

JURIDICAL REVIEW OF THE USE OF LETTER OF CREDIT IN ORDER TO GUARANTEE AND FACILITATE INTERNATIONAL TRADE PAYMENT TRANSACTIONS

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Abstract

Letter of Credit (L/C) is one of the safest methods of payment in international trade from the point of view of exporters and importers. One of the purposes of using a Letter of Credit in international trade is to guarantee and expedite payments from importers by utilizing banking services. Letter of Credit (L/C) will be a bridge for exporters and importers who are separated by countries that don't know each other well. To mediate and reduce the risks of each party, the solution offered is through the Letter of Credit mechanism, which will make it easier to settle payments, secure the funds provided by the importer and risks can be transferred to the relevant bank. The type of research used in this writing is normative legal research. The data sources used are primary data sources and secondary data sources and data analysis uses qualitative analysis. The results of the research can be concluded that the payment process for import transactions uses a letter of credit (L/C), that is, when a sale and purchase agreement has been reached between the exporter and importer, then opening a letter of credit (L/C) is followed by contact with the relevant bank for delivery implementation. transaction documents and payments.

Keywords: Letter of Credit (L/C), International Trade, Exporter, Importer

INTRODUCTION

A Letter of Credit (L/C) is a secure payment method or mechanism employed in international trade. It serves as a reliable guarantee for both exporters and importers, especially in transactions involving parties who may not be familiar with each other. Given the geographical and geological differences between exporters and importers, an L/C provides assurance to the exporter while ensuring that the importer receives the goods as specified.

An L/C, essentially a credit notification, outlines the terms of payment between the exporter and importer. It can be issued for either sight (cash) or time payments. When a bank issues a time L/C or modifies the payment terms, the deferral period is determined by mutual agreement between the bank, importer, and exporter. Indonesian banking regulations provide significant protections for importers as applicants for L/Cs, ensuring their peace of mind when using this payment method in international trade (Atmadjaja, 2021).

In today's increasingly globalized world, nations compete fiercely in areas such as technology, science, health, and natural resources. International trade, governed by mandatory legal rules, is a cornerstone of this competition. These rules, which regulate commercial relationships of a civil nature, govern transactions across borders (Aprita & Adhitya, 2020). In many countries, international trade is a major driver of Gross Domestic Product (GDP).

The unique challenges of international trade, such as differing political, economic, social, and cultural environments, have led to the development of specific mechanisms like international trade contracts. These contracts are grounded in legal principles and ensure that both exporters and importers are treated fairly. The increasing complexity of international trade, facilitated by advancements in technology, has made these contracts even more essential. At its core, international trade is driven by the fundamental human desire to exchange goods and services.

Trade is considered a 'fundamental freedom,' meaning everyone should have the liberty to engage in commerce. This freedom should not be restricted by differences in religion, ethnicity, beliefs, politics, legal systems, or other factors (Muhammad, 2019). International payment systems or methods are the means used to settle payments resulting from cross-border economic transactions or trade. In international trade, a country's central bank plays a crucial role. Therefore, central banks need to strengthen their foreign exchange reserves to provide foreign currency (Tobing, 2021). In international trade, the US dollar and Euro are commonly used as currencies for transactions. As we know, global trade has entered the phase of free markets or free trade. Free markets are designed to eliminate barriers to a product entering a destination country. However, even in a free market, a country still needs to protect its domestic products by imposing restrictions or even prohibitions on foreign products entering its market.

An examination of international trade transactions involving sellers (exporters) and buyers (importers) reveals that both parties have rights and obligations. Exporters are obligated to deliver goods and have the right to receive payment for those goods. Importers, on the other hand, must pay for the goods and have the right to demand the delivery of the purchased goods. Given the geographical distance between exporters and importers, payment settlement has its own characteristics. This is often due to the use of different currencies and the involvement of different national laws and regulations (Jusmaliani, 2008). International trade can be conducted without the need for face-to-face meetings, simply through the concept of a Letter of Credit. The long distance and lack of personal acquaintance can create risks for all parties involved. Exporters may worry that the goods they ship will not be paid for or that the goods will not be received or will not meet the agreed-upon specifications. Due to these concerns, international transactions rarely involve cash payments or advance payments, as this would be highly risky for importers. On the other hand, open account payments, where payment is made at a later date, pose a high risk for exporters (Widjaja & Yani, 2003).

In international trade, agreements are based on the laws of the respective countries where the exporter and importer are domiciled. Large-scale companies typically have legal divisions that handle contracts, and even a purchase agreement may be handled by a law firm, notary public, or other legal professionals. Therefore, if a breach of contract occurs between the exporter and importer, it can be resolved through legal proceedings. On the other hand, for small and medium-sized enterprises, purchase agreements are often simpler, relying more on mutual trust and understanding between the parties. Small and medium-sized export-import companies often face challenges related to pricing and financing. Consequently, price agreements and payment methods become the primary focus of negotiations.

A legally binding agreement executed before a notary public serves as a form of mitigation, reminding both the exporter and importer that if a breach of contract occurs, both parties can resolve the issue in court. Among the various payment methods available today, the "payment against document" method is considered ideal for both parties as it involves shared risk. The exporter can receive an initial down payment as a guarantee of the order, while the importer can optimize the available funds in their cash flow while awaiting the payment due for the ordered products.

One of the main purposes of using a Letter of Credit (L/C) in international trade is to guarantee and facilitate payments from the importer by utilizing banking services. A Letter of Credit (L/C) serves as a bridge between the exporter and the importer, who may be from different countries with limited mutual understanding (Ismail, 2010). To mediate and reduce the risks for both parties, the solution offered is through the Letter of Credit (L/C) mechanism, which facilitates payment settlement, secures funds provided by the importer, ensures the completeness of shipping documents, and transfers risks to the involved bank.

RESEARCH METHODS

The type of research used in this study is normative legal research. The research approach used in this study is a statutory approach and a conceptual approach. This type of normative research uses legal materials or sources from legislation, books, and other written legal sources (Marzuki, 2016).

RESULT AND DISCUSSION

The Mechanism of Using Letters of Credit (L/C) in International Trade

Generally, the issuing bank does not directly make the payment. Instead, another bank, authorized to do so, carries out the payment. The process of using this system begins with the involvement of a bank. The issuing bank's task is to guarantee that the importer will make payment according to the specified terms. Before issuing the L/C, the issuing bank analyzes the risk, similar to when granting credit. Not all banks can issue reliable L/Cs as the bank's credibility is influential. Subsequently, the bank receives a deposit (the amount to be paid to the issuing bank) from the importer. When issuing the L/C, based on the advice of the advising bank (representing the exporter), the exporter usually provides names of banks with recognized credibility to the importer. Typically, the exporter prefers the L/C to be issued by a government bank, a large bank, or one with a high credit rating.

A Letter of Credit (L/C) is a credit notification that constitutes an agreement for payment whereby the issuing bank promises to pay the exporter an amount equal to the L/C as long as the exporter fulfills the specified conditions. Essentially, payment under an L/C can be made when the required documents comply with the agreed-upon terms or contract. An L/C typically involves at least four types of contracts: the sales contract, the L/C issuance contract, and the agency contract (Simorangkir, 2000). However, in the implementation of payment transactions, this event has reduced the credibility of Indonesian companies in using L/Cs. Factors underlying the continued growth of L/C usage include foreign exchange controls in some countries, economic uncertainty, and the need for a way for exporters to facilitate payments for their exports. Although L/Cs are issued by banks, banks only deal with

documents, not the goods themselves. L/Cs have several roles, not only as an instrument to facilitate international trade financing but also several other functions (Rumengan, 2021).

Generally, a letter of credit (L/C) is used to finance long-distance sales contracts between a buyer and a seller who may not know each other well. In other words, a letter of credit (L/C) is used to finance international trade transactions. However, a letter of credit (L/C) is not a guarantee or a negotiable instrument. The UCP (Uniform Customs and Practice for Documentary Credits) states that a letter of credit (L/C) is a promise by the issuing bank to make payment or authorize another bank to make payment to the beneficiary upon presentation of documents (such as bills of lading, invoices, and insurance certificates) that comply with the terms of the letter of credit (L/C). It can be concluded from the UCP statement that the essence of an L/C is a "promise to pay" (Ginting, 2002). From the definitions presented earlier, it can be concluded that a letter of credit (L/C) is a vital payment instrument in international trade. It is a method of international payment that allows exporters to receive payment without waiting for news from abroad after goods and documents have been sent overseas (to the buyer) (Hendrik, 2019).

Exports and imports are separated, both geographically and geopolitically. In fact, exporters and importers don't even know each other personally. A letter of credit (L/C) is opened by the importer to provide a guarantee to the exporter, and vice versa, the importer opens a letter of credit (L/C) also as a guarantee to obtain complete shipment of goods according to what he wants. Meanwhile, the letter of credit (L/C) will not be disbursed without submission of shipping documents (Kobi, 2011). The following is the mechanism of letters of credit (L/C) in international trade, namely:

1. Buyer initiates a request for goods or services.
2. Seller asks the buyer to open a letter of credit (L/C), specifying the acceptable terms and conditions and the designated advising bank.
3. Buyer requests the bank where their account is held (issuing bank) to open a letter of credit (L/C), specifying the acceptable terms and conditions and the advising bank designated by the seller.
4. The issuing bank opens a letter of credit (L/C) and sends it to the advising bank. (A copy is also sent to the buyer, who then forwards it to the seller as confirmation that the letter of credit has been opened). If the issuing bank does not have a correspondent relationship with the advising bank, the buyer will find a correspondent bank to act as an intermediary.
5. The advising bank forwards the letter of credit (L/C) to the beneficiary (seller).
6. Once the ordered goods or services are ready for shipment, the beneficiary (seller) prepares the documents required under the letter of credit (export documents). Once the documents are ready, the beneficiary will submit them to the advising bank.
7. The advising bank will examine the documents. If they meet the requirements (in accordance with the terms of the letter of credit), the documents will be sent to the issuing bank for payment. If not, the documents will be rejected and returned to the beneficiary, along with a notification of the discrepancies.
8. Upon receipt of the documents, the issuing bank will verify the completeness and conformity of the documents received with the terms and conditions of the letter of credit. If they do not comply, payment will be rejected. If they comply, the issuing bank will pay the beneficiary (seller) through the advising bank and send the documents to the buyer. With the original documents received from the issuing bank, the buyer can claim the goods or services at customs. Without the original documents, the buyer cannot claim the goods or services.

The letter of credit (L/C) is a crucial financial instrument in the context of international trade. Its function as a guarantee of payment between the seller and the buyer helps reduce the risks associated with cross-border transactions. The primary roles of the letter of credit (L/C)

in supporting international trade are: payment guarantee, risk reduction, facilitating financing, regulatory compliance, and dispute resolution. Letter of credit (L/C) offers significant benefits to both exporters and importers in international trade transactions.

The Use of Letters of Credit (L/C) to Guarantee and Facilitate International Trade Payment Transactions

In international export and import activities, which bring together many different countries with diverse cultures, customs, languages, currencies, and climates, each country has its own unique characteristics. Conducting the export and import of goods and services that are needed by each country but may not be available or insufficiently produced domestically, and also to increase a country's foreign exchange reserves, which can help stabilize the country's economy for the needs of its people. By conducting the export and import of goods, it is expected that all needs can be met.

Choosing the governing law when using a letter of credit (L/C) as a method of import transaction is to anticipate any problems or disputes that may arise during the L/C process. Therefore, the L/C must specify the governing law to be used to resolve any disputes, such as the UCP 600 or national law. If the governing law is not specified in the L/C, the applicable national law will be chosen by the judge based on the principles of international private law.

In practice, there are sometimes obstacles in the payment process using a letter of credit (L/C) as a means of payment for import transactions. Obstacles in the import payment process using a letter of credit (L/C) include: economic crisis/monetary crisis in the issuing bank's country, delayed document submission, and document discrepancies. Another obstacle in the import payment process using a letter of credit (L/C) is document discrepancies, which can hinder the ongoing transaction process using a letter of credit (L/C). These document discrepancies are caused by differences in understanding the determination of document conformity among banks. If this happens, it can result in the rejection or delay of the letter of credit (L/C) payment (Ginting, 2015).

One of the main purposes of using a letter of credit (L/C) in international trade is to guarantee and facilitate payments from the importer by utilizing banking services. A letter of credit (L/C) serves as a bridge between the exporter and the importer, who may be from different countries with limited mutual understanding.

To mediate, a letter of credit (L/C) facilitates payment settlement, secures funds provided by the importer, and ensures the completeness of shipping documents, and risks can be transferred to the related bank. Exporters can rely on the letter of credit (L/C), as payment is guaranteed, and it can also be used as collateral to obtain a loan. For importers, having a letter of credit (L/C) means that they can import goods with minimal funds, at least until the goods arrive. Importers will feel secure because the bank will reject payment if all the requirements of the letter of credit (L/C) have not been met.

To ensure the rights and obligations of each party in international trade, everything that has been agreed upon must be included in the contract. The letter of credit (L/C) contract will specify each party's responsibilities, the type of goods, terms of delivery, shipping, insurance, payment method, and other necessary matters. Once the contract has been signed by both parties, the provisions stipulated in the letter of credit (L/C) contract will have the force of law, and each party must comply with and fulfill their obligations in accordance with the agreed-upon provisions. The following are the responsibilities of each party involved in a letter of credit (L/C) (Widjaja & Yani, 2003).

After the agreement and signing of the contract, the importer has the obligation to request the bank to open a letter of credit (L/C) for the benefit of both the exporter and the importer, which means depositing an amount of money equal to the price of the goods to be purchased and guaranteeing payment for the imported goods. The importer who applies for the

opening of a letter of credit (L/C) is required to complete and sign a contract regarding the opening of the letter of credit (L/C), which includes a clause stating that the importer adheres to the Uniform Customs and Practice for Documentary Credits (UCP). Payment to the exporter will be made when the exporter has submitted the documents required in the letter of credit (L/C), and then the importer can only take possession of the purchased goods from the carrying vessel after the documents from the exporter have been handed over to him by the issuing bank (Sudrajat, 1996).

CONCLUSIONS

To ensure the rights and obligations of each party in international trade, everything that has been agreed upon must be included in the contract. The letter of credit (L/C) contract will specify each party's responsibilities, the type of goods, terms of delivery, shipping, insurance, payment method, and other necessary matters. Once the contract has been signed by both parties, the provisions stipulated in the letter of credit (L/C) contract will have the force of law, and each party must comply with and fulfill their obligations in accordance with the agreed-upon provisions. The letter of credit (L/C) payment system plays a crucial role in international trade or export-import activities in guaranteeing the security of transactions between exporters and importers. L/Cs provide payment assurance to exporters and protect importers from the risk of receiving goods that do not comply with the agreement. With various advantages offered, such as risk mitigation, ease of international transactions, and guaranteed certainty for both parties, L/Cs have become one of the primary instruments in global trade. Therefore, although the letter of credit (L/C) is an effective instrument in international trade, a good understanding and careful application remain key to the successful use of this payment system.

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