

Corporate Banking

top@doc Newsletter

Payment under documentary credits: Agreement of a final instalment after goods have been accepted



Buyers and sellers often agree that the value of goods is not payable in one sum upon shipment of the goods or presentation of the corresponding transport documents under a documentary credit, but is to be paid in several instalments. Thus, for example, an advance payment is quite common and, in addition, the payment of a final instalment can be specified. This instalment is then usually payable when the delivered goods have arrived at the buyer's and meet his requirements, which can be documented by acceptance records, acceptance certificates or the like. However, the wording with which the maturity of this final instalment is defined is not always clear and, in practice, frequently leads to contentious discussions. In the current edition of top@doc we present three examples of this.

Example 1:

A documentary credit is advised to WellDone Ltd. by its principal banker, Free and Easy Bank. The relevant underlying transaction provides for the delivery of a beverage bottling machine by WellDone Ltd. The documentary credit is confirmed by Free and Easy Bank by order of the issuing bank, Careful Bank.

The documentary credit provides for shipment of the goods on 1 September 2017, at the latest. It is available with Free

and Easy Bank, payable at sight, and expires on 31 October 2017.

According to the credit conditions, the counter value of the bottling machine is to be paid in three instalments:

- "20 percent of the amount of the letter of credit is payable against presentation of an advanced payment guarantee."
- "70 percent of the amount of the letter of credit is payable against presentation of a commercial invoice in 3 copies, a full set of bill of lading, a packing list 4-fold and a certificate of origin in duplicate."
- "10 percent of the amount of the letter of credit is payable against the acceptance certificate, countersigned by the applicant, 120 days after shipment at the latest".

WellDone Ltd. checks whether the credit conditions comply with the agreements which were made in advance with the buyer of the goods. Various questions arise here for WellDone Ltd.

By what date is the acceptance certificate for payment of the final instalment to be presented at the latest? Does the confirmation of Free and Easy Bank extend beyond the life of the documentary credit even if the acceptance certificate is presented after expiry of the documentary credit, but within the 120 days after shipment of the goods? And what happens

if WellDone Ltd. does not present an acceptance certificate at all? After all, this is a credit condition which requires the co-operation of the buyer for its fulfilment (so-called “conditional” documentary credit, see also top@doc No. 106 “Joker Clause – conditional letter of credit: What is hidden behind these terms?”). Is the payment of the final instalment of 10 percent made automatically 120 days after the date of shipment, even without presentation of an acceptance certificate?

WellDone will no doubt have contacted its principal banker to clarify these questions – unfortunately, we do not know the reply of Free and Easy Bank. Commerzbank, however, would reply as follows:

In such a case, the confirmation of Commerzbank covers only the period of the documentary credit’s life, in other words until 31 Oktober 2017. If the acceptance certificate is presented after this date, the claim of WellDone Ltd. is no longer secured by the confirmation of the documentary credit.

Presentation of the acceptance certificate is compulsory for drawdown of the final instalment; no automatic payment is made 120 days after the date of shipment. If the buyer does not make this certificate available to WellDone Ltd., then WellDone Ltd. cannot present compliant documents for the partial amount of 10 percent and therefore does not have a payment claim secured by the documentary credit – either by the issuing bank or by Commerzbank. WellDone Ltd. should therefore consider carefully whether it is prepared to accept this credit condition.

Example 2:

Both the case construction and the credit conditions are identical to the first case study, but this time the conditions for payment of the final instalment are:

- “10 percent payable against the acceptance certificate, countersigned by applicant, 120 days after shipment at the latest without presentation of any documents”

If WellDone Ltd. is not able to present the acceptance certificate, in this case payment of the final instalment nevertheless takes place 120 days after the date of shipment – even when the documentary credit has already expired by then.

Commerzbank treats this case construction as a so-called “mixed payment” – upon presentation of the credit documents for the drawdown of 70 percent of the value of the goods (maturity at sight), the final instalment of 10 percent is simul-

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taneously noted as a deferred payment (maturity 120 days after the date of shipment), in other words by 30 December 2017, at the latest. The confirmation from Commerzbank is valid until the maturity of the final instalment, i. e. also beyond expiry of the documentary credit.

Example 3:

This example also proceeds on the basis of the above credit conditions, but with the following statement on the drawdown of the final instalment:

- “10 percent payable against the acceptance certificate, countersigned by applicant, or payable 120 days after shipment against a commercial invoice and the beneficiary’s declaration that an acceptance certificate can not be provided.”

The following scenario then emerges: everything is so far in order with the bottling machine which has been delivered and meanwhile put into operation, but for some reason WellDone Ltd. does not receive a corresponding acceptance certificate from the buyer. WellDone Ltd. first waits for a while – perhaps the certificate will arrive after all. Unfortunately they then lose track of the transaction, but at some point WellDone Ltd. notices that it is still missing the remaining amount of 10 percent. Now there is great excitement – it is already mid-October 2017, and the machine was shipped on 15 May 2017. The beneficiary’s declaration is prepared in a hurry and presented to Free and Easy Bank together with the commercial invoice for drawdown under the documentary credit on 25 October 2017.

Does Careful Bank have to pay? Or has the claim from WellDone Ltd. for payment of the final instalment under this documentary credit lapsed, since the period of 120 days after shipment has meanwhile expired?

WellDone Ltd. can relax – since the documentary credit has not yet expired, the company can certainly still assert this claim by presentation of the commercial invoice and the beneficiary's declaration. In this case there is no credit condition, nor is there a provision in the "Uniform Customs and Practice for Documentary Credits" (UCP) 600, to prevent this.

By its late drawdown of the final instalment, WellDone Ltd. has given the buyer of the goods an advantage. If WellDone Ltd. had not neglected to draw, the final instalment would already have had to be paid on 12 September 2017, in accordance with the credit conditions.