



CLIENT GUIDE TO TRADE FINANCE DISPUTES: LETTERS OF CREDIT

Letters of credit (LCs) are one of the oldest most common types of short-term trade finance, famously described by the English courts as the “lifblood of international commerce”. This guide outlines the key features of LCs, highlights legal and practical risks under English law and identifies areas where disputes can arise.

What is an LC?

An LC is a contract by which a bank agrees to pay the beneficiary upon the happening of a specific event or in connection with the export of specific goods, against the presentation of specified documents. LCs offer security of payment and receipt of goods for contractual counterparties who may be in different jurisdictions to each other – and who may be contracting to buy and sell goods which are located in a third jurisdiction, or which are in transit. They are standalone contracts, separate from the sale contract and under the autonomy principle, banks are concerned only with the LC contract, not the sale contract.¹ A feature common to all types of LCs is that money is raised on the documents, not on delivery of the goods.²

UCP 600 – What are they and why do they matter?

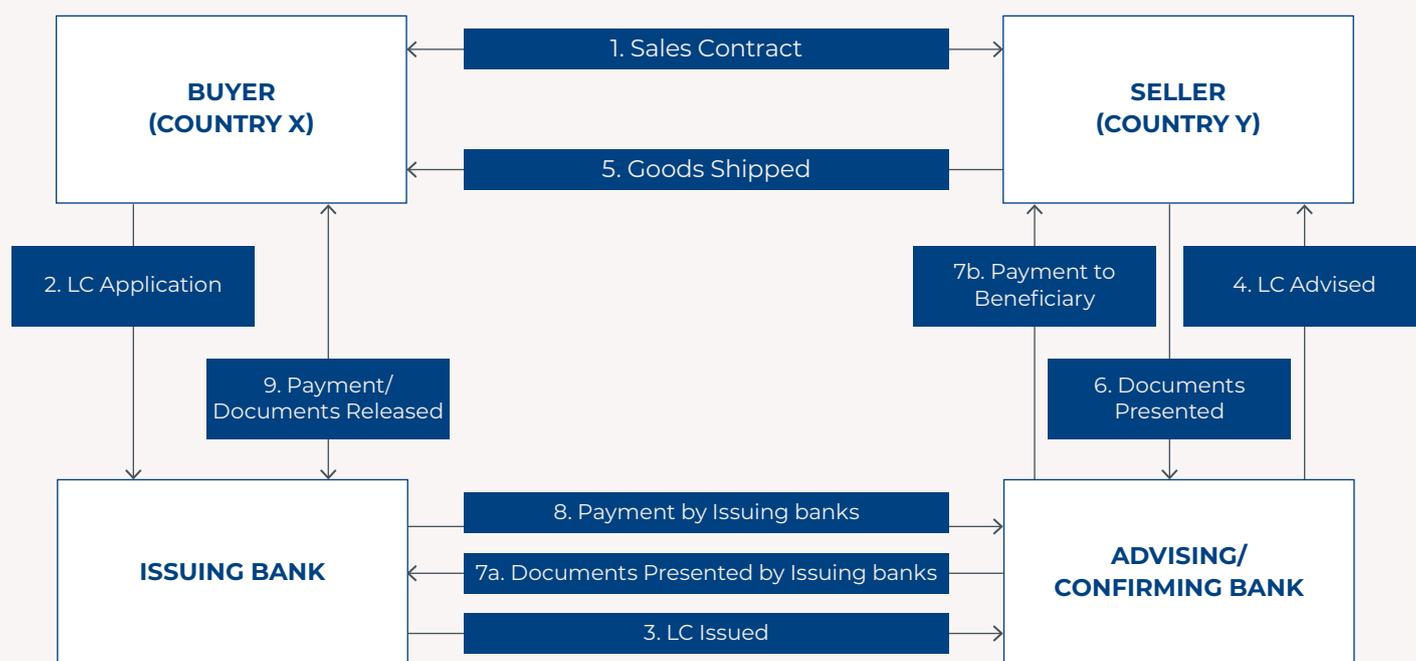
The Uniform Customs and Practice for Documentary Credits (“UCP”) 600 are international rules published by the International Chamber of Commerce (ICC) with the aim of standardising international banking practice in relation to LCs. The UCP 600 are only applicable if they are expressly incorporated (and there is provision for including them at field 40E in the SWIFT MT700). However, although a voluntary code, the majority of LCs are governed by the UCP 600. They are trans-national in application and set out detailed requirements which govern the scope of a bank’s obligations and which reflect universal custom and practice. It is possible to amend their application to an LC by modification or exclusion.

As the majority of LC transactions are governed by the UCP 600, all parties know what to expect and how to deal with problems when they arise. The fact that the UCP 600 have not been updated since July 2007 suggests that the market is comfortable with them and that they are operating effectively. A supplement, the eUCP, was introduced in 2019 to deal with electronic transactions.

¹ (Article 4 UCP 600).

² (Article 5 UCP 600).

Structure of a Typical Documentary LC Transaction



What does a typical LC transaction look like?

1. Seller and Buyer agree sales contract – with payment to be made by LC.
2. Buyer requests Issuing Bank to issue the LC – this is the Bank’s own irrevocable undertaking to pay the Beneficiary on compliance with conditions. Buyer agrees to indemnify Bank and gives pledge over documents.
3. LC issued and sent to Seller’s local bank (known as Advising Bank).
4. Advising Bank examines LC and informs Seller (and adds own undertaking if it is also Confirming Bank).
5. Seller ships goods to Buyer.
6. Seller presents documents under LC to Advising Bank (also called Nominated Bank if nominated as paying bank).
7. (a&b) Documents are checked. If they are in order, payment is made and documents are forwarded to Issuing Bank.
8. Documents are checked and reimbursement is made to Confirming Bank.
9. Documents are released against payment from Buyer (or other arrangements).
10. Buyer uses documents to obtain possession of goods.

Different Types of LC

- **Documentary** – an obligation by the issuing bank to pay the agreed amount to the beneficiary (usually the seller) on behalf of the applicant (buyer) upon receipt of the specified documents.
- **Standby** – this operates more like a demand guarantee. It is a secondary rather than a primary obligation to pay³, usually triggered by non-performance. It does not have to be issued by a bank. The issuer undertakes to pay in the event of default by the applicant and presentation of conforming documents by the beneficiary.
- **Irrevocable/revocable** – A revocable LC can be changed or cancelled by the issuing bank at any time and for any reason. An irrevocable LC offers more security as it cannot be changed or cancelled unless all parties agree.
- **Transferable** – this is an LC with an added provision permitting the bank to transfer the sum specified by the LC to another party at the request of the original beneficiary.
- **Back-to-back** – two LCs, one issued by the buyer’s bank to an intermediary and the next issued by the intermediary’s bank to the seller, usually to conceal the ultimate seller’s identity from the ultimate buyer.
- **Revolving** – a single LC which can cover multiple shipments, so the credit can be renewed either as to the amount or as to the time it is available. These are often used where regular shipments are made from the same seller over a period of time.
- **Sight Credit or Usance Credit** – generally LCs are paid “at sight” of the compliant documents by the bank. A usance credit is not paid at sight but at a future date.

³ For more information on guarantees, primary and secondary obligations to pay, see our client guide [here](#).

- **Confirmed L/C and Silent Confirmed L/C** – Confirmation is usually requested if the seller is concerned about the creditworthiness of the issuing bank and/or the buyer's country risk. The advising bank adds its confirmation to the LC at the issuing bank's request. The advising bank then becomes the confirming bank and undertakes to pay the beneficiary if the LC is complied with (this is a separate undertaking from the one given by the issuing bank and so offers extra security to the seller). Silent confirmation happens when the seller, not the issuing bank, requests confirmation, which is not disclosed to the other parties in the transaction.

Requirements for documents presented under an LC

Conformity and timing are the key issues here. All documents required under an LC must be submitted in time and must be conforming in order to trigger payment. A bank must decide, on the basis of the documents alone, whether the documents appear on their face to be compliant⁴. A complying presentation is one that meets the requirements of the credit and the applicable provisions of the UCP 600 and international standard banking practice⁵. The bank has a maximum of 5 banking days following the day of presentation to determine if a presentation is compliant⁶. The UCP600 imposes a doctrine of strict compliance – the documents must comply – there is no “de minimis” rule.

Documents which comply in all respects will trigger payment under the LC. If the advising bank accepts non-conforming documents it may not be reimbursed by the issuing bank.

UCP 600 Article 16 deals with discrepant documents, waiver and notice. Where documents do not comply, the bank may:

- Refuse to honour the credit.
- In its sole discretion, approach the applicant for waiver of the discrepancies.

If the bank refuses to honour the credit, it must give a notice stating this and listing each discrepancy. It must state: – that the bank is holding the documents pending further instructions from the presenter; or – that the bank is holding the documents pending a waiver from the applicant; or – that the bank is returning the documents; or – that the bank is acting in accordance with instructions previously received from the presenter.

If an issuing or confirming bank fails to follow this procedure, it will be prevented from claiming that the documents presented are not compliant. Notwithstanding the doctrine of strict compliance, courts will ignore trivial defects. What constitutes a “trivial” defect is not straightforward, however: for example, it has been held to include listing a buyer's telex number with one digit incorrect **but not** omission of an ampersand (“&”) or the word “and” from the name of a company.

Key legal issues to note – where can disputes arise?

The key advantages of using LCs, for both seller and buyer, are security and familiarity. Choosing English law and jurisdiction to govern an LC enhances these advantages because the English court system is widely regarded as reliable, efficient and commercially aware when resolving disputes, with law based on precedent offering users certainty of outcome.

Nevertheless disputes do arise, usually where the issuing bank refuses to pay out under an LC. Common reasons for resisting payment include document discrepancy, fraud or illegality and more recently, the impact of sanctions. Disputes also arise over jurisdictional issues, because the parties involved are typically located in different jurisdictions, or because the LC does not contain an express jurisdiction or governing law clause.

We have also seen situations where the security of an LC arrangement can come under pressure in circumstances a buyer has a strong relationship with the issuing bank and seeks to influence whether the bank honours the LC. This can occur particularly in circumstances where prices fall and the underlying sale contract is no longer appealing to the buyer. However, such scenarios are rare, especially as most reputable banks are keen to maintain their independence and standing within the market.

Example cases

Jurisdiction (1): choice of law and jurisdiction

A case heard by the English Court in 2024⁷ is a good example of the benefit of including both express choice of law and jurisdiction clauses – in favour of English law and the English courts – in LCs. Macquarie had agreed to purchase three cargoes of coal from a company, P. It made advance payments for the goods and obtained security by way of two standby LCs from the defendant Swiss bank, Banque Cantonale Vaudoise (BCV). The LCs were governed by English law but did not contain a jurisdiction clause.

When the goods were not delivered, Macquarie claimed under the standby LCs but BCV did not pay, despite there being no identifiable discrepancies in the underlying documents. Initially Macquarie had to commence proceedings against BCV in Switzerland, in which BCV claimed there had been a fraud by “an unknown person” and the contracts P had given them in order to obtain the LCs were fraudulent. The Swiss proceedings were then stayed.

Macquarie was then able to commence proceedings in the English Courts. BCV issued a jurisdictional challenge but the English Court agreed with Macquarie that it was the most appropriate forum for determining whether BCV was liable to pay out under the LCs. It also pointed out that under English law (the governing law of the LCs), “*the substantive characteristics of a letter of credit have important procedural implications, which are*

⁴ (Article 14(a) UCP600)

⁵ (Article 2 UCP 600)

⁶ (Article 14(b) UCP 600)

⁷ Macquarie Bank Ltd v Banque Cantonale Vaudoise [2024] EWHC 114 (Comm).

intended to prevent the payee's substantive rights being circumvented by procedural means." For example, BCV was required to show established and obvious fraud in order to resist payment and had not done so.

Here, Macquarie was able to claim the benefit of English law's sensible, commercial approach to the parties' rights under LCs. However, had the LCs contained express jurisdiction clauses in favour of the English Courts, considerable time and costs would have been saved.

Jurisdiction (2): enforcement

Issues of jurisdiction can arise particularly in relation to enforcement. One such case arose from the enforcement of an arbitration award, in which HFW acted for the successful claimant.⁸ The UK Supreme Court held (among other things) that a debt arising under an LC is located in the place where the debtor (here, the issuing bank, based in London) is located, not the place where payment was to be made (here, New York).

Sanctions/Autonomy

Since the increase in sanctions against Russian entities following Russia's invasion of Ukraine in 2022, a number of sanctions related claims have come before the English courts. One such case relates to LCs⁹ and has been heard by the UK Supreme Court in December 2025. The central issue is whether the payment obligation of a confirming bank under LCs was suspended by the operation of sanctions introduced against Russia in March 2022. It has placed the autonomy principle, which is central to the security offered by LCs, under scrutiny.

The claimants were beneficiaries under the LCs, which served as security for the payment obligations of certain Russian companies under a series of aircraft leases. The LCs had been issued by a Russian bank and confirmed by UniCredit Bank. Following the Russian invasion of Ukraine, the lessors terminated the leases and served payment demands on UniCredit. UniCredit declined to pay on the basis that it was prohibited from doing so, mainly as a result of Reg. 28(3)(c) of the Russia (Sanctions) (EU Exit) Regulations 2019. This prohibits the provision of financial services or funds in pursuance of or in connection with an arrangement whose object or effect is directly or indirectly making restricted goods or technology available to a person connected with Russia, or for use in Russia.

At first instance, the Court found against UniCredit, holding that payment under the LCs would not be "*in connection with*" the underlying leases and relying on the fact that the aircraft had been supplied before the imposition of sanctions and on the autonomy principle. UniCredit appealed and the Court of Appeal found in its favour. It held that the judge had failed properly to engage with the wide words "*in connection with*" in Reg.28(3)(c) which meant that payment would be in connection with the underlying leases, regardless of the autonomy principle or the timing of the sanctions. For

more information, see our briefing [here](#). This judgment was itself appealed and it now falls to the UK Supreme Court to decide.

Interpretation of the UCP 600

It is rare to come across a case in which the interpretation of the UCP 600 is debated, but HFW acted for the successful defendant in proceedings in 2017.¹⁰ The claimant, Deutsche Bank had acted as the confirming bank under LCs issued by the defendant, CIMB Bank Berhad. Deutsche was presented with conforming documents by the beneficiary and paid out under the LCs.

A dispute arose because Deutsche argued that having made payment to the beneficiary and having passed what it alleged to be compliant documents to CIMB, it was entitled to reimbursement from CIMB. CIMB disagreed. The issue between them related to the interpretation of Article 7(c) of the UCP 600, which states: "*An issuing bank undertakes to reimburse a nominated bank that has honoured or negotiated a complying presentation and forwarded the documents to the issuing bank [...] An issuing bank's undertaking to reimburse a nominated bank is independent of the issuing bank's undertaking to the beneficiary.*"

CIMB made a formal Request for Further Information as to whether payment had actually been made and Deutsche refused to comply, on the basis that an issuing bank must accept on its face a statement from a confirming bank that it has paid the beneficiary – there is no entitlement to enquire whether a confirming bank has actually made payment before reimbursing it. It argued that CIMB's undertaking to reimburse Deutsche arose once Deutsche had sent CIMB the allegedly conforming documents and stated that it had paid the beneficiary. CIMB, on the other hand, argued that its undertaking was contingent on Deutsche having actually made payment to the beneficiary.

The Court found in favour of CIMB. It agreed that whether the presentation of documents has been honoured by payment is a relevant matter for investigation. Whilst it is unlikely that an issuing bank would have cause to question a confirming or negotiating bank's assertion that it has honoured presentations under LCs, this decision gives them scope to do so if they find it necessary. It may prove useful where standby LCs are being used as a form of security and where it is often difficult for issuing banks to resist demands for reimbursement from confirming banks.

HFW Comment

LCs remain a critical instrument in trade finance, offering parties security and familiarity, particularly where they are governed by English law. To date, the consistency and commerciality of the English courts have provided parties with some reassurance and certainty as to the likely outcome should a dispute arise. For example, they have shown themselves reluctant to depart from the principle that if a compliant demand

⁸ Taurus Petroleum Limited v State Oil Marketing Company of the Ministry of Oil, Republic of Iraq [2017] UKSC 64.

⁹ Celestial Aviation Services v UniCredit [2024] EWCA Civ 628.

¹⁰ Deutsche Bank AG v CIMB Bank Berhad [2017] EWHC 81 (Comm), EWHC 1264 (Comm) and EWHC 3380 (Comm).

is made under a standby LC, the issuing bank must pay, with the only very limited exceptions being fraud and illegality. They have also been seen as fierce upholders of the principle of autonomy. However, the decision in *Celestial Aviation* places some doubt on this. It will be interesting to see how the Supreme Court decides the appeal.

HFW has acted in a number of high-profile disputes involving LCs and continues to advise clients on a regular basis.

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