (International Chamber of Commerce, 2007, p.133).

5 Conclusions

The reforms under the UCP 600 rules for L/C transactions have provided a mixed bag of positive and negative issues. The positive steps taken by the ICC to address some of the problems of the UCP 500 include:

- A new set of definitions of the most commonly used terms, helping to clarify matters.
- A reduction in the maximum time allowed to a bank for acceptance of the documents to a maximum of five banking days.
- The abolition of revocable credits from the application of the rules.
- An attempt to reduce discrepancies by not demanding exact data content, following the principles of the doctrine of materiality – except for the commercial invoices.
- Continuing to uphold the principle of independence.
- Clarifying and strengthening the responsibility of the advising bank in advising the credit to the beneficiary.
- Allowing the presenter of the documents to instruct the issuing bank to hold the documents and not seek a waiver from the applicant.

These issues will no doubt assist sellers and buyers to maintain confidence in the L/C as a method of payment.

The negative issues include:

- Increased prominence on options to exclude articles, and if articles are excluded, beneficiaries will be concerned about weakening of the credit risk protection offered by the L/C.
- The confusion over what constitutes international standard banking practices.
- The lack of authority of the ISBP.
- The possibility of different sets of international standard banking practices evolving.
- The lack of clarity over ‘all risks’ insurance.
- The continuing requirement for commercial invoices to show an exact matching description in accordance with the dogmatic doctrine of strict compliance principles.

The problem for beneficiaries in particular continues to be the challenge of documentary compliance. It is argued here that it is doubtful that without the removal of the doctrine of strict compliance, there will be a great reduction in discrepancy rates. Therefore, it is likely that beneficiaries will continue to run the risk of payment delays and/or defaults. The possible exclusion of articles and the lack of clarity over what constitutes international standard banking practice are other issues that cast doubt over the L/C as an acceptable payment mechanism.

As the implementation of the UCP 600 rolls out into the world of commerce, it will be interesting to discover what will be adopted easily and which of the articles will prove contentious, and require the intervention of the ICC to clarify the issues concerned. It would be useful to undertake more in-depth research in the future, once a sufficient period of time has lapsed and a body of knowledge has developed through the application and use of the UCP 600 to establish, at least, whether the ICC has been successful in reducing documentary discrepancy rates.

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Note

[1]In this article, the words buyer and importer are used synonymously, as are the words seller and exporter. References to him/his are also meant to be interpreted as being gender neutral.