Documentary Credit: Practices and Issues
An Extra View on Algerian Law

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Received: 04/10/2025 *Accepted: 14/12/2025* *Published:25/12/2025*

Abstract:
This paper aims to explore the practices and issues related to the letter of credit (LC), the latter is characterized by the dual principles of autonomy and strict compliance. The law on documentary credits is highly controversial as it attempts to balance two competing principles upholding the autonomy of documentary credits and preventing fraud and money laundering. The objective of the study is to show the usefulness of the Letter of Credit by the banks in accordance with strict compliance of the documents, it also demonstrates the pure letter of credit that has become a mode of the guarantee of the transaction all over the world in international sale of goods. However, the risks of fraud and violations of legislation and regulations relating to exchange and capital movements in Algerian law should not be ignored.
Keywords: Autonomy Principle, Strict Compliance, Fraud Exception, Algerian Legislature, Money Laundering, Capital Movements.

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1. INTRODUCTION

Letter of credit is also known as documentary credit (LC) or banker commercial credit which has been used as a mode of payment in the international sale of goods. It is a vehicle of choice for business to secure various financial liabilities obligations in international trade transaction. The primary purpose of the LC reduces the risks which associated with non- payment or non-performance. The bank usually adopts this instrument as a secure mode of transaction between the seller and the buyer. The LC has been used to facilitate trade for more than 150 years. It became widely used in the middle of the last century, especially after the Second World War. In the past, goods were exchanged and payment made without guarantee as to whether the goods have reached their destination. The LC acts by guaranteeing payment once the goods have arrived. The bank covers the risk of both parties and guarantees the transaction of funds. In the sale, the intention of the seller is to sell his goods and receive money, while the buyer is to receive goods and make payment. The documentary credit transaction is totally separated from the underlying contract, the banks are concerned only with documents not with goods. In fact, the banks can easily claim that the obligation to honor the credit is unaffected due to the act of fraud in connection with underlying contract. In the case of difference in interests, however some conflicts arise between the parties. Further, the seller prefers to be paid as far as he sends the goods which in fact insure the guaranty of payment. On the other hand, in some circumstances, there is uncertainty that the buyer can make the payment due to the buyer has not sufficient money to pay the goods. In this context, a letter of credit plays a vital role in reducing conflicts by ensuring secure sale transactions. A letter of credit facilitates the secure transfer of monies owed after establishing receipt of purchased item and or services. Despite the securities attached to an LC, there remains ways to undermine the role of the LC. To further ensure its role, regulation of Uniform Customs Practice (UCP) 600 entered into force on 1 July, 2007. Even if the UCP regulates the LC, many issues and cases have appeared in the international trade due to non-compliance of mutual obligations of the parties and fraud in documents. Additionally, in some circumstances, where the bank honoured wrongfully the payment to the beneficiary, notably, it can be seen as a participant

in the fraudulent act. Fraud exception which is highly a big problem to the LC, the common law intercepted with courts judgments over fraudsters since the leading case of sztejn, moreover, the fraud is upgraded, it is also involved in underlying contract which very known after appearance of the seminal case of Angelica. Civil law also faces the same dilemma of fraud that can be seen from two different angles, so far in documents and underlying contract respectively. That is to say, and beyond this concept, illicit trade is a global phenomenon as its underlying activities involve multiple countries**.** In some situations, the LC is used by different parties for smuggling money outside the country by transnational organized criminal groups, ranging from money laundering to the financing of other forms of transnational organized crime. In turn, Algeria also faces the same dilemma of smuggling money, or transfer of money outside the country by illegal methods such as inflates the value of maritime transport or false statement by traders.

2. Different Parties Involved in the Trade Transaction

Letter of credit is considered the heartbeat of international trade because it is among the most popular trade finance instrument used in international trade.(Alavi, 2017). It looks after both the exporter's and importer's interests, so it is considered the most effective and safest approach to secure the payment in an international trade transaction.**(**Haoyan& Ling Xiao, 2013).). So**,** there is a strong relationship between parties in the transaction. A letter of credit transaction comprises of three separate contracts: the first arises from an underlying contract ordinarily between a buyer and a seller and creates the basis for the letter of credit; the second arises between the account party which is the buyer and the bank issuing the letter of credit; and the third arises between the issuing bank and the beneficiary of the letter of credit.The parties involved in the documentary credit considered the major parts in the transaction of sale are the buyer, bank, and seller.(Grassi, 1995).

The buyer has many duties and obligations. He agrees with a seller about the sale and the type of payment. He contacts his bankand applies for the issuance of a letter of credit to the beneficiary. The buyer and the seller should agree that payment should take place byway of documentary credit. (Sellman& Evans, 1999). The buyer then makes payment and receives the goods.

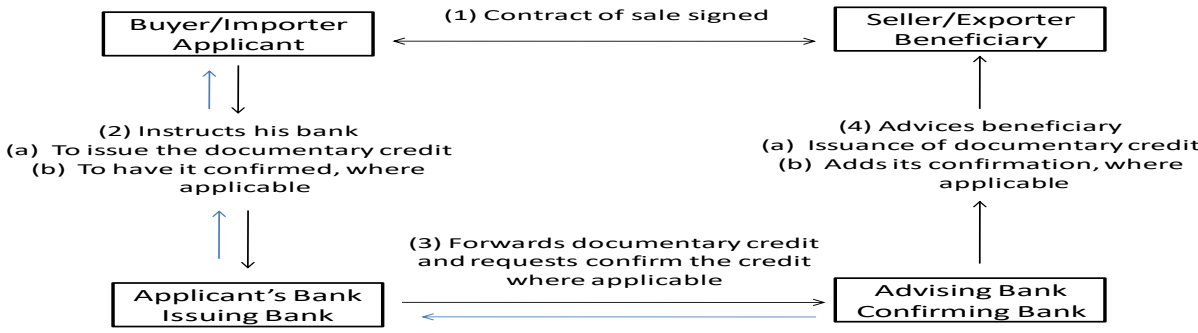
There are two types of banks: the issuing bank and confirming bank. They both play an important role for transacting money between seller and buyer. The issuing bank will issue notice to the seller that the credit is opened by the buyer in favour of the seller, and he must comply in order to obtain payment under that credit. The issuing bank may communicate the opening of credit to the seller via the mediation of another bank which is situated in the seller's country of residence called the advising bank. The confirming bank then confirms the transaction to the seller. If the beneficiary presents the stipulated documents conforming compliance with the credit, then the conforming bank undertakes to pay the seller. (Pang, 1999).

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The seller (beneficiary) is an important party in the contract, upon presenting the correct documents to the bank, he will be entitled to receive payment. Once the seller is advised about opening of credit, he must arrange shipment and tender the stipulated documents to the bank such as the bill of lading, insurance certificate and the commercial invoice. To be informed, by utilizing a letter of credit, the buyer, in turn, receives assurance that the value of the cargo is not paid until the seller shows evidence of discharging the obligations assigned to him under the contract of sale. A seller gets the cargo's value by the letter of credit, whereas the buyer receives the cargo and may sell it even before it arrives. In addition, the seller can also send the required documents to the buyer in order to advise him about the name of ship and the time of arrival to the port destination.

2.1The Functioning of a Documentary Credit Transaction

The LC as a mode of payment in international commercial transaction gives rise to many stages of separate transactions, as mentioned in figure 1 and explained below.



Source: presented by the researcher.

The parties must decide on which particular credit terms they want to use. The functioning of a documentary credit transaction has many stages or mechanisms between the different parties. Firstly, the transaction is between the seller and buyer. If they have agreed on the contract, then they must make the payment involved in the contract. In this regard, the documentary credit selected by both parties is a mode of payment defined by the contract which confirms the payment of credit based on the consent of both parties. The agreement between the seller and buyer is essential in order to establish the contract and the payment should be paid by letter of credit.

Secondly, the procedures between the buyer and the bank (issuing bank), the buyer should immediately contact the bank and open the credit in favour of the seller. The arrangement between the buyer and issuing bank would include some details about the documents, which need to be tendered by the seller. The buyer opens the credit which must conform to the terms agreed by the parties in the sale contract.Thirdly, the transaction between the banks themselves means that the issuing bank should contact another bank, namely the confirming bank situated in the country of the seller and the advising bank will add their confirmation to the letter of credit.

Fourthly, once the seller is advised about the opening of credit, he must arrange shipment and tender the stipulated documents to the bank. Under days article 14 of UCP the bank has a reasonable period of time, namely five days to examine documents and must exercise a reasonable care in inspecting the documents. The bank is under the legal obligation to pay the seller when specific documents are presented to it. Once the documents are accepted, payment has to be effected in the stipulated way. The bank having paid the seller will seek reimbursement from the issuing bank and the former bank seeks reimbursement from its client. Ultimately, the obligations of an issuing bank are established by the UCP 600. Compliance must be apparent on the face of the documents however, any defects in the goods must be a matter between the seller and the buyer. The only concern of the bank is whether the documents, on their face, comply with documents described in the credit.

2.2 The UCP 600 Applicable for the Letter of Credit

The practice of UCP 600 by the International Chamber of Commerce (ICC), introduced the UCP presenting in the unification of customs of documentary credits. UCP standardises commercial principles and is adopted by members party to ICC rules and regulations. The absence of such regulations would result in any number of challenges to international trade, especially since sellers and buyers are from different countries with different laws. As such, the main agenda of ICC is the unification of laws and customs of documentary credits for all traders by standardising trade processes and procedures. Additionally,thedefinition of the LC under UCP 600has been defined in a number of ways. The U.C.P is a set of standard terms that is incorporated by reference into the overwhelming majority of documentary credit issued around the world. Article 2 of the U.C.P. defines a letter of credit as:

Any arrangement, however named or described, whereby a bank the (Issuing Bank) acting at the request and on the instructions of a customer (the Applicant) or on its own behalf,i) is to make a payment to or to the order of a third party (the Beneficiary), or is to accept and pay bills of exchange (drafts) drawn by the beneficiary, or ii) authorizes another bank to effect such payment, or to accept and pay such bills of exchange (draft), or iii) authorizes another bank to negotiate, against stipulated documents, provided that the terms and conditions

of the credit are complied with.[1] The above definition has many meanings. It is clear that the arrangement between the buyer and seller can be realized by the intermediary of the issuing bank to guarantee the transaction. The bank can contact the advising bank located in the locality of the seller to make the payment for the buyer. Secondly, the issuing bank addresses documents to the advising bank (Confirming Bank) and if the beneficiary confirms the documents then the bank undertakes to pay the seller.

Article 1 of the UCP states the application on any documentary credit, the last sentence of the article notes that the contract is binding on parties unless otherwise agreed or excluded by the credit. This means that although parties incorporate the provisions to determine the operation of the credit, they remain free to exclude individual provisions which they consider inappropriate to their credit. Even when the UCP is adopted specifically or generally, the parties are at liberty to contract out of them as clearly expressed in the article.

2.3 The Different Laws Applicable to the Letter of Credit

The ICC (International Chamber of Commerce) was established in 1919, its primary goal facilitating the flow of international trade at a time when nationalism and protectionism posed serious threats to the world trading system. At the end of the 19th century through international banking practice, and without any legislative process, as an international mode of financing and warranty, banks soon expressed their concern that to be regulated by rules independent of any national laws. Reasonably, during the first quarter of the 20th century, some private bankers associations for example Paris, New York and UK, created some rules governing the documentary credits issued by banks members of those associations whereas in 1933 the ICC issued for the first time, its Uniform Customs and Practice for Documentary Credits. The revision of the Uniform Customs and Practice for Documentary Credits (commonly called UCP) is the sixth revision of the rules since they were first promulgated in 1933. These UCP rules were revised successively in 1951, 1962, 1974, 1983, and 1993. This UCP rules came into force since 1st January, 1994, and was published as the ICC publication nº 500, known as the UCP 500. The latest revision, the UCP text which was approved on October 25, 2006, and came into force on the 1st of July, 2007, they are known as UCP 600. It is the sixth revision of the Uniform

Customs and Practice for Documentary Credits, published as the ICC publication n° 600, by the ICC services Publication Department at 38 Cours Albert1er, Paris 75008. Thereby, last work of ICC was the fruit of more than three years of work by the International Chamber of Commerce's ICC. The universal acceptance of the UCP by practitioners in countries with widely divergent economic and judicial systems is a testament to the rules success. Simultaneously, the UCP 600 are still the most advance rules that govern the operation of the letter of credit. So, the UCP contents 39 articles, the main articles are 1, 2, 4, 5, 7, 8, 14, 17, 18, 20, 28. Interestingly, UCP (as well as other uniform rules issued by the ICC) does not contain any provisions with regards to fraud and its treatment. Thus, any fraud allegations should be examined by a competent court or tribunal pursuant to applicable law on a case-by-case basis. As far as, the UCP tackles the issues relating to the LC, apparently, there are some other regulations that combined the UCP, among them articles 5, 109 of Uniform Commercial Code (UCC), and articles 3, 15, 19, 20 of the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit 1995.

The United Nations Convention on Independent Guarantees and Stand-by Letters of Credit adopted by the General Assembly on 11 December 1995 and entered into force on 1 January 2000, is intended to facilitate the use of independent guarantees and stand-by letters of credit. This convention is the first document which presents details of the fraud rule in the letter of credit transaction at an international domain, so the convention limits its scope to independent undertakings, such as standbys and demand guarantees.The relationship between the UNCITRAL and the UCP is that the later does not include such rules regarding fraud. In contrast, the convention provides positive support to the UCP. In general, speaking about the provisions of the convention and its success can be seen that the convention condensed most of aspects of the fraud rules that have been developed in commercial practice by national courts and legislators. It is very important to note that there is provision indicating that either fraud in the documents or fraud in the underlying contracts could apply to the fraud rule. If there is such fraud crime being committed by fraudsters what kind of actions the victims of fraud should be taken whereas the fraud is clearly taking place. Therefore, it can be viewed that these provisions relating to the

fraud rules in this convention indicates a vital and positive development and offer guidance for national courts to exercise the fraud rules. In short, the convention demonstrates a constructive development on letters of credit fraud exception rules at the international level, although the application of such rules may be varied before national courts.(Susmitha, 2020, p233).

Notwithstanding, it should be informed that neither the Hague Visby Rules (International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading 1924) nor the United Nations Convention on Contract for the International Sale of Goods (CISG) 1980 have treated the letter of credit or fraud, and there is no rules or provisions through the CISG as a special matter of international sale of goods, and it did not cast the light on the LC at all. The question that arises here, is there other rules govern the LC besides the existing laws?

It exists the Documentary Instruments Dispute Resolution Expertise (DOCDEX), the ICC has adopted the DOCDEX rules in October 1997 in response to a growing number of disputes between commercial parties concerning documentary credits, and the apparent frustrations of bankers that many judges, lawyers and arbitrators failed to grasp the complexities of documentary credit practic.(Manganaro, 2011, p289).Therefore, the DOCDEX considers as a development of new practices and standards, which was revised in 2002, and 2007 consecutively by the ICC. The latest revision was in 2015. This last category of DOCDEX activities is setting up new practices and standards, it may become the most important instrument to regulate the trade finance field. Thus, it has been a minor portion of all activities, a number of issues with regards to the treatment of certain terms and conditions of the letter of credit were raised which were not covered by the UCP.(Zharikov, 2022, p14).

3. The Autonomy of Documentary Credit

The strict compliance principle means that demanding all documents presented by the seller to be in compliance with the predetermined of letters of credit. The autonomy principle requires all credit agreement between issuing banks and buyer is a separate agreement from underlying contracts between buyers and sellers, which mean the banks have to honor the credit whatever happens in the underlying transaction.

According to this principle, any disputes relating to the contract do not affect the LC. It is fundamental to credit transactions. It is interesting to note that payment using a LC is based on certain documents. The seller will be paid as long as he can produce and comply with all the necessary documents required by the buyer. The bank representing the buyer is obliged to pay the seller and cannot withhold or deny payment until the goods have safely reached the buyer. Whether the goods are in good condition at the time they are received by the buyer is irrelevant. This is based on the rule that all parties using the LC deal with documents and not with goods. The bank will not be involved in the underlying contract between the buyer and the seller, in most cases, the bank does not even have an idea what kind of goods are sold. The bank does not care whether the goods were damaged or not arrived, or lost on the way. This is what is known as the autonomy of the LC. The obligation of the bank is to pay the seller upon compliance of the documents; it cannot be interfered by any arguments between the buyer and the seller. The buyer has no choice except to make payment. This principle is completely based on presenting documents and the evidence of conformity. Furthermore, the bank is not obliged to make any investigations of such matters. Likewise, if the bank found falsification and documents do not comply with credit terms and conditions; it must refuse the documents as part of its job and no need to justify this rejection.

The principle of autonomy is stated in articles 4 and 5 of the UCP in international business practices. This principle is recognized by UCP 600 as embodied in article 4 which states that a credit by its nature is a separate transaction from the sale or other contracts. Article 5 illustrates this point by adding Banks deal with documents and not with goods, services or performance to which the documents may relate. Under the UCP, the buyer is placed in critical position, since he has no right to apply for an injunction to stop the bank from making payment. Therefore, the seminal case emerged and concerning the principle of autonomy as illustrated in the following:

In Maurice O'Meara Co. v. National Park Bank of New York, the letter of credit was in no way involved in or connected with, other than the presentation of the documents, the contract for the purchase and sale of the paper mentioned. That was a contract between the buyer and seller and does not concern the bank. The

bank's obligation was to pay slight drafts when presented if accompanied by genuine documents specified in the LC. If the paper when delivered did not correspond to what had been purchased, either in weight, kind or quality, then the purchaser can claim against the seller for damages. The bank was concerned only in the drafts and the documents accompanying them. Therefore, the decision of National Park Bank's obligation to pay the beneficiary's drafts submitted under its LC was separate and distinct from the contract of sale between the buyer and seller.

3.1 The Fraud Exception

Fraud itself is difficult to define comprehensively. The Oxford dictionary defines the term fraud: in including the use of false representations to gain unjust advantage. Generally, fraud means uncertainty. Fraud attacks public policy and is an equally serious threat to the commercial utility of the letter of credit. While fraud in the letter of credit represents unlawful action committed either by the seller or the buyer in order to obtain financial benefit by taking advantage from the loophole in the letter of credit mechanism, thereby resulting in economic loss to either the buyer or the seller. (Han et al., 2015, p459).The one established exception to the principle of the autonomy of the LC is fraud. The duty of the bank is simply to pay the seller if he presents the necessary documents after a careful review by the bank. The bank has a reasonable time to examine the compliance of the submitted documents before paying the seller. In the event of the submitted documents are falsified or fraudulent, it is a binding principle that a bank does not have to honor payment when the letter of credit involves fraud.(Sellman& Evans, 1999, p26).There are a number of risks to which the bank is expected because of the documents submitted to it. It may be related to the inaccuracy, inadequacy, correctness, falsity, or lack of general or special condition of the bank.(Emad et al., 2020,p58).As far as, there are other exceptions for the subject of fraud for instance, illegality, nullity, unconscionability, and recklessness, without a uniform international situation towards their recognition. (Alavi, 2016,p130).

The bank is not obliged to pay any credit when the documents contain statements known by the beneficiary to be false, or contain a forged signature, or invalid alteration. If it is later revealed that the documents are fraudulent, there is

no guarantee that the seller will return the sum to the bank. On the other hand, when a bank is certain that fraud is present, it may refuse payment to the beneficiary. This solution works well in the case of documentary credits because fraud can be presumed when one or more of the documents lack authenticity. If it is clear that the documents are not authentic, then payment is not due.The application of fraud is one of the exceptions to the autonomy of LC. The LC refers to fraud on documents not fraud relating to the goods.(Connerty, 2012).
Bearing in mind that if the fraud is clearly ascertained, the bank has the right to reject the documents, otherwise the bank bears the risk if the payment was done under its instructions.
If the documents are classified under lack of authenticity, thus for example, the submitted document has a false shipment day, it will be categorized as a fraud in documents.(Gaëll, 2012, p25).It is recognizable that the problem of fraud as introducing in documents as well as in the underlying contract. In fact, fraud is determined as an interrelationship between the two aspects. If there is a breach in the main contract of sale it can be seen as the fraud in documents, in addition, fraud is involved in the underlying contract that the presented documents to the bank were incorrect.

It should be noted that the parties must correctly assume their responsibilities in order to achieve what it is contracted in terms of securing the LC from the fraud and to avoid prosecutions between parties.(Meral, 2012, p48).
There are circumstances emerge after the occurrence offraud, it is obvious that where fraud exception applies, three sets of circumstances have to be distinguished: first, where there is allegation, communicated by the buyer to the bank, that fraud has occurred. In this context, the allegation may be founded on the suspicion. Secondly,it is clearly established to the satisfaction of the bank that fraud has occurred. There is unambiguous evidence before the bank, for instance that documents are fraudulent or forged. Thirdly, the bank has positive proof that fraud has been committed and that the seller knew of his fraud. In this case, the bank must not honor its obligation under the credit.

Fraud can also extend beyond the documents submitted to the issuer and can include fraud in the underlying contract. In this regards, the fraud is obviously intended by the beneficiary and not by the buyer. In fact, the buyer’s

fraud allegations were noted in all cases that merged in international sale. However, the buyer is always living in deception.

Bearing in mind that, if the documents are presented to the bank and appear in compliance with the credit terms and conditions, while it is counterfeit documents, the bank doubtfully cannot decide whether this fraud or not because it is not within the jurisdiction of the bank, but rather the jurisdiction of the court. Therefore, according to the court's decision, the bank will pay or refuse.(Al-Amaren and Aletein 2022, p52).

3.2 The Letter of Credit in Algerian Law

This part of the article tackles the adoption of the LC by Algerian legislator and the fraud exception as well. Algeria's independence was in 1962, till 1990, in this period, the state controlled and monopolized the international trade. Theoretically, the situation moved from the socialism to capitalism, as far as the business is changed from the public sector into the private sector regarding the international commerce. Therefore, foreign trade is freely to privates, subsequently, the Algerian legislator has adopted many laws which lead the privates to access to import merchandises from abroad as mentioned in articles 40- 41 of Algerian financial law 1990. The Constitution of 1996, brought a new principle which is freedom of trade and industry, article 37 elaborates more that the trade and industry should practice under the sphere of law. The Ordinance No 03-04 (2003), which concerns general rules ofimport and export of merchandises which the state conformstheprinciple of freedom of foreign trade. Moreover, article 2 of the later ordinance stipulated that the operation of import and export in foreign trade is freely of any constraint. The ordinance No 03-11 (2003), announced in article 69 that all the mode of payments which facilitate the transfer of monies whatsoever the contract and the technique method to be used. It should be noted that, the legislator attitude towards LC in foreign trade that he does not mention it in any different laws. So, since 2007, the legislator has adopted the regulation No 07-01, section 4 of article 18 mentioned the letter of credit as the cornerstone of any business transaction in international trade, in addition to that, the legislator has considered the LC as customs of International Chamber Commerce and it is an important tool of international exchanges. Accordingly, the legislator adopted the later law due to the reservation came out to the UCP 600 in the same year. It is obvious that, in foreign trade, the parties buyer and the seller are freely bound to conduct any contract depends on their mutual agreement transaction, however, no law can intervene to oblige them to conclude such transaction in selecting a particular mode of payment in foreign trade. This is clearly adopted in

article 28 section 01 of the system related to rules applicable to transactions with abroad including accounts currency, where the legislator has initially mentioned the different mode of payments in foreign trade with international recognition level. In fact, under this point of view, critically, the Algerian legislator has clearly taken a position regarding the mode of payment as pointed in national law, hence, there is no doubt that it never would be apart of LC. This is very officially confirmed by the supplementary financial law of 2009 and 2014 respectively that the unique mode of payment hitherto is the LC. Taking into account that, the intention of Algerian legislator talks about different mode of payments,but only using the LC, so far is compulsory in trade in order to combat such laundering money crime. This could reallybe happened due to such dishonest parties buyer and seller or even companies, as example here, if the documents are under compliance and no such fraud within, however, by this formulation, tradetransaction could be fake and no existence of merchandises, as a result, the whole money that being embezzled as a subject of laundering money abroad.

3.2.1 Algerian Bank's Duties

In Algerian banking system rules, it is similarly that the bank relies prior to examining the documents submitted by the both parties buyer (import) and seller (export) which contains important documents such as bill of lading, insurance certificate, and commercial invoice. In fact, the bank must examine the presented documents within the autonomy principle, and it decides whether it should hounour the credit or not, unless there is fraud after the accurate examination.

The LC as a mode of legal transfer of money abroad through the bank, as a unique model of payment applicable to any such transactions, usually the banks deal with Dollar currency in case of sale transaction including purchase of merchandises, engines, commodities, products, machines, equipments, factories,… etc. More precisely, the bank treats only with documents; it is unnecessary care about the goods that are to be brought from abroad. The bank situated in Algeria, deals with the foreign bank (advising bank) where the beneficiary's location, notably, bank is considered here as an agent of the foreign bank after obtaining the SWIFT code. The process takes place under the management and supervision of the bank containing the customer's account is registered.(Adel Bitam&WalidThabti 2018,p249).

The successful role of the bank is to verify the amount of documents submitted by the beneficiary, this is based on the use of reasonable care and

experiences of bank in this area, as well as using force of observation and supervision to discover what the documents hide the deceptive appearances.

From a purely civil law point of view, that is to say, there is no too much laws regarding the applicable of LC, except what it mentioned above, the bank has irrevocable obligation to play on presentation of documents that comply on their face. The fraud exception under Algerian perspective that fraud as an objective issue, it is clearly that the undertaking of the bank can reject the documents if there is clear evidence of fraud without any looking for the principle actor or third party.

Concerning the fraud exception under Algerian jurisdiction, there is no such court decisions regarding the fraud, but in returning to Algerian legislature, it found that there is a lacuna of laws regarding the LC generally and fraud specifically. It should take in consideration that Algerian perspective must be redressed the value of LC and fraud exception, then it would be better if Algeria ratifies the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit and collaborates with it.

3.2.2 Money Laundering By Using the Letters of Credit

Money laundering leads to unreliable changes in money demand overseas, major risks to a bank's soundness, affects the legality of financial transactions, also wreaks havoc on exchange rates due to unanticipated cross-border asset transfers. As money laundering is transnational by nature, many international coalitions have been developed in a bid to tackle the issue. Some of the major groups focused on combating money laundering and adjacent offenses including the Financial Action Task Force (FATF); the Egmont Group of Financial Intelligence Units, International Criminal Police Organization (INTERPOL), European Union Agency for Law Enforcement Cooperation EUROPOL, United Nations Office on Drugs and Crime (UNODC) and Wolfsberg Trade Finance Principles.Take into consideration that, money laundering has a very connected with forged documents, these documents are prepared by a very professional expert accountants in money laundering who working with transnational organized groups, also providing such new technological tools which facilitate the operation. Furthermore, it obvious that the penetration of information technology into international trade field leads to the easiness of such illegal

operations by using falsifying documents.In addition, some traders use false declaration on bill of lading in order to move capitals outside the country as discussing in the following in Algerian judiciary.

In the case of SPA GLOVIZ, which occurred between 2018-2020, a commercial transaction was with the Korean Hyundai Company, the judgment was on 2024, Algerian customs authorities contacted the shipping agents to verify the transportation value of the bills of lading (198 import operations), based on their response, it was determined that there was a discrepancy between the actual value of the transportation costs (included in the response) and the actual value of the transportation costs. The declared invoice value (inflating the value of the sea freight in all invoices) is considered an illegal transfer of foreign currency abroad, resulting in financial fines that must be paid, totaling $44,060,052.70. It is equal to four times the value of the crime object in terms of the difference, and after investigation it was proven that the shipping costs are high in terms of the total price of the goods CFR including the value of the goods FOB. The transportation FRET and the value FOB (free on board), (Delivery of goods on board the ship), meaning that the goods are delivered on board the ship, the seller fulfills his obligation to deliver when the goods pass the ship's rail at the designated port of shipment. This type of contract is only used in maritime transport or transport via inland waterways only. Shipping costs are borne by the seller, and the price paid by the buyer includes all costs, from the value of the goods and shipping to their delivery on board the ship. In accordance with Article 738 of the Algerian Maritime Code, which states the following: "The carrier undertakes, under a contract for the carriage of goods by sea, to deliver a specific commodity from one port to another, the shipper undertakes to pay the compensation called the freight? After an examination conducted by Batna Customs, a significant discrepancy was discovered, which constitutes an inflated value of the declared shipping costs and the illegal transfer of currency abroad. The accused inflated the value of the transport and made a false statement, which is a violation of the provisions of Order 2-96. Therefore, the four defendants convicted and punished in accordance with the penal law.

Another case occurred on 2019, the judgment was on 2024, the facts are summarized as follows: On 04 February, 2019, the Public Prosecution Office at

the Batna Court received a complaint registered under No. 19/9841 from the chief collector of Batna Customs against the defendant R.K. The complaint stated that, within the framework of an investigation opened by the customs administration in coordination with the Regional Service for Subsequent Control in Constantine. A subsequent control of import files was carried out and registered through various customs offices. Relating to customs clearance of imported industrial equipment and machinery within the framework of the tax and fiscal privileges system granted by the National Agency for Investment Development and Promotion, by exploiting the information base available to them, which shows the existence of a fraudulent trend active in smuggling foreign currency abroad. Exploiting the import operations of plastic industry equipmentby transferring this equipment from the port of Skikda to the public warehouse in Batna for the purpose of final customs clearance due to its lack of availability on the SIGAD information system, they received shipment No. 115 dated 13 January, 2019 from the head of the regional service in Constantine, an investigation was opened into the process of importing the equipment by the sole proprietorship and limited liability companyrepresented by its manager who imported a plastic manufacturing machine worth $121,840. After exploiting the customs administration's database for similar equipment from the same country, it became clear that the value of the same machine was imported for only $34,990, and by calculating the difference, it became clear that the smuggled value in dinars is 12,333,125.13 DZD, which is equivalent to$ 94870.19 the value of the smuggled currency abroad.

4. CONCLUSION

This paper establishes an overview regarding the role of LC in international trade arena. So, the letter of credit plays a crucial role in sale transactions. Likewise, it is a mode of payment that is not concerned with the contract sale of goods. The bank only treats documentary credit as an instrument of payment, in order to pay the seller after submitting the necessary documentations. The bank makes payment only with strict compliance of proper documents in order to protect the applicant against unscrupulous beneficiaries. The burden of this mode of payment is fraud exception, which makes the letter of credit ineffective. Many a times, geographical distance, currency problem,

absence of efficient prosecution and the diversity of legal system at the globe level strengthen and encourage the reason for commission of fraud by egregious customers involving documentary credit mechanism of banking institutions, or by connivance with the banking officials. Therefore, many disputes arise where the parties simply did not perform their mutual obligations in the transaction. The proliferation of fraud threatens the utility of letter of credit and the risk is always on behalf the buyer who cannot get his money back. Thus, the risk of fraud in the sale transaction is very expected, but unfortunately, the UCP 600 has taken an absolute silent position about the risk of fraud, leaving it opens to national legal systems. Nonetheless, the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit has extremely tackled the position against fraud exception. International judiciary, for instance, English courts require a high standard of proof of fraud, American and Canadian courts have widened the exception to the underlying contract, the Australian and Singaporean judiciary also including fraud as a matter of unconscionable conduct. Furthermore, the civil law does not exclude fraud as long as it vitiates the entire transaction. Therefore, there is no such internationally agreed construction of the fraud exception. In contemporary international trade arena, in most common letter of credit fraud cases buyers and banks are considered victims. It has to note that, critically, the UCP enshrined under article 14 (b) that the bank examines the documents in a maximum of five banking days following the date of presentation to compliance? However, how often the bank could examine a huge number of documents in very short period? There is an ambiguity through the existence of such laws which could be revised regularly. In other circumstances the LC is used as a matter of money laundering by criminal activities. Criminal group activities are able to exploit weaknesses in international cooperation, domestic legislation and online technology to conceal and facilitate illicit money flows. However, they do this through the use of international transfers, shell companies, money mules, cryptocurrency and other forms of money laundering through letters of credit. In fact, Monteiro has described fraud as cancer in international trade transaction in worldwide. Hence, the only way to resolve fraud offences that the ICC should revise the existing laws to be more relevant and effective to treat the threat of fraud phenomenon.

Moreover, a full coordinating of tailored response to such sophisticated phenomena requires close cooperation with partner organizations and association like the International Money Funds (IMF), INTERPOL, the Association of Certificate Fraud Examiners (ACFE), EGMENT Group and Wolfsberg Group, at this stage, to break all illegal activities related to money laundering using the LC that really weaken the economy of the states. Algerian legislator has tried to combat money laundering in terms of movement of capital through false declaration and cheating in bill of lading, here I just mention only few cases but still it needs more efforts and collaboration to eliminate money laundering.

In fact, the following suggestions and solutions come out by the researcher in order to highlight the remedy for the fraud exception and money laundering (movement of capitals) as follows:

-The bank must scrutinize the documents especially while the documents are presented by new or less- known client.

-Buyer is widely to be prudent to conduct an extensive investigation on the credibility of the business counterpart before stating into any contract with him.

-Buyer should prefer to choose method of exporting goods: Freight on Board (FOB) instead of *Cost, insurance, and freight* (CIF) because of security and guaranty.

-Use of Pre-shipment inspector or agent to the buyer: as the buyer bears the risk of loss in fraud transaction, he should appoint an independent agent or inspector in the country of the seller, to check the goods conformity in terms of quantity and quality, even if this procedure costs some money to the buyer, but it somehow secures the operation of sale in favor of the buyer's interest.

-It should be more collaboration between states to organize various workshops, and special training programs for bank's employees over the globe, to maintain, address, discuss, develop, reduce, and tackle the issues of fraud risks in transnational transactions of sale of goods by dishonestly misuse of letters of credit and money laundering.

-It should insistently a great collaboration and efforts internally and internationally between states to defeat and stop the red flag activities that are using money laundering overseas.

-Bank systems need more surveillance and technical assistance activities that offers opportunities for raising awareness of the need for a robust international anti-money laundering system.

- For Algerian legislator, it is necessary to undertake more responsibilities to develop effective policies, procedures, obligations and controls to detect and prevent the abuse of commercial letters of credit for the purposes of laundering illicit funds.

-The ICC should introduce some provisions to regulate the fraud problem and laundering money crime in their next publications and revisions.

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