



What's in a Name: Back to Back LCs

On many levels, so-called back to back LCs are troublesome. Nonetheless, they are useful and even important in many transactions. They provide an intermediary with an inexpensive means of obtaining credit in favor of an ultimate seller without tapping its own credit line, relying instead on the credit line of the ultimate buyer.

There are, of course, significant risks in this arrangement, particularly where the terms of one LC are not aligned with those of the other LC.

One of the most frustrating aspects of back to back LCs, however, is the confusion attendant on discussing issues and risks due to the lack of a universally accepted protocol for naming the parties and undertakings. The range of names is widespread and wild, with the most extreme being “slave credit” and the lack of practice rules addressing back to back credits ensures ongoing confusion. Before one can even discuss a question about the practice, it is essential to agree of the meaning of the names to be used with respect to the parties.

Part of the difficulty is the starting point: Is it the transaction between ultimate supplier and intermediary

Your Views Wanted

To facilitate harmonization of this practice, DCW invites bankers and lawyers to suggest a common terminology to be used to refer to the parties and LCs in connection with back to back LCs. Suggestions will be published in future issues with the name of the person suggesting it unless they prefer to remain anonymous.

(which is probably the first contract in time and which calls for an LC); or is it the contract between the ultimate buyer and the intermediary which is the source of the LC which is the basis for the LC in favor of the ultimate supplier? Of course, even these designations of “ultimate” are debatable since there may be additional parties on either end of the chain and they may also use LCs.

Some LC experts use designations such as primary or initial to describe the two LCs or the parties, but these terms could refer to the chronology of when they were issued, the chronology as to when the underlying contract required that they be issued, or their importance to question being discussed (both the ultimate supplier and the ultimate buyer would regard the LC relevant to it as primary).