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A Study on Reimbursement Mechanism and the use for Exporters*

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I. Introduction

In letter of credit arrangements, the reimbursing bank is the bank that serves as a source of funds payment to the beneficiary. Upon presentation of credit conforming documents nominated bank would need to pay the beneficiary and claim reimbursement from reimbursing bank or issuing bank.

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Upon stipulating a reimbursing bank (which is different from the issuing bank in the letter of credit), previous arrangements are made to reimburse the nominated/confirming bank. If documents are considered conform by the nominated/confirming bank a reimbursement claim will be presented to the reimbursing bank. Reimbursing banks have a reasonable time, not to exceed three banking days following the day of receipt of the reimbursement claim, to process claims.

If no reimbursing bank has been indicated, the nominated bank will have to wait until issuing bank pays the documentary remittance. Considering 2 days posting¹⁾ time of the documents and issuing bank's 5 working day document examining time, the payment can be delayed about 10 calendar days. The sooner the claiming bank (being nominated bank) can receive the money, the sooner beneficiary will be paid.

Unlike domestic transaction, the exporters and importers enter into contract for some amount in the currency in a third country. In letter of credit (LC) transaction, the LC currency is mostly is denominated in USD (United States Dollars) which is most convenient for international trade parties including Korean traders and banks, followed by EUR(Euro Currency), JPY(Japanese Yen), GBP(Great British Pound) and so on. A nominated bank (being claiming bank) under LC) may be asked to reimburse itself by drawing on the issuing bank's account with a bank in, say, New York²⁾. In such a case the bank in New York is known as the 'reimbursing bank'. The party that issues the instruction to the reimbursing bank is the issuing bank which originates the reimbursement processing'.

1) By courier services such as DHL and TNT, EMS(Korea'soverseasexpress)

2) New York is home land for USD denoted reimbursement. All Korean banks maintain USD account with one or more banks located in New York which are mostly USA banks. In addition r several Korean banks maintain USD reimbursement account with foreign banks in Hong Kong or Singapore as back up and/or for time sensitive cases as those areas are in about 1 hour time gap.

Many exporters want to get export proceeds as soon as possible but they are not aware of reimbursement processing which can give a handsome cost saving as well as safe fund obtainment whilst they appreciate the benefit of LC which is an issuing bank's payment undertaking toward the beneficiary. Also I understand that there has been little research activities in Korea regarding reimbursement in respective of exporter's benefit. Therefore this paper is aimed to let the Korean exporters and their banks utilize the reimbursement system to their ends.

II. Advantage of Letter of Credit to Exporter

1. Operations of Letters of Credit

The letter of credit is in principle a simple device. Typically, the exporter of goods to a foreign importer will ask for its use as the method of payment. The importer is required to engage a bank in his own country to promise, without right of revocation, to honor drafts drawn by the exporter, within a set time, up to a stipulated amount. In banking parlance the importer is the "customer," the bank promising to honor drafts is the "issuing bank," and the exporter is the "beneficiary."

As a rule the issuing bank will issue letter of credit through a branch or correspondent bank in beneficiary's country to notify him. Frequently the correspondent bank will engage to honor or negotiate on behalf of the issuing bank without committing itself to any liability to the beneficiary. Or sometimes the notifying branch or correspondent will be asked to "confirm" the credit. It is then understood that the correspondent bank is accepting an additional and independent liability to honor the drafts or documents presented by the beneficiary.

In the “documentary” credit, the beneficiary must surrender required documents which describe and give control of the goods to the holder in order to receive payment or acceptance of the drafts. Documents most often required are commercial invoices, bills of lading, consular invoices, and marine insurance papers. By contrast, in the “clean” credit, beneficiary need present no documents with the draft. A credit may combine both the “clean” and “documentary” forms by allowing beneficiary to draw a part of the total amount without surrender of documents. Most transactions, however, call for the documentary type.

Letters of credit usually permit the beneficiary to negotiate drafts, accompanied by required documents, to nominated bank. Hence, the beneficiary will often discount drafts with a local bank or with a notifying correspondent bank not specifically obligated to honor drafts under the terms of the credit. To receive payment or acceptance on a documentary credit, the third party will still have to present necessary documents along with the drafts. Previously when a LC specify deferred payment, it was hard for the beneficiary to get advance from deferred payment undertaking bank because of English Court's surprising decision³⁾. But UCP600 now resolves problems that have lingered in prior UCP versions resulting from the failure to explain the implications of a deferred payment undertaking and acceptance. UCP600 clarifies that a nomination inherently authorizes a bank to discount its own or another bank's obligation by prepaying (and thereby extinguishing) or purchasing it. In such a situation, UCP600⁴⁾ makes it clear that the nominated

3) *Banco Santander SA v. Banque Paribas*, [2000] C.L.C. 906 (C.A.) (court ruled that issuer did not have to Reimburse confirming bank that discounted because UCP500 does not authorize discounting of deferred payment obligations, and legal protection for discounting of acceptances does not apply to deferred payment obligations.

4) UCP600 Article 12(b) (Nomination) :

a. Unless a nominated bank is the confirming bank, an authorization to honour or negotiate does not impose any obligation on that nominated bank to honour or

bank is entitled to be reimbursed notwithstanding beneficiary letter of credit fraud.

2. Letter of Credit Financing for beneficiary

The letter of credit offers advantages to both exporter and importer. First, the exporter of goods has the primary promise of a bank, rather than merely his importer, that he will be paid. Consequently, he is able to enter markets where the risk of dealing with an unknown importer would otherwise be too great. Secondly, by negotiating his drafts/shipping documents, the exporter obtains payment immediately upon shipment, freeing capital for other transactions. Finally, he may use a letter of credit as means of securing advances to finance his end of the transaction. Thus, the exporter, in effect, often uses the importer's line of credit to finance a transaction from which both will profit⁵⁾.

The importer also benefits from use of the documentary letter of credit. As a means of financing his venture the credit is cheap and efficient⁶⁾. The issuing bank extends the credit cheaply, in part, because the obligation of the

negotiate, except when expressly agreed to by that nominated bank and so communicated to the beneficiary.

- b. By nominating a bank to accept a draft or incur a deferred payment undertaking, an issuing bank authorizes that nominated bank to prepay or purchase a draft accepted or a deferred payment undertaking incurred by that nominated bank.
 - c. Receipt or examination and forwarding of documents by a nominated bank that is not a confirming bank does not make that nominated bank liable to honour or negotiate, nor does it constitute honour or negotiation.
- 5) It is the general conclusion that no alternative to letters of credit offers to the exporter the combination of assured payment, no credit strain, and immediate payment upon shipment
 - 6) Bank fees for opening the letter of credit are normally quoted at 0.05~0.2% per quarter depending among other factors, on (1) the credit standing of the importer; (2) the nature of the bank's duties—whether typical or requiring additional functions; (3) the nature of the trade; (4) distances and countries involved; (5) the duration of the credit; (6) the amount of credit.

importer is at all times secured. Once the beneficiary or any presenter of drafts has turned over required shipping documents to the issuing bank, the latter continues to hold title to the goods until their arrival at the port of destination. Depending on the arrangement between importer and issuing bank, the goods may then be either turned over to the importer upon immediate payment, or given to him for resale against a trust receipt with the issuing bank retaining legal title until the goods are sold. Thus, unless the issuing bank requires additional security, the importer also has the advantage of having his free working capital

III. Frame Work of Reimbursement

1. Importance of reimbursement clause in LC

If the credit is available with the nominated bank, there must be a reimbursement instruction⁷⁾ in the credit, because in this method of availability the issuing bank is obliged to reimburse the nominated bank if that bank acts on its nomination⁸⁾. The reimbursement method (by claiming via SWIFT⁹⁾ or telex from the issuing bank or from a designated reimbursing bank would

7) The instruction given by the issuing bank constitutes the reimbursing bank's mandate. Technically, it is known as a 'reimbursement authorization'. The reimbursement authorization must spell out all the required details and, further, must be clear and unambiguous. .

8) The provisions regarding the reimbursement obligation of the Issuing Bank are found in UCP600 Article 7(c) (Issuing Bank Undertaking : 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. Reimbursement for the amount of a complying presentation under a credit available by acceptance or deferred payment is due at maturity, whether or not the nominated bank prepaid or purchased before maturity. An issuing bank's undertaking to reimburse a nominated bank is independent of the issuing bank's undertaking to the beneficiary.)

9) SWIFT Field 53

ensure a good cash flow for the beneficiary. If the credit does not include a reimbursement clause, the nominated bank should ask for such a clause upon receipt of the credit. Otherwise, i.e., if the nominated bank does not act on its nomination, then it will have to wait for the issuing bank's remittance of funds or its authority to claim payment from the designated reimbursing bank.

If a negotiating bank notices discrepancies in the documents and finds that they cannot be rectified by the beneficiary, the bank may then decide to negotiate the documents by taking an indemnity from the beneficiary. The bank then deducts the discrepancy fee¹⁰⁾ (stipulated by the issuing bank) and claims the balance from the reimbursing bank.

On the other hand, if the negotiating bank had not noticed any discrepancies, it may negotiate the documents and pay the beneficiary. It will not deduct any discrepancy fee but claim the full amount of the drawing from the reimbursing bank and forward the documents to the issuing bank.

When the issuing bank receives these documents and detects discrepancies, it would likely refer them to the applicant for a waiver. If the discrepancies are waived by the applicant, the issuing bank can only recover the discrepancy fee from the negotiating bank by making a separate claim. Sometimes, this claim is ignored and not even acknowledged by the negotiating bank. The issuing bank will then send reminders, and, if no response is received from the negotiating bank, the issuing bank actually does not have meaningful method in getting the discrepancy fee.¹¹⁾

To overcome the problem, some issuing banks are changing their method of providing reimbursement instructions. Banks which were previously nominating a reimbursing bank – and authorizing that bank to make payment under their

10) The discrepancy fee also has some relevance to URR 725, Article 16 (a) : A reimbursing bank's charges are for the account of the issuing bank). The responsibility of the reimbursing bank is to reimburse a claiming bank the amount that has been authorized by the issuing bank

11) The issuing bank may send one or two reminders, and if no reply is received from the negotiating bank, the issuing bank mostly ignore the matter.

credits – are now providing reimbursement instructions stating that payment will be made upon receipt of documents in conformity with the terms and conditions of the credit. This is to enable the issuing bank to deduct the discrepancy fee from the amount of the drawings when it makes payment¹²⁾. This also benefits the applicant in that he saves the interest from the date of reimbursed to the date of payment by the issuing bank.¹³⁾

2. Reimbursement Agreement

There are two sets of guidelines currently in effect. The first set is the Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits (URR), set by the ICC in 1995 and revised in 2008, which is URR 725. URR725 represents a comprehensive collection of the rules relating to bank –to– bank reimbursements. It states standard international practice regarding bank –to– bank reimbursements of payments under letters of credit. It focuses on the reimbursement authorization by the issuing bank and also provides for a "reimbursement undertaking" by which a nominated reimbursing bank makes an irrevocable commitment to honor a reimbursement claim by a claiming bank that is named in the reimbursement undertaking. URR725 is mentioned in the reimbursement rules of both UCP600¹⁴⁾ and ISP98.¹⁵⁾

12) "There is good income while it is considered that the objective is mainly to discourage discrepancies in documents. If the beneficiaries fails to be careful, they deserve to pay a fee for it

13) There is also a controversial that when the applicant waives the discrepancies, there is a discrepancy fee by the issuing bank

14) UCP600 (2007) Article 13(a) (Bank –to– Bank Reimbursement Arrangements) requires the credit to state whether the reimbursement is "subject to the ICC rules for bank–to– bank bank reimbursements … ."

15) ISP98 Rule 8.04 (Bank –to– Bank Reimbursement) provides "any instruction or authorization to obtain reimbursement from another bank is subject to the International Chamber of Commerce standard rules for bank –to– bank reimbursements

URR as Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits, its title reflects the prevalence of reimbursement instructions in documentary credit transactions.¹⁶⁾ URR governs the contract between the reimbursing bank and the issuing bank applying the autonomy principle, on the top of established autonomy principle in commercial letters of credit, in the instant case is that the reimbursing bank need not familiarize itself with the terms of the letter of credit.¹⁷⁾ The second is article 13(b)¹⁸⁾ of UCP 600. Under article 13(a),¹⁹⁾ the new provision applies if the letter of

16) URR725, art 1 : The Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits ("rules"), ICC Publication No. 725, shall apply to any bank-to-bank reimbursement when the text of the reimbursement authorization expressly indicates that it is subject to these rules. They are binding on all parties thereto, unless expressly modified or excluded by the reimbursement authorization. The issuing bank is responsible for indicating in the documentary credit ("credit") that reimbursement is subject to these rules.

17) Indeed, according to article 6(b) of the URR, the issuing bank must not send the reimbursing bank a copy of the letter of credit. It follows that the reimbursing bank's only concern is to carry out the actual instructions given to it by the issuing bank: Peter Ellinger, "the Law and Practice of Documentary Letters of Credit, Hart Publishing, London, 2010, p200,

18) UCP 600 art 13(b) : b. If a credit does not state that reimbursement is subject to the ICC rules for bank-to-bank reimbursements, the following apply: i. An issuing bank must provide a reimbursing bank with a reimbursement authorization that conforms with the availability stated in the credit. The reimbursement authorization should not be subject to an expiry date. ii. A claiming bank shall not be required to supply a reimbursing bank with a certificate of compliance with the terms and conditions of the credit. iii. An issuing bank will be responsible for any loss of interest, together with any expenses incurred, if reimbursement is not provided on first demand by a reimbursing bank in accordance with the terms and conditions of the credit. iv. A reimbursing bank's charges are for the account of the issuing bank. However, if the charges are for the account of the beneficiary, it is the responsibility of an issuing bank to so indicate in the credit and in the reimbursement authorization. If a reimbursing bank's charges are for the account of the beneficiary, they shall be deducted from the amount due to a claiming bank when reimbursement is made. If no reimbursement is made, the reimbursing bank's charges remain the obligation of the issuing bank.

19) UCP 600 art 13(a) : a. If a credit states that reimbursement is to be obtained by

credit does not state that reimbursement is to be subject to the URR.²⁰⁾

As to the relationship between applicant and issuing bank, the applicant and the issuing bank would enter into a letter of credit reimbursement agreement, under which the issuing bank is authorized or agrees to issue the letter of credit, and will issue the letter of credit on satisfaction of whatever conditions of issuance the bank specifies. The applicant agrees unconditionally to reimburse the issuing bank for payments made by the bank under its letter of credit. This means that the applicant for whose account the letter of credit is issued should evidence in an enforceable written agreement such applicant's unqualified obligation to reimburse the issuing bank for payments made under the letter of credit. Based on the issuing bank ensure other nominated bank to reimburse for their actions made on behalf of the issuing bank.

According to UCC, when an issuing bank or confirming bank honors a presentation, U.C.C. § 5-108(i)(1) [Rev] provides that it is entitled to reimbursement by immediately available funds. In the case of the issuing bank, it is the applicant who is obligated to reimburse.²¹⁾ This right to reimbursement obtains even if there is a claim of letter of credit fraud or forgery or even actual fraud or forgery provided that payment is permitted under U.C.C. § 5-109(a)(2).²²⁾

a nominated bank ("claiming bank") claiming on another party ("reimbursing bank"), the credit must state if the reimbursement is subject to the ICC rules for bank-to-bank reimbursements in effect on the date of issuance of the credit.

- 20) This new article replaces article 19 of UCP 500. In reality, the URR are, in themselves, an updated version of article 19. A cross reference in UCP 600 to the URR would have been adequate, especially if coupled with a provision subjecting letters of credit governed by UCP 600 to the URR. : Peter Ellinger, *ibid*, p199
- 21) Cases stating this general proposition: In re Mayan Networks Corp., 306 B.R. 295, 42 Bankr. Ct. Dec. (CRR) 196, 52 Collier Bankr. Cas. 2d (MB) 815, 53 U.C.C. Rep. Serv. 2d 105 (B.A.P. 9th Cir. 2004) (California Revised Article 5) (an issuing bank who has honored a presentation has the right to be immediately reimbursed by the applicant)
- 22) U.C.C. § 5-109(a)(2) [Rev] provides:
- (a) If a presentation is made that appears on its face strictly to comply with the terms

3. Reimbursement undertaking

A reimbursement undertaking is a bank-to-bank undertaking by the correspondent of the issuing bank of a letter of credit known as the reimbursing bank that irrevocably undertakes to honor a claim from a claiming bank that has acted under the terms of the credit. These arrangements arise in situations where the issuing bank does not have a correspondent relationship with a nominated bank. The issuing bank makes an irrevocable reimbursement authorization to the reimbursing bank that, designates the nominated bank as a claiming bank and authorizes the reimbursing bank to honor a reimbursement claim from the claiming bank. The undertakings of the reimbursing bank in its reimbursement undertaking and issuing bank in its reimbursement authorization (where a reimbursement undertaking is authorized) are irrevocable, documentary, definite, and independent from the credit or any preceding or underlying undertaking.

A reimbursement undertaking issued in accordance with Article 9 of URR 725 constitutes an irrevocable commitment from the reimbursing bank to effect payment to a claiming bank provided a claim is submitted in conformity with the terms of the reimbursement undertaking.²³⁾

The duty of a reimbursing bank that has issued its reimbursement undertaking is to effect settlement upon receipt of a valid reimbursement claim from the claiming bank. In the event of there being a dispute between the issuing bank and the negotiating bank with regard to the acceptability of the

and conditions of the letter of credit, but a required document is forged or materially fraudulent, or honor of the presentation would facilitate a material fraud by the beneficiary on the issuing bank or applicant:

(2) the issuing bank, acting in good faith, may honor or dishonor the presentation in any other case.

- 23) Article 9(Reimbursement Undertaking): a. In addition to the requirements of sub-articles 6 (a), (b) and (c) of these rules, a reimbursement authorization authorizing or requesting the issuance of a reimbursement undertaking must comply with the provisions of this article.

documents, this is a matter for resolution by those two banks without any involvement or action on the part of the reimbursing bank.²⁴⁾

IV. Cases

Below are 3 cases : one court case and the second one came from ICC Opinion where a beneficiary could avoid non-payment or late payment from the issuing bank owing to reimbursement clause in the letter of credit. The last one is to show bad practice often occurring in LC instruction regarding reimbursement.

1) Gulf International Bank B.S.C. vs Albaraka Islamic Bank B.S.C²⁵⁾

Reimbursing bank (Gulf International Bank B.S.C) sued Issuing bank and confirming bank (Albaraka Islamic Bank B.S.C) for recovery of reimbursement on an LC paid by mistake to Confirming bank.

(1) Factual Summary:

Issuing bank (Albaraka Islamic Bank B.S.C) maintained an account with reimbursing bank (Albaraka Islamic Bank B.S.C)'s New York branch. On the application of Solo Industries (being the applicant), the issuing bank issued a letter of credit in favor of English Beneficiary (Simetal, Ltd.), in the amount of US\$1,887,100 payable 180 days after negotiation, to be confirmed by confirming bank (Wachovia Bank NA)'s London branch. The confirming bank was authorized by the issuing bank to claim reimbursement from the issuing bank's USD account with reimbursing bank.

24) ICC Official Opinion R495 – 2000/01

25) [2004] EWCA Civ 416 (Feb), a reference to Documentary Credit World, Institute of International Banking Law and Practice, New York, 2005

Several days later, confirming bank accepted documents presented to it by Beneficiary, and advanced payment to beneficiary in the amount of USD1,821,215.31, and then forwarded the documents to the issuing bank. On receiving the documents, the issuing bank informed the confirming bank that the documents presented were in order with authorizing reimbursement at maturity from the reimbursing bank. At the same time the issuing bank authorized the reimbursing bank to reimburse the confirming bank..

A month later (before maturity), however, the issuing banks cancelled its reimbursement authorization and received acknowledgment from reimbursing bank that the authorization was cancelled. Right after the issuing bank informed the confirming bank that the LC was under investigation and it requested confirming bank to stop payment until further notice. However, the issuing bank did not withdraw the confirming bank's reimbursement right on the ground that the confirming bank already discounted the LC. Then the confirming bank sought repayment from reimbursing bank.

With this reimbursement request, the reimbursing bank paid confirming bank the requested amount in spite of the cancellation of the reimbursing authority, and debited issuing bank's account in that amount. When Issuing bank noticed the miss debiting, the reimbursing bank re-credited the amount to the issuing bank's account and sought a refund of the sum from confirming bank. But the confirming bank refused to return the money.

Mediation between the parties went but was unsuccessful. With this unhappy outcome, reimbursing bank brought an action against issuing bank and confirming bank to recover the amount paid. The trial court granted summary judgment in favor of issuing bank, but denied summary judgment to reimbursing bank.

On appeal, the court set aside the orders granting summary judgment to the issuing bank and affirmed the denial of summary judgment²⁶⁾ as to the dispute between reimbursing bank and confirming bank.

26) Simple judgment processing before a merit, in other words : default judgment

(2) Analysis

Reimbursing bank claimed that due to its mistaken payment to confirming bank it was entitled to recover the payment to confirming bank as a mistake of fact. Alternatively reimbursing bank claimed it was entitled to recover from issuing bank if it was not entitled to recover from confirming bank or if the payment to confirming bank discharged any liability of Issuing bank under the LC.

Confirming bank argued that it had accepted the payment from reimbursing bank in discharge of a debt by Issuing bank owed to it under the LC in good faith and without knowledge of reimbursing bank's mistake or issuing bank's revocation of reimbursing bank's authority to make payment. It argued that it was therefore not obligated to return the mistaken payment.

Issuing bank argued that it was not liable to Reimbursing bank because the payment was made without its authority and Reimbursing bank re-credited its account with the amount of the payment after Issuing bank protested that the initial debit on its account was unauthorized.

(3) Conclusion

The Appellate Court, in remanding the case for trial, reversed the summary judgment granted in favor of Issuing bank against Reimbursing bank and concluded that:

I do not think that Reimbursing bank's claim against [Issuing bank] can fairly be regarded as fanciful ----- For these reasons, I would allow the appeal and permit Reimbursing bank to proceed to trial to enable it to advance a claim against [Issuing bank] should its claim against [Confirming bank] fail

(1) Comments

According to the appellate court's decision, the reimbursing bank was accepted for their exercise of subrogation rights to the issuing bank lastly.

The confirmation bank was safe as they were not asked to stop reimbursement by the issuing bank. This gives a lesson that once the proceeds are reimbursed without offending the reimbursement rule, the ball falls in to the ground of issuing bank. And there might be a fight between the applicant and the issuing bank in interpretation of reimburse agreement between them.

On the other hand, the applicant, in balance, can exercise subrogation right in following case like : Nominated bank honors the presentation and passes the documents on to issuing bank Issuing bank finds the documents in order and reimburses the nominated bank . Applicant then reimburse the issuing bank. After the goods arrive, however, they are found to be rubbish. Since applicant paid Issuing bank, applicant claims to be subrogated to the rights of issuing bank against the nominated bank. Issuing bank will be required to honor nominated bank's presentation if the nominated bank paid in good faith.²⁷⁾ But the nominated bank was found not to pay the proceeds in good faith. Applicant is now subrogated to the issuing bank's rights against nominated bank and can recover whatever damages the issuing bank could recover.²⁸⁾

Case 2 : Unpublished query TA.388 – (Banking Commission meeting of May 2000)

27) UCC Section 5-109(a)(ii).

28) Allowing applicant to be subrogated to the rights of issuing bank against nominated bank is not inconsistent with the independence principle for several reasons. First, the subrogation occurred only after the letter of credit was honored. Second, subrogation allows the applicant to succeed only to the privy rights of Issuing bank against nominated bank. Subrogation does not allow applicant to sue nominated in tort. Subrogation of applicant importer to the rights of issuing bank only changes the name of the plaintiff but not the amount of damages to be claimed. Needless to say, no consequential or punitive damages would be recoverable in the subrogation suit. :Gerald T. McLaughlin, Exploring Boundaries : A Legal and Structural Analysis of the Independence Principle of Letter of Credit Law, Banking Law Journal June, 2002

(1) Factual Summary:

"Issuing bank issued a letter of credit and it was negotiated by a nominated bank in beneficiary's country. After the negotiation, the negotiating bank claimed reimbursement and received the funds from the reimbursing bank. However, the issuing bank did not receive the documents. A thorough investigation revealed that the documents were lost in transit.

With this documents missing, the issuing bank requested the negotiating bank to refund the funds, but they refused on the grounds of Article 16 of UCP 500.

(2) Analysis and conclusion

A negotiating bank is protected by the content of Article 16²⁹⁾ in the event that documents are lost in transit. And therefore the negotiating bank does not have to refund the money they received from the issuing bank.

(3) Comments

If LC provided³⁰⁾ that the issuing bank undertakes to pay the beneficiary upon receipt at its counters of conforming documents: "Upon receipt of full set of documents in conformity with the L/C terms, we will effect payment as per your instruction."³¹⁾ ; The issuing bank will investigate for some time in

29) Article 16 states: 'Banks assume no liability or responsibility for the consequences arising out of delay and/or loss in transit of any message(s), letter(s) or document(s), or for delay, mutilation or other error(s) arising in the tele-transmission of any telecommunication. Banks assume no liability or responsibility for errors in translation and/or interpretation of technical terms, and reserve the right to transmit Credit terms without translating them.

30) under SWIFT field 78 (Instruction to pay)

31) In some cases the issuing bank wishes to obtain an assurance that the reimbursing claim is made on the basis that the claiming bank has negotiated complying documents. To this end, the issuing bank may instruct that the reimbursement claim be accompanied by a certificate, or be backed by a statement, that the

case the documents are lost during the transit. And then the beneficiary probable get paid outside 5 banking days allowed for the issuing bank's document examination. This is because the issuing bank have no live documents in hands and may first exercises actions for the blocking of goods which are security for it.

Case 3 : Inappropriate usage of expression for reimbursement³²⁾

Below is cases where instructions as to reimbursement is often misled, a suggestion for remedy is followed by.

(1) L/C term: L/C available by negotiation with the Nominated Bank. T/T reimbursement is prohibited.

Suggestion: what might be the purpose of the Issuing bank's prohibiting T/T³³⁾ reimbursement? This is probably the issuing bank hopes to gain transit interest³⁴⁾ from the applicant who might not be aware of reimbursing mechanism. The issuing bank would ask transit interest though no debit from the issuing bank has been made. If the issuing bank want to earn actual transit interest, they shall allow reimbursement claim..

(2) Additional condition: "Payment under reserve or indemnity is not allowed."

claiming bank has received regular documents. Article 6(c) of the URR sets out to discourage the practice. Under it, the issuing bank 'shall not require a certificate of compliance with the terms and conditions of the credit in the reimbursement authorization'. A provision to the same effect is to be found in article 13(b) of UCP 600. : Peter Ellinger, *ibid*, p201

32) Documentary Credits Insight, Volume7 No.2 Spring 2001 refers

33) Telegraphic Transfer

34) Transit Interest : an interest (by the issuing bank) occurred for the period from the debit from issuing bank's account with reimbursing bank to repayment (settlement of import proceeds)from the applicant.

Suggestion : An issuing bank must not interfere with the action of Nominated Bank. Nominated Bank shall be free to pay under reserve or indemnity according to its relationship with the beneficiary. Therefore it is recommended that the issuing bank use following expression "claiming reimbursement from the reimbursing bank is not allowed in case payment under reserve or indemnity"

V. Conclusion

Though the portion of LC in Korea is relatively decreasing among other payment methods such as Open Account, the actual LC amount and transaction numbers are enlarging according to the nation's substantial increase of exports toward global market. This trend is expected to continue in the near future.

Korean exporters are very busy in getting orders and are very much pleased when they obtain LCs which ensure concrete payment. They attend on terms and conditions of LC so that they make right documents avoiding possible discrepancies from the issuing bank. They do not, however, treat well reimbursement clause in the LC. It seems they do not tell the actual difference between reimbursement claim from reimbursement bank and issuing bank's remittance after documents required are given to the issuing bank. Furthermore, the Korean bankers appear not aware of relationship among and between issuing bank, nominated bank and reimbursing bank.

I believe that the cases especially *Gulf International Bank vs Albaraka Bank* deliver meaningful message for the exporters as well as bankers. The Gulf case, being case 1, tells that the nominated bank could keep the proceeds (reimbursed LC amount) because the LC allowed reimbursement claim. Case 2 tells that the beneficiary did not have to wait the LC payment from the issuing bank, though the documents were missing during the transit, thanks to

the reimbursement claim instruction in the LC. Case 3 point out few bad practices of issuing bank and therefore the exporter and their banks shall ask amendments to the issuing bank for their safety

In conclusion, the Korean exporters are needed to obtain TT reimbursement LC as much as possible for finance cost saving and fund safety and further ask amendment when they see issuing bank's unclear reimbursement instruction. Korean bankers are also recommended to revisit legal point of reimbursement matters such as relationship amongst issuing bank, nominated bank and reimbursing bank.

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ABSTRACT

A Study on Reimbursement Mechanism and the use for Exporters

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In letter of credit arrangements, the issuing bank nominate a reimbursing bank which serves as a source of funds payment to the beneficiary. The reimbursing bank could be 3rd party bank or the issuing bank itself.

In view of working capital requirements, most beneficiary want to get export proceeds in advance through nominated banks and therefore letter of credit usually permit the beneficiary to negotiate drafts, accompanied by required documents, to nominated bank. If the credit is available with the nominated bank, there must be a reimbursement instruction in the credit, because in this method of availability the issuing bank is obliged to reimburse the nominated bank if that bank acts on its nomination

There are legal relationship among issuing bank, nominated bank and reimbursing bank with regard to reimbursement activities. Related rules are UCP and URR and UCC (in case of USA). Korean exporters and bankers do not appear to know well the role of reimbursement and usage. 3 cases (court case + ICC Opinion + bad practices) were employed to study the reimbursement mechanism and suggest better usages.

The beneficiary is strongly recommended to know the benefit of reimbursement claim from independent reimbursing bank. The benefits include speed payment (thereby saving finance costs) and safe funds (in case of stop payment by the issuing bank right after the proceeds are reimbursed). And further the beneficiary banks (being nominated or claim banks) are also recommended to take advantage of the 3rd party reimbursement in view of the cases illustrated.

Key words : Reimbursing Bank, Reimbursement Subrogation, URR