



COMMERZBANK



## Discrepant letter of credit documents finally refused by an issuing bank – is the letter of credit considered as utilised for the amount of the documents?

It can happen quickly: A letter of credit document is not signed as required in the letter of credit, or specifications required in line with letter of credit conditions regarding the delivered goods are missing due to an oversight. Therefore, it is not uncommon for presented letter of credit documents to contain discrepancies. The nominated bank of the letter of credit, to which the beneficiary presents the documents, will inform the beneficiary of the discrepancies it has identified. Usually it is to be assumed that the beneficiary resolves the discrepancies identified, if possible, by correcting or replacing the documents presented.

However, there are also instances where discrepancies in the documents cannot be corrected or where the beneficiary deliberately decides to present discrepant documents to the issuing bank for payment.

### An example:

**A letter of credit issued by Careful Bank in favour of WellDone Ltd. includes the following payment terms:**

- I. 10% down payment
- II. 80% upon shipment
- III. 10% after acceptance of goods.

The documents required are specified separately.

Regarding the final payment of 10%, the letter of credit requires, among other things, presentation of an acceptance protocol signed by the applicant, to be presented 180 days after shipment date at the earliest.

The goods are already accepted after 120 days. WellDone Ltd. is certain that the applicant agrees to premature presentation of the acceptance protocol and thus to premature payment. Therefore, it presents the protocol and all other documents required prior to the expiration of the 180-day period to its bank, the Free and Easy Bank, which has advised the letter of credit. After examination of documents, it is informed by the bank that the documents are discrepant: Presentation is too early, as the conditions of the letter of credit state that the documents for the final payment must be presented 180 days after shipment date at the earliest.

Since WellDone Ltd. assumes that there will be no problems in the further processing of payment, it asks its bank to send the documents to the issuing bank on approval basis.

As the presented documents are discrepant, Careful Bank refuses to honour them in compliance with article 16 of the “Uniform Customs and Practice for Documentary Credits (UCP 600)”.

What happens is rare, but basically possible: Much to the surprise of WellDone Ltd., the refusal of the documents is final, and Careful Bank returns the documents.

What next?

WellDone Ltd. is not concerned about the return of the documents and, after the 180-day period following shipment has elapsed and within the validity of the letter of credit, re-presents the documents, to Free and Easy Bank for payment. Free and Easy Bank claims again that the presented documents are discrepant. It refuses the documents with the remark that the amount of the letter of credit is overdrawn and argues that the drawing of part III is already completed.

WellDone Ltd. is confused and questions whether the arguments of Free and Easy Bank are justified.

The UCP 600 do not explicitly deal with this topic – but why should it? Article 2 of the UCP 600 defines a letter of credit as

any arrangement, however named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honour a complying presentation.

### Do you have any questions or suggestions regarding top@doc?

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As Careful Bank did not honour the discrepant documents, its obligation under the letter of credit has not been reduced either. The refusal and return of the documents by Careful Bank is tantamount to a non-utilisation. The rejection of documents alone does not reduce or cease a letter of credit.

The view of Free and Easy Bank that the amount of the letter of credit is overdrawn with the re-presentation of documents is wrong. The re-presented drawing of part III does not lead to an overdraw of the amount of the letter of credit.

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Please note that fictional names used in this document are for illustrative purposes only.