DEFERRED PAYMENT LETTERS OF CREDIT

A deferred payment letter of credit (DPLC) is a credit which:
(1) calls for presentation of specified documents on or before a specified date;
(2) provides for payment to be made to the beneficiary a specified number of days or months after the presentation of documents, or after date of shipment, or other specified date; and
(3) usually does not call for drafts or other negotiable instruments to evidence the debt obligation of the parties involved.

Some countries have heavy stamp tax on bills of exchange and therefore resort more to DPLC as an alternative to usance credits.

Reasons for discouraging DPLC

When a deferred payment letter of credit is issued or confirmed, the bank exposes itself to a greater than normal risk and can become caught in a dispute between the buyer (account party) and the beneficiary. Upon acknowledgement of the correctness of the documents, a liability to make future payments to the beneficiary is created. This liability is often over an extended period, and nearly always after the title documents have left the control of the bank. The time span involved generally allows the account party to take possession of the merchandise while there are still unfulfilled obligations on the letter of credit. This gives counsel for the importer (account party) a better opportunity to seek court orders enjoining the issuing bank from paying the exporter (beneficiary) if the importer is dissatisfied with the product or the service delivered under the letter of credit. At the same time the beneficiary can hold the issuing bank legally responsible for payment in accordance with their undertaking to pay on the due date.

In view of the additional risk involved, where it is practical to do so, the beneficiary and correspondent banks should be persuaded not to use deferred payment letters of credit.

When DPLC is utilised, we should keep the following in mind:
(a) the shorter the period of the deferred payment the better, and should be for not longer than one year; (b) charge at least normal profit margins and preferably more, due to risk involved; (c) risk is reduced when both the account party and the beneficiary are known to be financially sound and reputable companies which pursue their business in an ethical manner.

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