

# Transferable, confirmed sight documentary credit

## Parties and how it works

The documentary credit is both a flexible means of payment and an instrument for short-term financing.

The documentary credit is an irrevocable promise of payment by a bank. The bank promises the seller of goods or services to pay a certain amount if it submits compliant documents within the specified period.

The simplest transferable documentary credit transaction involves a supplier, a middleman and a buyer. To secure the transaction between the buyer and the middleman, a confirmed documentary credit in favor of the middleman with the note "transferable" is opened. The middleman can use this basic documentary credit to secure its transaction with the supplier. To this end, the middleman transfers it to the supplier. No additional credit limits are required for this purpose.

Documentary credits take different forms depending on the application, desired security and the method in which the payment is made.

### Criteria for application: transferable

A documentary credit designated as transferable may normally be transferred once. In the case of part deliveries, parts of the documentary credit can be transferred to several suppliers.

### Security criteria: confirmed

Two banks participating in the documentary credit assume a payment liability.

### Payment terms: at sight

The payment is made "at sight", i.e. immediately upon presentation of the relevant documents.

### Parties

There are normally six parties involved in a transferable documentary credit transaction:



#### Middleman

As the middleman, it acquires the export goods from the supplier and sells them to the buyer on its own account. It wants payment security from the buyer and delivery security from the supplier. It is the first beneficiary of the transferable, confirmed documentary credit and the principal for the transfer.



#### Buyer

It orders the basic documentary credit for the benefit of the middleman; it thus receives delivery security from the middleman.



#### Supplier

With the transfer of the basic documentary credit in its name, it secures the payment to which it is entitled from the middleman.



#### Buyer's bank

It issues the basic documentary credit and a promise of payment.



#### **Middleman's bank**

As the bank confirming the basic documentary credit, it is liable with respect to the middleman and as transferring bank to the supplier.



#### **Supplier's bank**

It examines and advises the transferred documentary credit.

### **How it works**

The procedure for a transferable, confirmed sight documentary credit for exports is set out below. The procedure is divided into two parts – opening of the documentary credit and its utilization.

#### **Opening of the documentary credit**

##### **1. Signing of contract by buyer/middleman**

A buyer in Japan and a middleman in Switzerland enter into an agreement for the delivery of cotton from Argentina.

As the means of payment, the parties conclude a transferable sight documentary credit that must be confirmed by the middleman's bank.

##### **2. Opening instruction for the basic documentary credit**

The buyer issues an instruction to its bank to open the documentary credit.

##### **3. Solvency check of the buyer**

The bank examines its client's creditworthiness, checks whether the order is complete and the apparent authenticity of the signatures on the order to open the documentary credit.

##### **4. Opening of the basic documentary credit**

The bank then opens the basic credit payment and transfers it (usually by SWIFT) to the middleman's bank – along with the instruction that the documentary credit be confirmed and advised to the middleman. The buyer receives a confirmation of execution.

##### **5. Examination of the basic documentary credit**

The middleman's bank examines the creditworthiness of the opening bank and the country risk as well as the apparent authenticity of the documentary credits and checks whether it is subject to the rules of the International Chamber of Commerce in Paris, is complete and whether it contains ambiguous instructions.

##### **6. Confirmation and advice of the basic documentary credit**

The bank now confirms and advises the documentary credit to its client. The middleman now knows that both its bank and that of the buyer accept liability for the payment.

##### **7. Examination of the basic documentary credit**

The middleman examines whether the documentary credit conditions are consistent with the purchase agreement. If not, it must request amendment by the buyer.

##### **8. Signing of contract by middleman/supplier**

The supplier in Argentina and the middleman in Switzerland sign a purchase agreement. They conclude a sight payment credit as the means of payment. The supplier agrees that the transferred documentary credit will not be confirmed.

### 9. Transfer instruction

The middleman now issues an instruction to its bank to transfer the basic documentary credit to the supplier. At the same time, the middleman amends certain conditions of the basic documentary credit in line with its agreement with the supplier – for example, it replaces its sale prices with its cost prices; the delivery, presentation and validity periods are also amended.

### 10. Transfer of the documentary credit

The middleman's bank sends the documentary credit balance by SWIFT to the supplier's bank and issues the order to the latter to issue a non-binding advice to its client as the secondary beneficiary. The middleman receives a confirmation of execution.

### 11. Examination of the transferred documentary credit

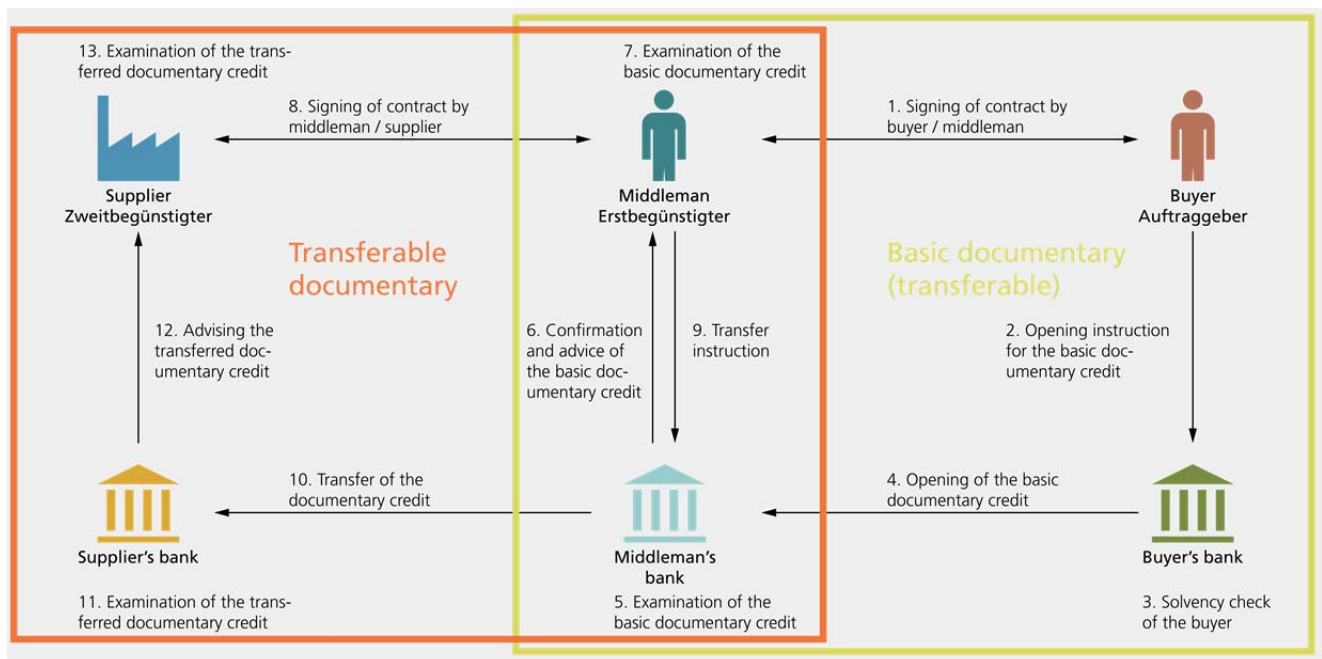
The supplier's bank examines the apparent authenticity of the documentary credit, checks whether it is subject to the rules of the International Chamber of Commerce in Paris and is complete and whether it contains ambiguous instructions.

### 12. Advising the transferred documentary credit

The bank now advises the transferred documentary credit to its client. The latter now knows that the transferring bank and the bank that opened the basic documentary credit are liable with respect to it for the payment.

### 13. Examination of the transferred documentary credit

The supplier examines whether the documentary credit conditions are consistent with the agreement between itself and the middleman. If not, it must request an amendment by the middleman.



## Utilization of the documentary credits

### 14. Delivery of goods

The supplier ships the cotton directly to the buyer.

### 15. Presentation of documents

The supplier then compiles the documents required by the documentary credit transferred to it and submits these to its bank.

### 16. Examination of documents

The bank examines whether the documents fulfill the conditions of the transferred documentary credit – if there are any discrepancies, the supplier loses its security of payment.

### 17. Request for payment and dispatch of documents

If the documents are compliant with the documentary credit, the supplier's bank sends the documents to the middleman's bank and requests payment of the document value.

### 18. Submission of middleman's invoice

The middleman's bank advises the receipt of the documents in relation to the transferred documentary credit to its client. It also requests the middleman to present its invoice and any bills of exchange. The middleman immediately complies with this request.

### 19. Examination of documents and exchange of invoices

The middleman's bank examines that its client's documents comply with the conditions of the documentary credit. If yes, it replaces the supplier's invoice and where applicable the bill of exchange with those of the middleman.

### 20. Request for payment and dispatch of documents

It then requests the buyer's bank for payment of the document, sends the documents to the buyer's bank ...

### 21. Cover

... and credits the requested amount to the supplier's bank.

### 22. Payment to the supplier

The bank pays the amount to its client after deducting its commissions and expenses.

### 23. Payment to the middleman

The middleman's bank credits its client the difference between the two invoice amounts less commissions and expenses. In addition, it presents to the middleman the supplier's invoice and bill of exchange.

### 24. Cover

The buyer's bank transfers the required amount to the middleman's bank ...

### 25. Debiting of the buyer's account

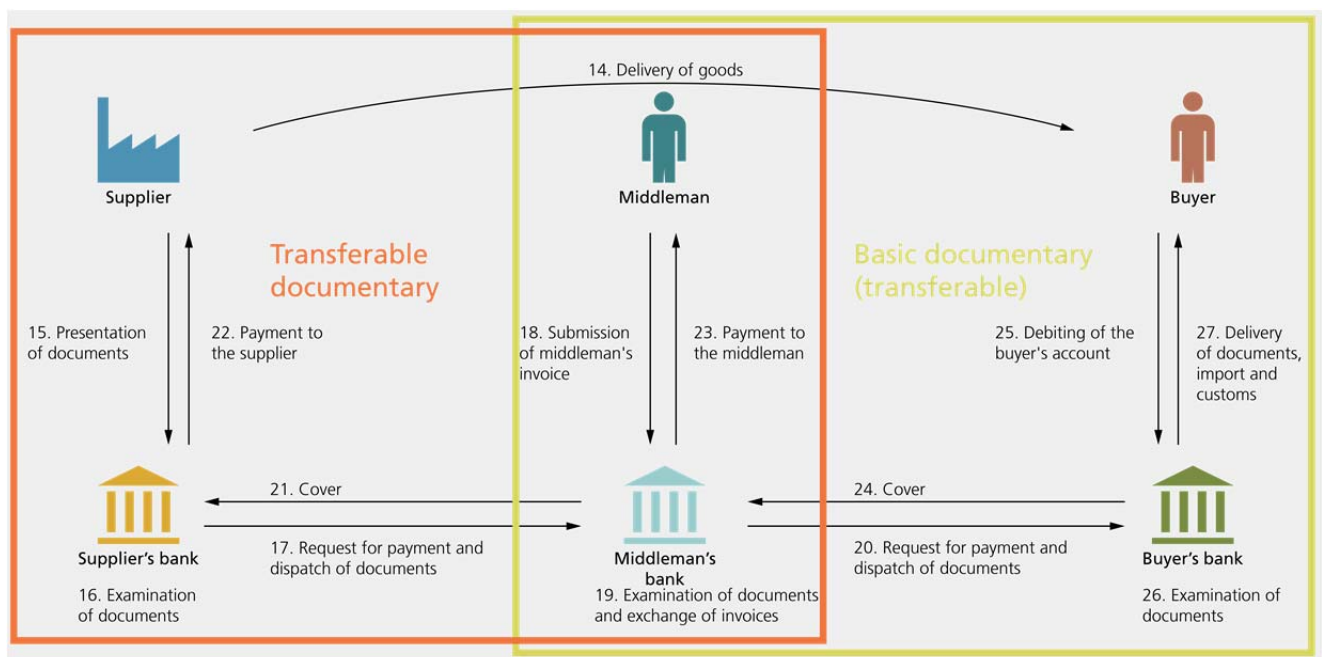
... and debits its client by the amount requested from the middleman's bank plus commissions and expenses for its obligations in relation to the documentary credit.

### 26. Examination of documents

It examines whether the documents received are consistent with the conditions of the documentary credit.

### 27. Delivery of documents, import and customs

If yes, it hands over the compliant documents to its client; the latter can now organize customs clearance and import the cotton.



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Trade & Export Finance  
P.O. Box, 8098 Zurich

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