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“Fraud and Mistakes in International Trade” – The Second Transfer Case

A deceptive LC transfer leads a confirming bank to pay twice. Explore this trade finance fraud case from Abdurrahman Özalp’s book on international trade.

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Over the course of his 35 years in banking, Abdurrahman Özalp has seen or heard of the good, the bad, and the bizarre that can occur in international trade.

In 2024, the trade finance consultant who currently serves as Chairman of the ICC Türkiye Banking Commission published “Fraud and Mistakes in International Trade”. In the first half of his 210-page eBook, Özalp discusses the proper channels to conduct international trade – valid methods of payment and security – with particular emphasis on the letter of credit process. Özalp then delves into the dark side of trade by presenting more than 50 case studies rife with an array of fraudulent tactics and outright mistakes.

The wide range of deceitful schemes and flawed practices he addresses includes instances involving collusion under a transferable LC, defective goods, notification of assignment, NVOCCs, careless bank actions, unclear collection instructions, misuse of draft LC text, unauthorized guarantee sent via SWIFT, letter of indemnity, and charter party bills of lading.

To give DCW readers an idea of the case studies gathered and examined by Özalp, consider the details that follow and the Second Transfer Case.

Applicant:	Company A
First Beneficiary:	Company B
Second Beneficiary:	Company C
Third Beneficiary:	Company D
Second Beneficiary's Bank:	S Bank (New Nominated Bank)
Issuing Bank:	I Bank
Nominated/Confirming Bank:	C Bank
Letter of Credit Amount:	USD 700,000 by payment

The Timeline

Upon instruction and application by Company A, a Letter of Credit for USD 700,000 is issued by I Bank in favor of Company B. The LC is confirmed, with a term of six months, expiring on 15 October 20xx by nominated/confirming bank (C Bank). Company B intends to transfer the LC to a second beneficiary, so it sends instructions to C Bank to transfer USD 650,000 of the LC to Company C through its bank (S Bank). Other details in the instruction include a new expiry date of 15 September 20xx and the new nominated bank, S Bank.

Upon the instruction of Company B, C Bank prepares an MT720 (transferred LC) and advises through S Bank with its confirmation by nominating S Bank in MT720. (S Bank is not the confirming bank but only the advising bank under the transferred Letter of Credit, i.e., MT720.)

No transaction occurs under the transferred LC for five months; nor does any shipment or presentation occur, and the transferred LC expires. One day after the expiry of the transferred letter of credit, Company B approaches C Bank and states that the LC is unused, has a maturity of about a month, and therefore wants to transfer it to a new customer. Indeed, since the first LC is for six months (15 October 20xx), there are 29 days remaining before it expires. C Bank checks its records, finds no utilization record, and determines that Company B is entitled to make such request. C Bank then acts on this instruction and transfers the LC to a third beneficiary (Company D) on 16 September 20xx for USD 650,000 with a new expiry date (10 October 20xx). C Bank calculates and determines that the LC has terminated since no submission or demand has been received.

Two days after the transfer (on 18 September 20xx), Company D ships the goods and presents documents to the C Bank on the same day. C Bank examines the documents, finds them compliant, and pays Company D on 23 September 20xx.

The Scheme

After two days (25 September 20xx), a reimbursement request from S Bank and complying documents presented by Company C are sent to and received by C Bank. C Bank is unable to understand and contacts S Bank, stating that the LC had been transferred to another beneficiary (i.e., Company D) and that Company D had been paid upon its compliant presentation due to C Bank not receiving a request within the due date (5 months) of the first transferred LC before it expired. Therefore, C Bank was not in a position to meet S Bank's reimbursement request.

S Bank then informed that Company C had presented documents on the last day of the transferred LC (that is, not on 15 September 20xx, i.e. expiry date of the transferred LC, but the next business day which was 21 September, explained as follows below). S Bank said it examined the documents, found them to be compliant, and paid on 24 September 20xx, which was reasonable according to UCP. Asked why documents were submitted on 21 September 20xx, instead of 15 September 20xx, S Bank said the reason was a combination of a four-day religious holiday and a two-day weekend, resulting in a six-day holiday. Since the last day of the LC fell within this six-day holiday, the last day for presentation of documents was extended to the next business day (21 September 20xx) after the holiday. Company C submitted its documents on this date (21 September 20xx) which complies with UCP 600 Article 29(a), as noted by S Bank on its cover sheet as per Article 29(b).

The relevant portions of UCP 600 Article 29 (Extension of Expiry Date or Last Day for Presentation) state:

> ***a.*** *If the expiry date of a credit or the last day for presentation falls on a day when the bank to which presentation is to be made is closed for reasons other than those referred to in article 36, the expiry date or the last day for presentation, as the case may be, will be extended to the first following banking day.*

> ***b.*** *If presentation is made on the first following banking day, a nominated bank must provide the issuing bank or confirming bank with a statement on its covering schedule that the presentation was made within the time limits extended in accordance with sub-article 29 (a).*

The Result: C Bank Pays Twice

S Bank repeated its request by stating that it is entitled to reimbursement as the authority to honor a compliant presentation was given by the C Bank when it was appointed as the nominated bank in the transferred credit (MT720). The party acting with this authority must be reimbursed by the confirming bank. C Bank reimbursed S Bank. Consequently, C Bank paid twice. It attempted to contact Company C to recover its initial payment, but was unsuccessful.

Since the error was its own mistake, C Bank cannot seek recourse from I Bank for both presentations, but only one and incurs loss due to the fraud. Company B was deceitful and, in collusion with Company C, orchestrated manipulation of the expiry date of the transferred letter of credit. Presentation was deliberately made on the last day of the transferred LC, misleading C Bank and enabling transfer of the same LC to another beneficiary, causing the bank to pay twice. C Bank’s mistake and failure are significant; it should not have proceeded with any further transfer without verifying whether a presentation had been made by S Bank to which it was transferred and nominated, and whether the balance of the transferred LC existed. The fraudster (Company B) exploited this blind spot of C Bank and defrauded it.

Read More

“Fraud and Mistakes in International Trade” by Abdurrahman Özalp is available through Google Books here.

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