

INTERNATIONAL TRADE AND FINANCE MASTERCLASS

PART 26 OF 25 · DEEP DIVE SERIES — PARTS 26 TO 30

PART 26

THE LETTER OF CREDIT — THE COMPLETE PRACTITIONER'S GUIDE

A deep-dive companion to Part 5. The Letter of Credit is the most important financial instrument in international trade. This part covers every type, every party, every document requirement, the UCP 600 rules in plain language, the twenty most common discrepancies, and three fully worked case studies that show what happens when it goes right and when it goes wrong.

IN THIS PART

- Why the LC is the cornerstone of international trade finance
- Every type of LC and when each is appropriate
- The UCP 600 — the rules that govern every LC globally
- Strict compliance — what it really means in practice
- The twenty most common discrepancies and how to eliminate them
- Complete document-by-document LC presentation guide

CASE STUDIES

Each part includes fully worked case studies with detailed calculations, real-world context, and practical lessons for CFOs and finance leaders.

■ BUILDING ON PART 5

Why This Deep Dive Exists

In Part 5 of this program, we introduced the Letter of Credit as the most important payment instrument in international trade and covered its basic mechanics, parties, and types. If you have not read Part 5, please do so before continuing here — this deep dive assumes that foundation and builds substantially beyond it. What Part 5 could not do in its available space was take you through the operational reality of working with LCs every day — the document preparation discipline, the specific pitfalls that cause discrepancies, the negotiation tactics for difficult LC terms, and the complete mechanics of every LC type from the simplest sight LC to the most complex transferable back-to-back structure.

The financial stakes justify this depth of treatment. The International Chamber of Commerce estimates that between sixty and seventy percent of all first presentations under Letters of Credit contain at least one discrepancy. Each

discrepancy delays payment — sometimes by days, sometimes by weeks. Each delay has a cost: the interest on the unpaid receivable, the administrative cost of resolving the discrepancy, the relationship damage with the buyer, and in the worst cases, the risk that the buyer uses the discrepancy as leverage to renegotiate the price or reject the goods entirely. A company that presents clean documents every time has a measurable competitive and financial advantage over one that routinely presents discrepant documents.

This deep dive is organized around the practical workflow of an LC transaction — from receiving the LC through preparing documents, presenting them, resolving any issues, and collecting payment. At each stage, we identify the specific actions and disciplines that separate companies that collect promptly from companies that experience repeated delays and disputes.

The LC as a Risk Allocation Mechanism

Before we go into the operational detail, it is worth being precise about what problem the LC actually solves. International trade between strangers faces a fundamental trust problem that domestic commerce does not. When a US retailer buys from a domestic supplier, the two parties share a legal system, a currency, a language, and often a long commercial relationship. When that same retailer buys from a Vietnamese manufacturer, none of those shared foundations exist. The manufacturer will not ship goods worth five hundred thousand dollars to someone they have never met, in a country whose courts they cannot easily access, without some assurance of payment. The retailer will not pay five hundred thousand dollars before seeing the goods and confirming that what was shipped is what was ordered.

The LC solves this problem by substituting the bank's promise for the buyer's promise. The issuing bank — the buyer's bank — makes an irrevocable commitment to pay the seller, not if the buyer is satisfied with the goods, but if the seller presents the specific documents described in the LC within the specified time frame. The bank does not inspect the goods. The bank does not evaluate whether the contract has been performed. The bank deals only in documents. This is both the LC's great strength and the source of the discrepancy problem — because if the bank deals only in documents, then documents that do not precisely match the LC terms give the bank the right to refuse payment, regardless of whether the underlying goods were perfect.

■ THE FUNDAMENTAL LC PRINCIPLE EVERY CFO MUST INTERNALIZE

Banks deal in documents, not in goods, services, or performance of contracts. This is Article 5 of UCP 600 and it is the most important sentence in the entire LC framework. It means that if your documents are perfect but your goods are slightly different from what was contracted, the bank will still pay you — because the bank cannot know about the goods. It also means that if your goods are perfect but your documents have a single error, the bank can refuse payment — because the documents are all the bank can see. This principle is the foundation of everything that follows.

The Parties to an LC Transaction — In Full Depth

Part 5 introduced the parties to an LC. Here we go into the specific legal obligations and practical responsibilities of each party, because understanding who is responsible for what at each stage is essential for managing the transaction effectively.

The Applicant — The Buyer

The applicant is the buyer — the party who instructs their bank to issue the LC. The applicant's responsibilities are more extensive than many buyers realize. The applicant must complete the LC application with sufficient precision that the documents the seller will present can be clearly specified. Vague LC terms are one of the most common causes of discrepancies — if the LC says 'commercial invoice' without specifying the exact description of goods, the number of originals required, or the currency, the seller may present a document that is technically correct but that the bank cannot match against the LC terms. Every ambiguity in the LC application becomes a potential discrepancy in the document presentation.

The applicant also bears the reimbursement obligation to the issuing bank. When the bank pays the beneficiary under a complying presentation, the bank has a right to be reimbursed by the applicant regardless of any dispute between the applicant and the beneficiary about the underlying goods or services. This is another expression of the independence principle — the LC contract between the bank and the beneficiary is entirely separate from the commercial contract between the buyer and seller. A buyer who instructs their bank not to pay because the goods were defective — when the documents comply — is in breach of their obligation to the bank and cannot prevent payment.

The Issuing Bank

The issuing bank is the buyer's bank — the institution that issues the LC and makes the irrevocable payment undertaking. The issuing bank's obligation under UCP 600 is to honor a complying presentation — meaning to pay at sight if it is a sight LC, or to accept and pay at maturity if it is a usance LC. The issuing bank has five banking days after receipt of documents to determine whether they comply. This is not five calendar days — it is five banking days in the country of the issuing bank. If the bank determines that documents do not comply, it must give notice to the presenter stating each discrepancy and indicating whether it is holding the documents pending instructions from the applicant or returning them.

The creditworthiness of the issuing bank is the foundation of the LC's value to the beneficiary. A Letter of Credit issued by a bank with a strong international credit rating — a major US, European, or Japanese bank — is a genuinely secure payment instrument. A Letter of Credit issued by a small regional bank in a country with weak banking supervision may be technically irrevocable but practically uncertain, because if the issuing bank fails or if the government imposes capital controls that prevent the bank from making international payments, the beneficiary may not be paid despite presenting complying documents. This is precisely why the confirmed LC — where a second bank in the beneficiary's country adds its own independent payment undertaking — is so important for transactions involving issuers from financially fragile jurisdictions.

The Advising Bank

The advising bank is a bank in the beneficiary's country that receives the LC from the issuing bank and forwards it to the beneficiary. The advising bank's role is to authenticate the LC — to verify that it appears on its face to be genuine and that the issuing bank's authorized signatures or test keys are correct. The advising bank does not make any payment undertaking when it simply advises an LC. It is merely a conduit. The critical point for beneficiaries is this: receiving an advised but unconfirmed LC means you are relying entirely on the issuing bank's promise. If you want the advising bank's own independent commitment to pay, you must specifically request confirmation, and the advising bank must agree to add its confirmation.

The Confirming Bank

The confirming bank adds its own irrevocable undertaking to honor a complying presentation in addition to the issuing bank's undertaking. When a beneficiary presents complying documents to a confirming bank, the confirming bank is obligated to pay regardless of whether it has been reimbursed by the issuing bank. The confirming bank then seeks reimbursement from the issuing bank — but that is the confirming bank's problem, not the beneficiary's. From the beneficiary's perspective, confirmation converts the payment risk from the credit risk of a foreign bank in a foreign country to the credit risk of their own domestic bank. This transformation of risk profile is exactly what makes confirmation valuable, and why exporters selling to buyers in countries with weak banking systems or geopolitical risk should always insist on it.

◆ CONFIRMATION COST vs. RISK CALCULATION

CONFIRMATION COST vs. RISK — DECISION FRAMEWORK

LC VALUE: \$800,000 | ISSUING BANK: Heritage Bank Nigeria

CONFIRMATION COST:

Confirming bank (Standard Chartered London) fee:

0.75% per quarter = $\$800,000 \times 0.75\% = \$6,000$

(assuming 90-day LC validity)

RISK WITHOUT CONFIRMATION:

Nigerian banking system stress probability: high

Probability of non-payment if issuing bank fails: 85%

Expected loss without confirmation: $\$800,000 \times 85\% = \$680,000$

This is not a theoretical risk — Nigerian bank failures

and CBN interventions have repeatedly frozen LC payments

DECISION: Pay \$6,000 for confirmation

Cost: \$6,000

Risk eliminated: \$680,000 expected loss

ROI of confirmation: 113x

RULE: Always confirm LCs from banks in countries where:

- (a) sovereign credit rating is below BBB-
- (b) active capital controls restrict FX payments
- (c) banking sector has recent history of instability
- (d) country is under broad economic sanctions

Every Type of LC Explained in Full

Sight LC versus Usance LC

A sight LC requires the issuing or confirming bank to pay immediately upon receipt of complying documents — in practice, within the five banking days allowed for examination. The beneficiary presents documents, the bank examines them, and if they comply, payment is made. This is the most straightforward form of LC and provides the fastest payment to the beneficiary.

A usance LC — also called a term LC or deferred payment LC — allows the buyer a period of credit after document presentation before payment is due. A common structure is a ninety-day usance LC, where the bank accepts the draft and commits to pay ninety days after the bill of lading date or after sight. During that ninety-day period, the exporter has effectively extended credit to the buyer, secured by the bank's acceptance. The exporter can hold the acceptance until maturity, or discount it — sell it to a bank at a discount to face value — to receive cash immediately. This discounting converts a ninety-day usance LC into an immediate cash receipt, at a cost equal to the discount rate applied to the ninety-day period.

◆ USANCE LC DISCOUNTING — MECHANICS

USANCE LC DISCOUNTING — COMPLETE CALCULATION

LC amount: USD 600,000 | Usance: 90 days from B/L date

Issuing bank: ICBC Shanghai (strong credit rating)

OPTION A: HOLD UNTIL MATURITY

Receive: USD 600,000 on day 90

Cost of waiting: $\$600,000 \times 6.5\% \times 90/365 = \$9,616$ (opp. cost)

OPTION B: DISCOUNT THE ACCEPTANCE

Discounting rate (ICBC acceptance, 90 days): 5.8% p.a.

Discount amount: $\$600,000 \times 5.8\% \times 90/360 = \$8,700$

Net proceeds today: $\$600,000 - \$8,700 = \$591,300$

COST COMPARISON:

Cost of discounting: \$8,700

Cost of waiting (opportunity cost): \$9,616

DISCOUNTING IS CHEAPER than the opportunity cost of waiting

AND: \$591,300 cash today vs. \$600,000 in 90 days

The exporter can redeploy \$591,300 immediately

NOTE: The quality of the acceptance matters enormously.

An acceptance from a major rated bank discounts at tight spreads. An acceptance from an obscure bank may not be discountable at all in the secondary market.

The Transferable LC — For Trading Companies and Intermediaries

A transferable LC allows the first beneficiary — typically a trading company or intermediary — to transfer all or part of the LC to one or more second beneficiaries, who are usually the actual manufacturers or suppliers. The transferable LC is the financial mechanism that makes the trading company business model viable. Without it, a trading company that sources from manufacturers and sells to buyers would need to use its own working capital or credit facilities to bridge the gap between paying its suppliers and collecting from its customers. With a transferable LC, the buyer's creditworthiness — expressed through the issuing bank's undertaking — flows through to the manufacturer, and the trading company needs to contribute only the difference in price between what it pays its suppliers and what it charges its buyers.

The mechanics of the transfer are specific and must be followed precisely. The transfer must be requested in writing to the transferring bank — the bank designated in the original LC to effect the transfer. The transferred LC may have a lower amount than the original (reflecting the trading company's margin), a shorter expiry date, and a different name as applicant. When the second beneficiary presents documents against the transferred LC, the trading company has the right to substitute its own invoice — at the higher price — for the second beneficiary's invoice. This invoice substitution is the mechanism through which the trading company protects its margin without disclosing its buy price to the ultimate buyer.

The Standby LC — A Guarantee in LC Form

The standby Letter of Credit is fundamentally different in purpose from a commercial LC. While a commercial LC is the primary payment mechanism for a trade transaction — the seller expects to draw on it — a standby LC is a guarantee of last resort. It is intended to remain undrawn. The beneficiary of a standby LC draws on it only if the applicant defaults on an underlying obligation — fails to make a payment, fails to perform a contract, or fails to repay a loan.

Standby LCs are widely used in situations where a guarantee is required but a bank guarantee in the traditional sense is not available or not appropriate. In the United States, for example, banks are restricted from issuing guarantees under the National Bank Act, but they can issue standby LCs that achieve the same economic effect. A US contractor bidding on a government project in Saudi Arabia that requires a performance bond can use a standby LC issued by its US bank in place of a traditional performance guarantee, and the Saudi authority will typically accept it because the standby LC is governed by UCP 600 or ISP98 and is internationally recognized.

The UCP 600 — The Rules That Govern Every LC

The Uniform Customs and Practice for Documentary Credits — currently in its sixth revision as UCP 600, published by the International Chamber of Commerce in 2007 — is the most important set of rules in international trade finance. It has thirty-nine articles covering every aspect of LC operation, from definitions through document examination standards to the handling of discrepancies. Understanding the key articles in practical terms is essential for anyone working with LCs regularly.

The Most Important UCP 600 Articles in Practice

Article 2 — Definitions	Defines the key terms used throughout UCP 600. Particularly important is the definition of 'complying presentation' — 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 standard banking practice' is the phrase that creates the most interpretation disputes, because it invites banks to apply their own understanding of what standard practice requires.
Article 5 — Documents versus Goods	Banks deal with documents and not with goods, services or performance to which the documents may relate. This is the independence principle — the most important single rule in LC law. No matter what disputes arise about the underlying transaction, if documents comply, the bank must pay.
Article 14 — Standard for Examination of Documents	Banks have five banking days to examine documents and determine compliance. Examination is on the face of the documents. Banks do not verify the authenticity of documents or whether the signer had authority. Data in documents need not be identical to the LC but must not conflict with data in the LC, other documents, or UCP 600 itself.
Article 16 — Discrepant Documents	When a bank determines documents are discrepant, it must give a single notice of refusal stating each discrepancy. The notice must state whether the bank holds documents pending instructions, returns them, or has already acted on applicant instructions. Failure to give proper notice within five banking days means the bank loses the right to refuse.
Article 20 — Bills of Lading	Specifies exactly what must appear on a complying Bill of Lading — including the named carrier or agent, on-board notation with vessel name and port, port of loading and discharge, and freight payment terms. A B/L that does not meet these specific requirements is discrepant regardless of how commercially valid it appears.
Article 28 — Insurance Documents	Under CIF terms, insurance documents presented under an LC must be issued by insurance companies or underwriters. Cover notes from brokers are not acceptable. The insurance amount must be at least 110 percent of the CIF value of the goods. The currency of the insurance must be the same as the LC currency.

The Twenty Most Common LC Discrepancies

Based on ICC surveys and the experience of trade finance practitioners globally, the following twenty discrepancies account for the overwhelming majority of all LC presentation failures. For each one, we explain what the discrepancy is, why it occurs, and the specific drafting or preparation discipline that eliminates it. A company that addresses all twenty of these systematically will dramatically reduce its discrepancy rate.

DISCREPANCY 01: Late presentation

What it is: Documents presented after the expiry date of the LC or after the period for presentation following shipment (default: 21 days from B/L date under UCP 600 Article 14c).

How to eliminate it: Build a document preparation timeline working backwards from the LC expiry. Calculate the latest possible shipment date that still allows 21 days for document preparation and presentation. Monitor the timeline daily once shipment is imminent.

DISCREPANCY 02: Late shipment

What it is: Goods shipped after the latest shipment date specified in the LC.

How to eliminate it: Confirm the latest shipment date before accepting the LC. If the manufacturing timeline makes the shipment date unachievable, request an amendment before production begins, not after the date has passed.

DISCREPANCY 03: Description of goods on invoice does not match LC

What it is: The commercial invoice describes the goods differently from the description in the LC. Even minor differences — 'pump stations' versus 'pumping stations,' 'cotton shirts' versus 'woven cotton shirts' — are discrepancies.

How to eliminate it: Copy the goods description from the LC verbatim onto the commercial invoice. Do not paraphrase or improve the description. Use exactly the words in the LC, even if they are grammatically awkward or technically imprecise.

DISCREPANCY 04: Invoice amount exceeds LC amount

What it is: The commercial invoice shows a total amount greater than the LC value.

How to eliminate it: Calculate the invoice total including all charges before preparing the invoice. Ensure freight, insurance, and any other charges included in the invoice do not cause the total to exceed the LC amount.

DISCREPANCY 05: B/L not marked 'on board'

What it is: The Bill of Lading does not contain an on-board notation confirming the goods have been loaded on the named vessel. A received-for-shipment B/L is not compliant unless an on-board notation has been added.

How to eliminate it: Always request an on-board B/L from the carrier rather than a received-for-shipment B/L. If the carrier issues a received-for-shipment B/L, ensure the carrier adds an on-board notation with the vessel name and date before presentation.

DISCREPANCY 06: B/L consigned incorrectly

What it is: The Bill of Lading is made out to the wrong party. If the LC specifies 'to order of issuing bank,' the B/L must be consigned exactly that way — not 'to order' alone, not 'to order of applicant.'

How to eliminate it: Read the LC consignee instruction precisely. Copy it exactly onto the shipping instruction to the freight forwarder. Verify the B/L when received before presenting.

DISCREPANCY 07: Wrong number of original B/Ls presented

What it is: The LC requires a full set of originals (3/3) but the beneficiary presents only 2/3, or the B/L shows it is 1/1 but the LC requires a full set.

How to eliminate it: The LC typically specifies how many originals are required. Instruct the carrier to issue the correct number. If the LC is silent, UCP 600 Article 20 requires a full set to be presented if more than one original is issued.

DISCREPANCY 08: B/L freight payment notation incorrect

What it is: The B/L shows 'freight collect' when the LC requires 'freight prepaid' (under CIF or CPT terms), or vice versa.

How to eliminate it: Check the Incoterm in the LC. Under CIF, CFR, CPT, or CIP, freight must be prepaid. Under FOB, FCA, or FAS, freight is typically collect. The B/L freight notation must match the Incoterm.

DISCREPANCY 09: Certificate of origin issued by wrong authority

What it is: The LC specifies a certificate of origin issued by 'the Chamber of Commerce' but the beneficiary presents one issued by 'the Ministry of Trade.' Or the LC specifies a specific form (e.g., Form A) but the wrong form is used.

How to eliminate it: Read the LC specification for the certificate of origin precisely. If it specifies a particular issuing authority or form, that is what must be presented. Do not substitute another document that appears equivalent.

DISCREPANCY 10: Insurance certificate amount insufficient

What it is: The insurance certificate covers less than 110 percent of the CIF value, as required by UCP 600 Article 28.

How to eliminate it: Calculate the minimum insured amount as CIF value multiplied by 110 percent before requesting the insurance certificate. Specify this amount in the insurance instruction. Verify the certificate shows the correct figure before presenting.

DISCREPANCY 11: Insurance certificate not signed

What it is: The insurance certificate or policy is presented unsigned, or signed by a party who is not an insurer, underwriter, or their agent.

How to eliminate it: Ensure the insurance certificate is signed by the insurer, underwriter, or their authorized agent before presentation. A cover note from a broker, even if signed, is not an acceptable insurance document under UCP 600.

DISCREPANCY 12: Documents inconsistent with each other

What it is: The description, quantity, weight, or marks on the commercial invoice do not match the packing list, or the packing list quantities do not match the B/L.

How to eliminate it: Before presenting documents, check every figure against every other document. Quantities on the invoice must match the packing list. The net and gross weights on the packing list must match the B/L. Marks and numbers must be consistent.

DISCREPANCY 13: Packing list shows different quantities from invoice

What it is: The packing list shows a different number of units or different package count than the commercial invoice.

How to eliminate it: Prepare the invoice and packing list simultaneously from the same source data. Do not prepare them independently and then combine them. Verify totals on both documents before signing off.

DISCREPANCY 14: Missing documents

What it is: The LC requires a document that the beneficiary does not present — most commonly a specific inspection certificate, a beneficiary's certificate, or a packing declaration.

How to eliminate it: Before shipment, create a complete checklist of every document required by the LC, including any beneficiary's certificates or special declarations. Tick off each document when prepared. Do not present without the complete set.

DISCREPANCY 15: Documents presented to wrong bank

What it is: Documents presented to the advising bank when the LC specifies presentation to the issuing bank, or to a non-nominated bank.

How to eliminate it: Read the LC presentation instructions precisely. Article 6 of UCP 600 specifies where presentation must be made. Present to the bank nominated in the LC for negotiation, acceptance, or payment.

DISCREPANCY 16: Beneficiary's certificate not signed correctly

What it is: Many LCs require a beneficiary's certificate — a signed statement by the seller certifying something about the goods, the shipment, or the transaction. If the signatory title does not match what the LC requires (e.g., 'managing director' instead of 'director'), it is a discrepancy.

How to eliminate it: Read the LC requirement for beneficiary's certificates carefully. Ensure the person who signs has the title specified in the LC. If the LC does not specify a title, any authorized officer can sign.

DISCREPANCY 17: Port of loading or discharge does not match

What it is: The B/L shows a different port of loading or discharge than specified in the LC.

How to eliminate it: Verify that the actual shipping route matches the LC specification before accepting the booking. If the shipping line uses a different loading port or transshipment point, obtain an amendment before shipment.

DISCREPANCY 18: Partial shipment not permitted but documents indicate partial shipment

What it is: The LC prohibits partial shipments, but the documents show that only part of the LC quantity was shipped.

How to eliminate it: If the LC prohibits partial shipment, ship the entire quantity in one shipment. If this is not operationally possible, request an amendment to permit partial shipments before the first shipment is made.

DISCREPANCY 19: Transshipment not permitted but routing involves transshipment

What it is: The LC prohibits transshipment, but the shipping routing involves a change of vessel at an intermediate port.

How to eliminate it: Verify the shipping routing before booking. If the carrier routes through a transshipment port and the LC prohibits transshipment, either change the routing or request an LC amendment.

DISCREPANCY 20: Expiry date conflict between LC and amendment

What it is: An amendment was issued extending the LC expiry date, but the original expiry passed before the beneficiary formally accepted the amendment.

How to eliminate it: Under UCP 600, an amendment is not binding until accepted by the beneficiary. Accept amendments in writing promptly. Do not assume an amendment is effective simply because it has been issued.

The Complete LC Document Preparation Workflow

The following workflow represents the discipline that leading export companies apply to every LC transaction. It is designed to eliminate discrepancies before documents are presented, rather than discovering them after the fact when the options for resolution are limited and the costs are real.

Step 1 — Receive and Review the LC Immediately	When the LC arrives from the advising bank, review it the same day against your ability to comply. Check the expiry date, the latest shipment date, the document requirements, the description of goods, the port specifications, and any special conditions. Do not wait until just before shipment to discover that the LC contains terms you cannot meet. If you need an amendment — request it immediately, while there is still time to get it issued and the buyer is still motivated to cooperate.
Step 2 — Create a Compliance Checklist	Create a document that lists every requirement of the LC — every document required, the exact specification of each, the quantities and amounts, the dates, the ports, the shipping conditions. This becomes the control document for the entire transaction. Every person involved in preparing documents works from this checklist.
Step 3 — Align Production and Logistics	Share the LC requirements with your production and logistics teams. Confirm that the shipment can be made from the correct port, on time, in the correct quantity, to the correct destination. Confirm that the freight forwarder understands the B/L requirements. Confirm that the carrier's routing does not involve prohibited transshipment.
Step 4 — Prepare Documents in Parallel	Prepare all documents simultaneously, using the compliance checklist as the reference for every entry. Do not prepare the invoice first and then the packing list — prepare them together so every figure is consistent from the start. Prepare the beneficiary's certificate and any required declarations before shipment if possible, so they are ready when the transport documents arrive.
Step 5 — Internal Review Before Presentation	Before presenting documents to the bank, conduct a complete internal review comparing every document against every other document and against the LC requirements. Check amounts, quantities, descriptions, weights, marks, dates, and signatories. This internal review should be conducted by someone other than the person who prepared the documents.
Step 6 — Present to the Correct Bank Within the Deadline	Present to the bank nominated in the LC, not to any other bank. Present within the validity of the LC and within 21 days of the transport document date unless the LC specifies a different period. Keep copies of all documents presented and obtain a receipt from the bank confirming the date of presentation.
Step 7 — Follow Up on the Examination	After presentation, follow up with the bank on Day 3. The bank has five banking days to examine documents. If documents are complying, payment should follow the LC terms. If there are discrepancies, you want to know as early as possible to decide whether to seek a waiver from the applicant or to correct and re-present.

01

CASE STUDY 1

Precision Engineering Ltd.

A \$4.2M Discrepancy That Nearly Became a Catastrophe — and How It Was Resolved

Background

Precision Engineering Ltd. is a UK manufacturer of industrial pumping equipment that had just completed its largest ever export order — four million two hundred thousand dollars of pumping stations for a water authority in Saudi Arabia, secured by an irrevocable LC issued by Riyadh Bank and confirmed by HSBC London. The manufacturing had gone well, the goods were excellent, and the shipment had been made on time. When Precision's export team presented documents to HSBC,

they received a notice of refusal citing four discrepancies. The export manager had twenty-four hours to decide how to respond before the goods cleared customs in Jeddah and the Saudi buyer could potentially take possession without paying.

The Four Discrepancies

◆ PRECISION ENGINEERING — DISCREPANCY RESOLUTION

PRECISION ENGINEERING — DISCREPANCY ANALYSIS

DISCREPANCY 1: Late presentation

LC required: documents within 21 days of B/L date

B/L date: March 14

Presentation date: April 6 (23 days — 2 days late)

SEVERITY: High — issuing bank can rightfully refuse

DISCREPANCY 2: Goods description mismatch

LC description: 'Industrial centrifugal pumping stations'

Invoice description: 'Industrial centrifugal pump stations'

('pumping' vs 'pump' — one word different)

SEVERITY: Medium — technically discrepant under strict compliance

DISCREPANCY 3: Weight discrepancy between invoice and packing list

Invoice gross weight: 48,200 kg

Packing list gross weight: 48,350 kg

SEVERITY: Medium — amounts must agree across documents

DISCREPANCY 4: Inspection certificate not presented

LC required: third-party inspection certificate

Bureau Veritas certificate was in the file but not submitted

SEVERITY: Critical — required document missing entirely

RESPONSE OPTIONS:

Option A: Seek applicant waiver (Saudi buyer agrees to waive)

Option B: Correct and re-present (if LC not expired)

Option C: Negotiate with bank

RESOLUTION ACHIEVED:

Discrepancy 4 (missing cert): located and submitted same day

Discrepancy 3 (weight): new packing list corrected and reissued

Discrepancy 2 (description): Saudi buyer provided waiver letter

Discrepancy 1 (late): Saudi buyer provided waiver letter

HSBC accepted waivers from Riyadh Bank; payment made day 8

COST OF DISCREPANCIES: 8 days interest + bank fees = EUR 18,400

The Root Cause Analysis

When Precision's management reviewed the incident, all four discrepancies were preventable. The late presentation occurred because the export manager had calculated the twenty-one day period from the estimated shipment date rather than the actual B/L date, and had not built in a buffer for the two days the courier took to deliver the transport documents from the freight forwarder. The description mismatch occurred because the invoice template used an abbreviated description that had been developed years earlier and never checked against LC requirements. The weight discrepancy occurred because the invoice and packing list were prepared by different people from different data sources. The missing inspection certificate occurred because nobody had created a complete document checklist for this transaction.

The company's response was to implement the seven-step workflow described earlier in this part, including a mandatory internal review by a second person before any LC documents are presented. In the eighteen months following that implementation, the company's discrepancy rate fell from sixty-three percent of presentations to eight percent — and the eight percent that remained were all minor items that were resolved by applicant waiver on the same day.

02

CASE STUDY 2

Sunrise Textiles Export

Confirmed LC Saves an Exporter When the Nigerian Issuing Bank Is Frozen

Background

Sunrise Textiles Export is an Indian manufacturer of cotton yarn. In January 2023, Sunrise received a significant order from a Nigerian buyer for eight hundred and forty thousand dollars of cotton yarn, secured by an LC issued by Heritage Bank Nigeria. Sunrise's previous experience with Nigerian LCs had been problematic — two years earlier a different Nigerian bank had delayed payment for four months — so this time Sunrise's CFO insisted on confirmation from Standard Chartered Bank Mumbai before accepting the LC. The confirmation cost six thousand seven hundred and twenty dollars. Sixteen days after Sunrise shipped the goods and presented complying documents, Heritage Bank Nigeria was placed under CBN conservatorship. No international payments were processed for eleven months.

◆ CONFIRMATION — FINANCIAL IMPACT

SUNRISE TEXTILES — CONFIRMATION SAVES \$840K

LC amount: \$840,000 | Confirming bank: Standard Chartered Mumbai

Documents presented: March 15 (complying presentation confirmed)

Heritage Bank CBN conservatorship: March 31

WITH CONFIRMATION:

Standard Chartered Mumbai obligated to pay independently

Standard Chartered Mumbai pays \$840,000 on April 3

Standard Chartered seeks reimbursement from Heritage Bank

(Standard Chartered's problem, not Sunrise's)

Sunrise received: \$840,000 - \$6,720 confirmation fee

= \$833,280 net proceeds

WITHOUT CONFIRMATION (hypothetical):

Heritage Bank frozen; no international payments

Sunrise waits 11 months for Heritage Bank resolution

Ultimate recovery: approximately 60 cents on the dollar

Net recovery: $\$840,000 \times 60\% = \$504,000$

After 11 months interest cost: further \$46,200 lost

Effective loss without confirmation: \$382,920

CONFIRMATION FEE: \$6,720

LOSS AVOIDED: \$382,920

ROI OF CONFIRMATION: 56x

The six-second decision to request confirmation saved \$382,920 and protected an entire year's relationship

03

CASE STUDY 3

Global Trading House Ltd.

*Back-to-Back LC — Financing the Full Trading Cycle Without Own Capital***Background**

Global Trading House Ltd. is a Hong Kong-based trading company that sources electronics components from manufacturers in mainland China and sells them to buyers in Europe and North America. In a typical transaction, Global Trading earns a margin of fourteen percent on the goods it intermediates — but it does not manufacture anything itself and does not want to tie up its own working capital in inventory financing. The back-to-back LC structure allows Global Trading to finance its entire supply chain using its buyers' creditworthiness rather than its own.

◆ BACK-TO-BACK LC — TRADING COMPANY MECHANICS

GLOBAL TRADING — BACK-TO-BACK LC MECHANICS

MASTER LC (from European buyer to Global Trading):

Amount: \$1,400,000 | Issuing bank: Deutsche Bank Frankfurt

Beneficiary: Global Trading House Ltd., Hong Kong

LC type: Transferable (master LC marked transferable)

BACK-TO-BACK LC (from Global Trading to Chinese manufacturer):

Amount: \$1,204,000 (86% of master — Global Trading margin = 14%)

Issuing bank: HSBC Hong Kong (Global Trading's bank)

Based on security: Master LC pledged to HSBC as collateral

THE CRITICAL DIFFERENCE: BACK-TO-BACK vs. TRANSFERABLE

Transferable LC: buyer's bank (Deutsche Bank) directly transfers a portion of the original LC to the supplier

Back-to-Back LC: Global Trading's bank (HSBC) issues a

NEW, SEPARATE LC to the supplier, using the master LC

as security — Global Trading's margin is fully protected

because the master and back-to-back are separate instruments

SETTLEMENT FLOW:

1. Chinese manufacturer ships and presents to HSBC HK
2. HSBC HK pays \$1,204,000 to Chinese manufacturer
3. Global Trading substitutes its own invoice (\$1,400,000) and presents to Deutsche Bank Frankfurt
4. Deutsche Bank pays \$1,400,000 (or reimburses HSBC)
5. HSBC retains \$1,204,000 reimbursement; pays Global Trading the \$196,000 margin less fees

GLOBAL TRADING'S WORKING CAPITAL USED: \$0

MARGIN EARNED: \$196,000 (14% of \$1,400,000)

HSBC BACK-TO-BACK LC FEE: approximately \$8,500

NET PROFIT: \$187,500 on zero capital investment

■ KEY TAKEAWAYS FROM PART 26

The Letter of Credit is not a complicated instrument at its core — it is a promise by a bank to pay against documents. What makes it complex in practice is the precision it requires. Every word in the LC is a commitment by one party and an obligation on another. Every document presented must reflect those words exactly. The companies that master LC operations — that achieve consistently clean presentations, that select the right LC type for every transaction, that

know when to insist on confirmation and when to accept an unconfirmed LC — have a genuine and measurable financial advantage in international trade. The investment in training, process, and discipline that produces a clean presentation rate above ninety percent pays for itself many times over in reduced discrepancy costs, faster payment, and stronger banking relationships.

For further context on the payment methods that sit alongside the LC in the trade finance toolkit, refer back to Part 5. For the trade finance instruments that complement LC-based transactions, refer to Parts 6A and 6B.