Compliance Rules in Documentary Credit Transactions*

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Abstract
The purpose of this paper is to review compliance rules in transactions involving documentary letters of credit. The principle of strict compliance used in most banks (as a tool to determine whether or not discrepant factors exist) has shown a tendency to take a pragmatic approach considering the functions of the commercial credit and the essential features of the compliance rules in letters of credit, as well as the necessary guidance that ISBP 745 gives to identify these matters. Understanding the criteria in checking the documents presented may reduce refusal rates of those documents on presentation.

Keywords: Discrepancy, ISBP 745, Strict Compliance, Unclear Instruction
JEL Classifications: F18; F33; F35

I. Introduction

Documentary credit was devised to facilitate commercial transaction that is performed internationally. The use of documentary credit minimizes or eliminates the risks of non-payment to the exporter and non-delivery of contract goods to the importer. The documentary credit mechanism (which provides the exporter’s goods and the importer’s payment, interchanged through the bank involved) provides security for the contracting parties through a linkage of payment and security functions.

Documentary credit (D/C) as a payment tool has been used as a secure method of
payment available in international sale transactions. Its usefulness is widely acknowledged. However, the seller can be exposed to a difficult situation that prevents him from making a payment. Sometimes the documentary compliance standard does not permit the banks to make a payment to the presenter, including the beneficiary. The bank concerned carries out an examination of the documents presented, and without any detailed knowledge concerning the goods' condition when shipped or the contents of the underlying transaction. Therefore, the construction and application of the examination standard of the documents are important in documentary credit transactions. One of the most important roles of banks\(^1\)(such as the issuing bank, nominated bank or, the confirming bank, if applicable) would be to reasonably construct and apply the examination standard considering D/C practice when determining if the presented documents are consistent with the criteria established in the documentary credit practice. Documentary credit offers great benefits to the seller, but the documents tendered by the beneficiary should comply with the requirements of the credit for payment. The problem with discrepancies would come about when the bank dishonors the documents because of trivial or minor errors (for example, an actual mistyping or a mistake in the beneficiary's address in the documents). Surveys have revealed that even in trading centers bank reports, discrepancy levels are over 50% (that is, more than 50% of initial presentations of documents contain at least one discrepancy) (Jimenez, 2012; ICC, 2014).\(^2\) In falling markets, discrepancy rates of 60% to 90% have been reported. In these market circumstances, buyers may rely on the seller's documentary errors to refuse a payment (Jimenez, 2012; ICC, 2014).

This paper reviews the attitude toward interpretation of the examination standard in actual practice, and application of compliance requirements provided in the Uniform Customs and Practice for Documentary Credit, 2007 Revision (UCP 600) Art. 2 Compliance is vital and an essential condition to secure payment in documentary credit transactions. The prerequisite of compliance requirement required by the UCP has been relaxed in recent years, both by courts and the UCP and international standard banking practice (ISBP). Thus, I tried to survey the current practice tendency and the factors to be considered implementing the examination standard.

II. Cases of Unclear Instructions and Discrepancy in Documentary Credit

1. Unclear Instructions and Risks with Documentary Credit

Where an examination standard is applied to determine whether or not the documents tendered constitute a complying presentation, it was ruled that discrepancies that arose due to unclear instruction in commercial credit do

\(^1\) See Graham (2001) for the responsibilities and obligations of the banks involved in documentary credit transactions.

\(^2\) The statistical data relating to refusal of documents by banks may be shown to be a little different by the Institutes of survey. According to a report on a survey by the ICC, the refusal rate of documents (2013 compared with that in 2012) appears to be decreasing from 46% to 33.96%.
not justify a fair refusal of payment to the presenter, provided a reasonable construction of those instructions was made (Fortis Bank SA/NV v. Indian Overseas Bank 2009; Credit Agricole Indosuez v. Muslim Commercial Bank Ltd, 2001). In the case of Fortis Bank vs. Indian Overseas Bank (2009) treating the matters of ambiguous instructions in D/C transactions, the court judged that the issuer making the credit involving the unclear contents bears the risk of ambiguity in D/C. Solving the problem of unclear instructions in documentary credit, the court examined the documents considering each as a set of documents constructed by intelligent consideration and judgment, rather than a mechanical application of this rule. This case reflected a recent operative direction of the application of the compliance rule, considering the substantial role of the document in practice and the significance of the data specified in the documents, respectively, requested in D/C. Details of the case are narrated in the succeeding paragraphs.

The case of Fortis Bank vs. Indian Overseas Bank (2009) was related to the sale of containerized scrap and five D/Cs were issued totaling US$8,269,000. Only three of the D/Cs was confirmed. The underlying contract was concluded between a seller (Stemcor) and a buyer (SESA International Ltd.), and involved MSTC, an Indian government-owned company, as facilitator. The real buyer was SESA International Ltd. and MSTC provided financial services to SESA.

The instructions in the D/Cs in question in the Fortis Bank case were as follows:

1. MSTC will act as facilitator.
2. All documents except for the certificate of origin must be prepared in the name of the Buyer, SESA International Ltd, 31 Shakespeare Sarani, Jasmini Tower 6th Floor, Kolkata 70017.
3. Full set of clean on board ocean bills of lading stamped, prepared and signed market freight consigned to the order of Indian Overseas Bank, International Business Branch, 2, Wood Street, Kolkata 700016, India and notify the applicant and SESA International Ltd, 31 Shakespeare Sarani, Jasmini Tower 6th Floor, Kolkata 70017, India.

Five contracts for the sale of containerized scrap were facilitated by the applicant MSTC. Field 72 of the D/C requested that the advisor advise the D/Cs, which it did. Field 49 (CONFIRMATION INSTRUCTIONS) stated that advisor “MAY ADD” its confirmation. The advisor added its confirmation at the request of the seller to three of the five D/Cs.

The issuing bank claimed four discrepancies and refused to authorize reimbursement of the confirming bank and payment to the beneficiary:

1. Invoice and other related documents are not prepared in the name of the buyer.
2. Bill of Lading is not made out to the buyer.
3. Port name on commercial invoices is contrary to D/C terms.
4. Statement on consolidated certificate is contrary to D/C terms.

In relating to the first discrepancy data, the issuing bank alleged that “this is inconsistent with the true commercial facts, which were that the D/C was issued in relation to a transaction of a seller and buyer and with facilitator’s defined role (as facilitator) with in the D/C.” The bank also pointed out that the contract details were contained in Field 46A and that Field 47A stated that “MSTC WILL ACT AS FACILITATOR.”
In response to the above allegation by the issuing bank, the court ruled that what matters in the D/C transaction is not the "true commercial fact" but the documentary requirements of the D/C. The D/C does not stipulate the name of the person to whom the documents are to be addressed and does not identify the name of any buyer. The only parties identified in the D/Cs are the "APPLICANT" (MSTC) and the "BENEFICIARY" (Stemcor). Even if field 47A of the D/C stated, as an additional condition, that "MSTC WILL ACT AS FACILITATOR," it does not follow that documents issued in the name of the facilitator rather than an unnamed buyer, do not comply with the terms and conditions of the D/C. Also, the judge mentioned that in Art. 18(a) of the UCP 600, a commercial invoice must be made out in the name of the applicant. The judge concluded that if the UCP so provided for the invoice, "there can be nothing wrong (in the absence of dear instructions to the contrary) in preparing "other related documents" in facilitator's name." In the alternative, the judge concluded that the instructions in this transaction were ambiguous (Fortis Bank v. Indian Overseas Bank, 2009).  

In relating to the second discrepancy, the bills of lading presented were made out in accordance with instruction 3 required on the D/C. The problem would arise from the difference between instructions 2 and 3. Instruction 2 required the bill of lading to be issued in the buyer's name, but instruction 3 required the bill of lading to be consigned to order of the Indian Overseas Bank. Among these conflicts between two different instructions, the beneficiary selected "to order of the Indian Overseas Bank," which specified more concretely the bill of lading. However, although the beneficiary prepared the bill of lading issued in the buyer's name, the document was not compliant. Justice Hamblen said Stemcor and Fortis Bank acted on a reasonable construction thereof (Fortis Bank SA/NV and Another v. Indian Overseas Bank 2009). Where the D/C requires the document to be issued in the name of the applicant, use of the name of the D/C applicant complies even if it is not the actual buyer in an underlying contract.

The third discrepancy arose from unclear content specified in the D/C. The D/C required that "beneficiary's consolidated certificate certifies as follows: we hereby certify the following……" that the negotiating bank has been advised to dispatch original shipping documents only by air courier service to the D/C opening bank at our cost……." However, the consolidated certificate presented by the beneficiary stated "……to the D/C opening bank at issuer's cost." The judge ruled that this discrepancy justified refusal because the words "we hereby certify the following……" make it plain that "our" is to be identified with "we"- i.e. the person giving the certificate-namely seller/beneficiary. He also said that there is no ambiguity and it would be known that issuer was not charged for dispatch of the documents.

The beneficiary sued the issuing bank for unjustifiably dishonor, and the confirming bank negotiated the documents presented by the beneficiary sued the issuing bank for
reimbursement.

Instructions on the five D/Cs issued in the *Fortis Bank vs. Indian Overseas Bank* (2009) case were not unified. The issuing bank (Indian Overseas Bank), according to instructions from MSTC, intended that the documents requested would be made out in the name of the buyer, SESA International. But the intended effect of MSTC was not reflected on the documents submitted by the beneficiary. So the issuing bank claimed that the tendered documents did not constitute a complying presentation and refused to make a payment to the confirming bank. However, Justice Hamblen concluded that because the instructions in the D/Cs were ambiguous, the issuing bank could not have the intended effectiveness through this D/C transactions and a rejection of payment by the issuing bank was not justified.

**2. Reasonable Construction and ISBP**

In the *Fortis Bank vs. Indian Overseas Bank* (2009) case, an ambiguity arose from the difference in instructions in the same D/C, which could not meet both instructions at the same time. Given the different instructions, Hamblen ruled that the judgment of the beneficiary Stemcor and Fortis bank reasonably constructed on two different instructions matters in D/C.

The attitude of taking reasonable action was indicated by the view of Devlin in the *Midland Bank Ltd. v. Seymour* (1955). He said that "the true view of the matter, I think is that when an agent acts upon ambiguous instructions, he is not in default if he can show that he adopted what was a reasonable meaning." After that, Diplock evaluated the view of Devlin as a well-established principle in relation to documentary credits in the case of *Commercial Banking Co. of Sydney v. Jalsard Pty. Ltd.* (1973). Then, he ruled in the case, by adopting Devlin's view, that if the instructions given by the customers to the issuing banker as to the documents to be tendered by the beneficiary are ambiguous or are capable of covering more than one kind of document, the bank is not in default if it acts upon a reasonable meaning of the ambiguous expression or accepts any kind of document which fairly falls within the wide description used (Commercial Banking Co. of Sydney v. Jalsard Pty. Ltd., 1973).

While a beneficiary would bear the risk of discrepancies, an applicant would bear the risk of ambiguous instructions. ISBP 681 and 745, in part of the Preliminary Considerations, provided to whom the risk of an ambiguous instruction belongs:

"The applicant bears the risk of any ambiguity in its instructions to issue or amend a credit. Unless expressly stated otherwise, a request to issue or amend a credit authorizes an issuing bank to supplement or develop the terms in a manner necessary or desirable to permit the use of the credit."

As a well-established rule of common law of England, the principle that bears the risks of ambiguous instructions is stipulated in the ISBP which is very important and meaningful. The case of Fortis Bank was exactly appropriated for this provision of ISBP.

**3. Judgment on Compliance Rule**

The third discrepant data claimed by the issuing bank was the port's name on commercial invoices as mentioned previously. The fourth D/C contained a trade term "US$600.00 NET MT, CFR CY, Haldia/Kolkata, India." However, the invoice tendered specified "US$600.00 NET MT, CFR CY, Haldia, India and
omitted Kolkata. The issuing bank’s notice of refusal stated “the commercial invoice does not comply with the price term of the D/C.”

Because of the fact that Haldia is a port in Kolkata, the judge accepted that Haldia and Kolkata were being referred to in the price term as alternatives and that a reference to Haldia alone is appropriate or at least suffices in circumstances where the goods were shipped under the Haldia bill of lading. The judge noted that because the price term of the D/C was not a documentary requirement, there was no inconsistency in circumstances where Haldia is one of the named ports. Furthermore, the judge said that where a D/C contains a virgule, the use of either term separated by the virgule complies with the terms of the D/C (Meynell, 2013). The court also stated that the compliance rule needs to be interpreted intelligently rather than mechanically.

With this attitude toward interpretation of the documents presented, the position of data stated on the documents requested should not affect the complying presentation. For example, even though the buyer’s name was stated on “Description of Package and Goods,” it would not be considered as a discrepancy because the buyer is clearly not a package.

III. Fraud and the Application of the Compliance Rule

When circumstances arise whereby the seller has reason to be concerned with the buyer’s ability to pay, or the buyer has reason to doubt the seller’s ability to deliver the goods, a D/C provides that both parties appropriately perform the payment and shipment requirements (Cronican, 2014; Graham, 2001). Since the buyer is not present to supervise the performance of the sale contract, he has to rely on the accuracy of the documents. The principle of compliance in the D/C transaction offers a certain degree of security for both the issuing bank and applicant/buyer, but it also may contain several loopholes caused by documentary transactions irrespective of the actual performed fact. Documents could be prepared dishonestly, such as through forgery or falsification of documents. Being unaware of the dishonest circumstances, the banks could make a payment to the presenter. Banks examine the documents tendered by applying the compliance standard but without any knowledge of the condition of the goods shipped or the actual fact performed in the underlying contract. This characteristic of the payment mechanism in the D/C transactions might be the cause of fraudulent acts by parties in making the documents. The payment system of credit has both aspects of security and inaccuracy.

The case submitted to the District Court of Hamburg in 2000 implied that the principle of compliance could not perfectly protect the issuing bank from damages arising due to

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5) ISBP 745 Paragraph A2 indicates clear guidance that virgules will allow the use of one or more of the options.
6) Evans IC noted that “the question of compliance should be considered intelligently rather than mechanically and may involve the exercise of judgment (Krediet Bank Antwerp v. Midland Bank 1999).”
7) In order to claim that a party had committed L/C fraud, it is required that clear and sufficient proof supporting its defense shall be shown. See Bulgrains & Co. v. Shanghai Bank (2013); Caledonian Bank & Trust Ltd. v. Fifth Third Bank (2013); Century Pulp & Paper v. M/V “MSC Damla” (2013); Cheng Kelly Kit Yin v. Secretary for Justice (2013); Fink v. Corporate Liaison (2013).
8) The issuing bank must pay even if a buyer is insolvent,
wrong doing, as can be seen from the following example (Timothy, 1993; Cronican, 2014).

On January 11 1999, the carrier issued a bill of lading stipulating the seller was the shipper of the goods and confirming that the goods had been shipped on board a certain vessel that was to transport them from Goteborg, Sweden, to Dubai. However, the goods were not shipped on board this vessel on January 11 1999, but at a later date, perhaps on January 14 1999. According to subsequent instructions offered by a subsidiary of the applicant, the goods shipped were not transported to Dubai, but to Singapore, where they went missing.

After it became apparent that the bill of lading had been issued dishonestly, the issuing bank which honored the presenter sued the carrier for reasons of fraud. The carrier argued that there was no causation between the incorrect bill of lading and the damages suffered by the issuing bank. He also claimed that the cause of damage was the disappearance of the goods shipped, not the inaccurate on-board notation.

By applying the principle of the compliance, the court ruled that the issuing bank was entitled to request damages resulting from the carrier’s dishonesty. The court pointed out that the presentation of the incorrect bill of lading caused the issuing bank to honor the beneficiary, and thus it was the actual cause of the bank’s damage. Perhaps, the court should look to find out the substantial cause of damage suffered by the issuing bank. The essential cause of loss arose from the incorrect decision relating to the on-board notation. Thus, the forged bill of lading was sufficient to cause damage to the issuing bank, thus the issuing bank could recover the relative damages caused by the carrier’s dishonest behavior.

Actually, where the bank examined the documents tendered and its decision to honor the beneficiary were not related to whether or not the goods were on board on the actual shipment dates. The judgment of the court reaffirmed the fundamental role of the compliance rule in documentary credit transactions and its operation for the bank’s protection and for keeping the payment system secure.

This case would be regarded as a leading case against issuers of dishonest or fraudulent documents (Blue Rider Financial, Inc., v. Harbor Bank Maryland, 2013).

IV. Permissible Error and/or Trivial Discrepancy Fraud

1. Examination as a Set of Documents

The documents required by the D/C are closely related to the performance of the underlying contract executed between a seller and a buyer. The documents generally include items such as bills of lading, documents indicating that the items have been shipped, or proof of insurance, which a buyer wishes to be performed by a seller. For a buyer in a foreign country it is not easy to confirm whether or not a seller performed the contract observing the agreed-upon terms and conditions. Usually, the documents typically requested for payment constitute a commercial invoice such as a bill for price, a bill of lading as evidence of shipment, an insurance policy,

cannot, or refuses to reimburse the bank for payment to the beneficiary.
a survey report as certificate of quality, a certificate of origin, a packing list and other necessary documents. Because the data and contents indicating all documents specified in the D/C provide a basic level of proof that the seller has properly followed an underlying contract, the checkers of the document need to have the right attitude to consider the documents as a whole, and then should decide whether or not to honor the presenter.

Generally, when bank personnel review the presented document, they would examine data in the document based on each document tendered. Where the examination of documents is enacted based on each document, the number of disputes around discrepancies in the D/C transaction would increase. In relation to this matter, UCP 600 Art. 14(d) provides that "data in a document, if not be identical to, but must not conflict with, data in that document, any other stipulated document or the credit." The requirements of the documentary credit, the contents and purpose of the document itself, and international standard banking practice need to be assessed, understood and taken into consideration in determining the compliance of a document (ICC, 2007). For example, data relating to the consignee in a certificate of origin that differ from the consignee data in the bill of lading would not be deemed as indicative of conflict between documents. The consignee specified in the certificate of origin would be needed for customs purposes, whereas the consignee in the bill of lading relates to the function of the document as a document of title. The name of "consignee" is required in both documents, but serve different purposes in different columns in the documents. It is clear that each document constituting a set of documents is linked to other documents requested in the D/C. In the case of Midland Bank Ltd. v. Seymour (1955), Devlin said "... it is sufficient that the description should be contained in the set of documents as a whole and that the documents should each one be valid in itself and each be consistent with the other..." He also said "the documentary credit ... does not say specifically which particulars are to be put in which document (Midland Bank Ltd. v. Seymour, 1955)." The ICC also describes the documents stipulated in documentary credit are relating to "linkage" in the documents. By using the phrase "if stated" in sub Art. 14(e), it also emphasizes that there is no need for a "description of goods" to appear on every document. This is a clear reference to those ICC national committees that believed that the UCP should include a description of the goods on each document tendered as one of the ways to achieve linkage (ICC, 2007).

There was the DOCDEX case which reviewed the documents as a whole (Collyer, 2014). In both credits with special conditions, certain data, as required by the credit, are not indicated in the documents: the D/C number and date in the first credit; apart of the vessel name in the second.

Special Conditions applied to both credits: "All required documents must indicate our L/C number and date."

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9) Concerning the principle of compliance rule, Schmitthoff mentioned that "the legal principle that the bank is entitled to reject documents which do not strictly conform to the terms of the credit is conveniently referred to as the doctrine of strict compliance (Murray et al, 2007)."

10) UCP 600 Art. 14(e) specified "In documents other than the commercial invoice, the description of the goods, services or performance, if stated, may be in general terms not conflicting with their description in the credit."
"Any minor typing mistake which will not affect quality, quantity, price, value and the expiry date and shipment date shall be acceptable."

The issuing bank in credit 1 refused to make a payment due to "invoice not indicating LC number and date." For the above reason to dishonor, the negotiating bank claimed: a. the missing LC number and date indicate a typing error, while the LC number and date are correctly shown on other invoices and other documents in the presentation, b. the lack of credit number and date is covered by the special condition in the credit where "typing mistake which will not affect quality, quantity, … shall be acceptable"; c. ISBP paragraph 25 indicates a practice where misspelling or typing errors do not make a document discrepant and d. Banking Commission Opinions R289 and R635 state that a credit number on a document only assists in tracing documents and even the misquoting of a credit number is not a ground for refusal of documents.

The issuing bank in credit 2 refused the documents because the "invoice indicated different name of vessel from that of bill of lading."

Considering those facts, the court ruled that the documents tendered under credit 1 and credit 2 do not constitute discrepancies, and that it is sufficient evidence in the documents as a whole to reflect compliance with the credit.11)

2. Trend in Treatment of Trivial Discrepancies and Interpretation of Complying Presentation

Would an inconsistency to some degree be constituted to be a true discrepancy? What role should the complying presentation in the documentary credit system play in supporting mechanisms that certify to the safety of the trade finance system?

A response to these queries will be helpful to judge whether the documents presented comply with a credit’s requirement. The banks are not obliged to make any examination beyond the face of a document to establish if a document complies with a requirement in a documentary credit or with any requirement in the UCP and ISBP. Thus, the banks must decide on the basis of the document alone. The principle that the banks deal with documents themselves serves to protect the banks, but it also may work against a beneficiary (usually the seller). The more discrepancies would be pointed out by the banks, the more weak the seller’s position would be (Jimenez, 2012). Where the compliance standard is strictly constructed, it may permit the banks to avoid payment to the beneficiary. Considering these dilemma, namely protection and prevention, the banks will closely review there levant documents to see if they complied with the credit conditions. In actual practice, it is said that most discrepancies do not prove harmful because the buyers are usually willing to tolerate the discrepancy (Jimenez, 2012).

The judicial constructions of the word compliance have been developed so as to distinguish between true discrepancies and simple (minor) errors. However, the criteria used by the court to distinguish the kind of

11) ICC Opinions R289, 578, 635 and TA 774 all address this matter and are consistent in their conclusion: "A requirement for the insertion of a credit number on a document is only to assist in tracing documents should they go astray. Since the documents were received by the issuing bank and the issuing bank is applying the presented bill of lading under the correct credit number, it would seem to be an irrelevance, and not valid grounds for refusal."
discrepancies would depend on the case in question. In the Bankers Trust Co. v. the State Bank of India (1991), Lloyd considered as trivial discrepancy the fact that the telex number of the buyers’ office was given as 931310 instead of 981310. The other example of a trivial error as an obvious typographical error was offered in Krediet bank Antwerp v. Midland Bank, where Smithh was used instead of Smith.

UCP 600 Art. 14(d) and (e) indicate that the function of the document requested in credit and the other relationships of data in the submitted documents must be considered. As stated previously, the description of goods on a document other than the commercial invoic e12) could show a minor difference and that difference would not justify dishonor where all the other documents do not conflict with any other documents. Besides, the concept of “on their face” of UCP 600, as it is used in relation to the examination of documents, can be extended to the review of data within a document in order to determine if complying presentation was made. The phrase “on their face” does not refer to a simple front versus the back of a document (ICC, 2007).

In the case of Choheung Bank v. Bank of China (2001), the court judged that a compliance standard was not necessarily required or that documents required must be consistent with the exact lettering, but that the documents should be deemed as consistent with conditions of the credit, where even though there are slight differences, there is no difference in meaning in the wording and no harm is done to the credit conditions. In addition, the court interpreted that where a bill of lading contains two dates, the later date will be considered to be the shipment date of the bill of lading (B/L) based on UCP 600 and does not necessarily prohibit a separate shipment date on the B/L. The earlier date would be disregarded, whatever the reason. Such as light difference could be seen as complying with the terms and conditions of the documentary credit on its face from the viewpoint of ISBP.13) Also, in the case of the Korea First Bank v. Korea Export Insurance Corp. (2002), the court noted that for the documents attached to the documentary credit to be strictly in accordance with the terms and conditions of the credit, it does not necessarily mean that they must be completely in compliance with each other letter to letter. When there exists a slight difference in words and phrases but the bank considers that it does not constitute enough of a difference and does not harm the terms desired by the documentary credit at all from its face, it should be regarded as in accordance with the terms and conditions of the documentary credit. These judicial decisions in Korean court implicitly indicate adopting a progressive approach to discrepancies in credit transactions.

According to ISBP, a mistyping does not affect the meaning of a word, for example, a description of the merchandise as “machine” instead of “machine”, “fountain pen” instead of “fountain pen” or “model” instead of “model” would not make the document discrepant. However, a description as “model 123” instead

12) The DC described the goods as “Wheat Bran Pellets in bulk” in the commercial invoice, but invoice presented described the goods as “Bulgarian wheat grain pellets.” The court rules that “the description of the goods in the invoice did not comply with the terms and conditions of the credit (Bulgrains & Co v. Shinhan Bank, 2013).

13) Misspellings or typing errors of the ISBP 681: “A misspelling or typing error that does not affect the meaning of a word or the sentence in which it occurs, does not make a document discrepant.”
of “model 321” would not be regarded as a typing defect and would constitute a discrepancy. Such an error would be interpreted as different merchandise. Considering the issue of complying presentation, it is reflecting the policy of a documentary credit without the mirror-image principle. In 2004, the China court also ruled whether or not the documents were incompliance with the terms and conditions of the L/C based on the function of a documentary credit, which is the means to make a payment rather than a means to refuse payment (Bank of China (Fujian Branch) v. Bank of East Asia, 2004; Civil Judgement, 2002; Min Jing Zhong Zi Na 126). The appellate court indicated that strict compliance does not mean slavish conformity to the terms of the commercial credit (Bank of China (Fujian Branch) v. Bank of East Asia, 2004).

In Israel during the 1990s, the standard to judge the complying presentation was changed from a formalistic strict compliance approach to an essential approach considering a substantial purpose of the contract (Bank Leumi Le-Israel B. M. v. Halimex Trade, A.G., 1994). Moreover, the good faith principle was implemented in a decision over the matter concerning whether or not the discrepancies exist. The application of the good faith principle in the Israeli legal system indicates that the documentary discrepancy in credit transactions needs to be examined, considering the essence of the business transaction and its purpose. It does seem that several decisions rendered by district courts in Israel indicate a transition from strict compliance to practical compliance without adhering to the word of strict compliance itself.15)

Where there is no justification for dishonoring trivial discrepancies, the method to solve this important problem is to differentiate between a trivial discrepancy and a true discrepancy. The bank would not be in a position to verify actual performance of the underlying contract (ALYK (H.K) Ltd. v. Caprock Commodities Trading Pty Ltd, 2012). The way to decide whether or not trivial discrepancies exist depends on a case-to-case analysis, and it is not difficult to establish a generalized standard.

A reasonable operation in judging the complying presentation could be worked out through an appreciation of the significance and practical role of the documents requested in the documentary credit and terms under the ISBP, and the significance of data with respect to other data in that and other documents. Such an operation should be considered when examination, documents required by the documentary credit reflect the terms and conditions of the underlying contract. And it is clear that triviality of the defect must be decided from the document alone.

V. Conclusion

Lately, some courts have shown willingness

14) In decision of this case, the court maintained that “One should not accept a strict compliance argument in respect to the conformity of documents with letters of credit, as this constitutes splitting hairs over insignificant details, which reflects failure to act in good faith.”

15) This new trend has placed the burden of discretion on the bank in order to determine whether there is room for flexibility. These rulings have been criticized by Israeli bankers working in the field, as well as lawyers, who have argued that this type of discretion was never intended to be the task of the bank.
to make a payment when the discrepancy in a set of documents could be admitted as trivial or minor.

With regard to the examination of documents presented, the UCP itself shows a more flexible approach. Through the definition provided in UCP 600 Art. 2, complying presentation should be made in accordance with ISBP, indicating the treatment of misspellings or typing errors (ISBP 745, A23) (Soh, 2014).16

UCP 600 widened the scope so that standard banking practice is now apart of the test of compliance. Also, UCP 600 Art. 14(d) and (e), respectively, seem to take a flexible approach where Sub-art. (d) states “data in a document———need not be identical to, but must not conflict with———” and Sub-art (e) defines “……the description of the goods, services or performance, if stated, may be in general terms not conflicting with this description in the credit.” The ICC admitted that over the years, the approach by banks to documents that may be deemed to be inconsistent with one another has been proved, in many cases, to be subject to misuse due to a misinterpretation of the rule (ICC, 2007). The high rate of discrepancies in documentary credit is clearly a matter for concern, since it weakens the position of sellers, and gives too much decision-making power to buyers. According to ICC Global Trade Finance Survey 2014, the trend in documents refused indicated as light downward flow in refusal rate of documents on first presentation from 46% in 2012 to 33.96% in 2013 (ICC, 2014).

The standard for determining whether discrepancies exist is required to promote certainty, and to maximize predictability and sustainability for D/C transactions.

There is no definitive solution to establish the new standard for examination of documents other than vigilance in the issuance of the D/C and the preparation of documents. The environmental changes in commercial transactions, which need time from the conclusion of the contract to the making of a payment, would affect the function of the D/C and the operation of the compliance rule. Where the banks uphold strong compliance standards and regulations, they would minimize their own risk whereas traders would seek out alternatives in making payment to avoid inefficiencies of the commercial letter of credit.

It is not an easy matter to unify the different approaches and to arrive at the perfect solution concerning the compliance doctrine. The best solution would be one in which the issuing bank, the applicant and the beneficiary are all protected. Furthermore, it is clear that the examiner should consider the developing standardized approach, terminology, and technology that would minimize any negative consequences on trade finance business (ICC, 2014). The principle of strict compliance is still a little uncertain about what the required standard of compliance is regarding documents and the matter of a proper interpretation.

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