NIBM-CDC-2025-23
December 2025

National Institute of Bank Management

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Ambiguity in Drafting Documentary Requirements in A Standby Letter of Credit: When Services have no Transport Document

Case Synopsis

This case delves into a complex dispute between an issuing bank and a confirming bank over a hybrid standby letter of credit (SBLC). This unique financial instrument serves to secure payment obligations that span both the delivery of physical goods and the completion of services, as stipulated in the contractual agreement between the applicant and the beneficiary. The conflict arose when the beneficiary initiated a drawing for services rendered, failing to provide a crucial transport document, bill of lading (BL) —a key document typically associated with the shipment of goods. Although the issuing bank has rejected the payment, citing the absence of a BL for services rendered, the confirming bank has raised a valid argument: for services, there is no possibility of issuing a BL, so rejecting the payment on this ground is not acceptable. Also, confirming bank suggested that asking for BL for services rendered is wrong on behalf of the issuing bank. This conflict between the issuing bank that has drafted the documentary requirements wrongly has raised significant questions about compliance with the SBLC terms and the responsibilities of both banks involved in the transaction.

The case examines the **doctrine of strict compliance**, the **interpretation of ambiguous documentary conditions**, and the implications of **poorly drafted credits** under **Uniform Customs & Practice for Documentary Credits – 600 (UCP-600)**. It may be noted that an SBLC can be opened under UCP 600 or the International Standby Practices – 98 (ISP-98). This case illustrates the pitfalls of poor drafting and its business implications in a comparative framework of UCP 600 and ISP -98 and suggests ways to mitigate documentary risks in trade finance operations.

Learning Objectives

After analyzing this case, students should be able to:

1. Explain the **nature and purpose** of standby letters of credit in trade finance.

2. Apply the **doctrine of strict compliance** under UCP 600 and ISP98 to documentary disputes.

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3. Identify and analyze the risks of **ambiguous drafting** in credit terms.

4. Evaluate the roles and responsibilities of **issuing** and **confirming banks**.

5. Recommend best practices for drafting clear and enforceable credit documentation.

Case Narrative

Universal Engineers Global LLC (UEG), an Engineering, Procurement and Construction (EPC) contractor, is engaged in the business of constructing infrastructure projects on a Build Operate and Transform (BOT) basis. They regularly bid for both private and public projects and have a presence in five states in India. The consolidated turnover of the company for 2024-25 was close to Rs 800 crore. The company has a positive cash flow and net worth.

Recently, they bid for a project to construct a new integrated manufacturing plant for P&T Corporation (P&T), a manufacturer of commercial vehicles in Dubai. The total project cost was USD 25 million and included the design and construction of a foundry, a machine shop, an assembly line, a paint shop, and other facilities. The project cost included both goods /materials and a service component.

The scope of construction work included:

- All design and engineering activities and services required to complete the work as per the terms of the contract.
- All construction activities and services as required to complete the work as per the contract.
- Procurement of all materials necessary to conduct and complete the work as per the contract.
- Hiring of all manpower, including skilled and unskilled labour, supervisors, testing, and other support services as required.
- The project cost and payment structure were based on the achievement of pre-decided project milestones.

P&T corporation, as part of the payment structure, provided a Standby letter of credit under UCP 600, from its banker, Reliable Bank Ltd, Dubai, for a value of USD 10 million representing payment for materials procured and supplied, design, labour, and construction activity, including both goods and services for the 1st stage of construction. Another bank, from the beneficiary country, SBI Mumbai, has confirmed this SBLC. This bank was chosen by the issuing bank to mitigate the country risk[3].

UEG was required to submit invoices with supporting documentation as needed, certifying the supply, installation, and construction in accordance with the scope of work. Upon receipt of the bill, P&T would make the payment within two working days, subject to UEG presenting the required documents as specified in the T&C of the SBLC.

In case the presentation remained unpaid for two working days, UEG could claim the amount by presenting a claim under the SBLC.

[3] It may be noted that a confirming bank is ideally located in the beneficiary country. But if the country rating of the beneficiary country itself is low, a confirming bank may be chosen by the issuing bank from a country having high country rating.

The SBLC was payable at sight and stated that any drawing under it must include:

1. A **draft**,
2. A **written declaration** from the beneficiary,
3. A **copy of the unpaid invoice**, and
4. A **copy of the transport document representing the value of the goods only**.

A few months into the arrangement, the beneficiary (UEG) submitted a **drawing under the credit** for USD 500,000, representing **services rendered but not paid for**. Since no physical goods were shipped in exchange for the service rendered, **no transport document existed**. The beneficiary presented the required draft, written declaration, and invoice, but not the transport document.

On receipt of the claim, Reliable Bank, the **issuing bank, refused payment**, citing the absence of a transport document as a discrepancy under the credit terms. The **confirming bank objected**, asserting that the transport document requirement applied only to claims involving goods and was not applicable to services.

This disagreement led to a dispute between the two banks. It raised a fundamental question about the **interpretation of the wording in SBLCs** and **documentary compliance** in standby letters of credit.

Conclusion

SBLCs can be issued either under the Uniform Customs and Practice for Documentary Credits (UCP 600) or under the International Standard Practices (ISP 98). These are a set of globally accepted rules established by the International Chamber of Commerce (ICC) to standardize trade practices and provide a stable framework for the seamless and dispute-free processing of trade transactions. Earlier, before ISP -98 has come in operation, SBLC were issued only under UCP (600). Later on, with the ISP-98, banks are allowed to issue SBLC either under UCP-600 or under ISP -98.

Under UCP 600, Article 14(a), banks are required to examine the documents presented “on their face” to ensure they comply with the terms of the credit. In a similar vein, ISP98 Rule 4.01 states that compliance is assessed solely based on the conformity of the documents. However, ISP98 Rule 4.03 and the commentaries on UCP 600 acknowledge that ambiguous terms should be interpreted reasonably and aligned with the overall commercial intent.

Discussion Questions

1. Should the issuing bank’s refusal be upheld under the doctrine of strict compliance? Why or why not?
2. How does the purpose of a standby letter of credit differ from that of a commercial documentary credit?
3. What drafting changes could have prevented this dispute?
4. If this case were governed by **ISP98** instead of **UCP 600**, would the outcome differ?
5. As a trade finance officer, what steps would you recommend to ensure clarity and enforceability in future credits?