

Chapter Seven: Disputes Between the Buyer and Seller (in the Underlying Contract) in Relation to Letters of Credit

Chapter Seven: Disputes Between Buyer and Seller on the Underlying Contract in Relation to Letters of Credit

Introduction

This chapter intends to deal with disputes between the seller (beneficiary) and the buyer (applicant) on the sale contract, in relation to letters of credit. The letter of credit contract is created by virtue of the sales agreement between buyer and seller. Its purpose is to provide security to the seller to replace that which was represented by the shipping documents, which he gives up in exchange for the credit. Although the sale contract imposes a duty on the buyer to open a documentary credit in the seller's favour, the letter of credit contract is entirely a matter between the seller and the banker. However, as will be discussed later, the involvement of the buyer is vital in both the opening and alteration of the credit. Although the contract between the buyer and seller is the cause of the letter of credit contract, they are totally independent.

The chapter consists of two sections: the first section will examine the contract between the buyer and the seller, under which several matters will be discussed, namely: (i) questions of interpretation concerning the nature of the buyer's obligation, in relation to his duty to open the credit; (ii) agreed variation and the effect of non-compliance by the buyer, where the seller accepts a non-conforming letter of credit; (iii) the seller's remedies for the buyer's failure of duty; (iv) the seller's duties upon the opening of a credit; (v) buyer's remedies after realisation of credit; (vi) whether payment by letter of credit is considered as absolute or conditional; and (vii) suggestions for the buyer and the seller to safeguard their rights. Although all these issues will be addressed, the main issue for discussion here will be centred around whether payment is absolute or conditional and this will also act as the main focus point of section two, where it will be evaluated in light of the basic principles. There are, for example, some possible conflicts with the well-established principles of letters of credit. On one hand, the principle of independency requires the payment by letter of credit to be absolute; on the other hand, as will be seen later in the chapter, there is a line of authorities which go

against this supposition. So, if the seller cannot get payment out of the bank which should be a matter under the letter of credit, he may still have recourse against the buyer.

Section One: Contract Between Buyer and Seller

1. Questions of Interpretation Concerning the Nature of the Buyer's Obligation in Relation to his Duty to Open the Credit

1.1. Condition Precedent

A letter of credit arrangement occurs when the buyer and seller agree in the sale contract that the payment should be effected by opening a credit. By incorporating this particular clause, the buyer is under a duty to procure the opening of a credit in the seller's favour. This obligation is not necessarily a condition precedent to the performance of all the seller's duties, but it is often a condition precedent to his duty to deliver the goods.¹ There may be in place, certain conditions precedent to the buyer's duty, which provide a credit under the sales contract in which the seller has to perform. For instance, in a case where a sale of copra was concerned², there was a requirement for a provisional invoice, which was a condition precedent to the buyers' obligation of opening the credit. Upon the seller's failure to provide such a provisional invoice, it was held that "The buyers' obligation to provide a letter of credit did not arise until a provisional invoice was tendered by sellers and proper notice given by him as to the form of credit he required".³ Therefore, it was evident from the judgment that as both the seller and the buyer had initially agreed, under the sale contract, that the seller would provide the buyer with a provisional invoice, then it followed that this would be a condition precedent to the buyer's obligation to procure the opening of a confirmed credit. It is usual, within the well-established principle of letters of

¹ *Benjamin's Sale of Goods*, Fifth edition. (edited by A.G. Guest) (Sweet & Maxwell, London, 1997) n15 at § 23-064 p.1684. See also Tiplady, D., *Introduction to the Law of International Trade* (London, 1989) p.176.

² *Knotz v. Fairclough, Dodds and Jones Ltd.* [1952] 1 Lloyd's Rep 226.

³ *Ibid.*

credit, that it is the duty of the buyer to open a letter of credit, as required by the sale contract. If the contract terms are themselves incomplete, and unresolvable by reference to custom, the supposed duty to cooperate would be no more than an agreement to agree, which is not a workable contractual term. Moreover, “the scope of the proposed duty in any given case would be impossible to define with the degree of precision necessary for a workable term.”⁴ In the case of Giddens v. Anglo-African Produce Ltd.,⁵ an action was brought by the purchasers against the sellers for damages for non-fulfillment of the contracts of sale. The sellers claimed that the credit required by the sales contract had not been opened. Thus, the condition precedent for their performance had not arisen. Bailhache J., in delivering judgment for the sellers said:

“Here is a contract which calls for an established credit and in purported satisfaction of what this contract calls for what they get is this: ‘Negotiations of drafts under these credits are subject to the bank’s convenience. All drafts hereunder are negotiated with recourse against yourselves.’ How that can be called an established credit in any sense of the word absolutely passes my comprehension.”⁶

Further, in the case of Trans Trust S.P.R.L. v. Danubian Trading Co. Ltd.,⁷ upon failure of the buyers to open the credit in accordance with the requirements of sales contract, Denning L.J. was of the view that, since the buyer did not procure the opening of the credit, the sellers were not obliged to perform at all. He continued to say:

“What is the legal position of such a stipulation [that a credit should be provided]? Sometimes it is a condition precedent to the formation of a contract, that is, it is a condition which must be fulfilled before any contract is concluded at all. In those cases the stipulation ‘subject to the opening of a credit’ is rather like a stipulation ‘subject to contract’. If no credit is provided, there is no contract between the parties. In other cases a contract is concluded and the stipulation for a credit is a condition which is an essential term of the contract. In these cases the provision of the credit is a condition precedent, not to the formation of the contract, but to the obligation of the seller to deliver the goods. If the buyer fails to provide the credit, the seller can treat himself as discharged from any further performance of the contract and can sue the buyer for damages for not providing

⁴ *Siporex v Banque Indosuez* [1986] 2 Lloyd’s Law Rep, 146, at 162.

⁵ *Giddens v. Anglo-African Produce Ltd* (1923) 14 Ll.L. Rep. 230.

⁶ *Ibid.*, at p. 230 (col.2).

⁷ *Trans Trust S.P.R.L. v. Danubian Trading Co. Ltd* [1952] 2 Q.B. 297.

the credit.”⁸
 Todd⁹, on commenting on the above quote, claims that there are significant differences between the two types of cases. He states that in the first type, both the seller and the buyer are equally exempt from an obligation to perform in situations where no credit has been issued. In contrast, the second type reveals that the buyer remains liable in damages unlike the seller, who is relieved of such a performance obligation. Denning L.J. regarding the above case, held that in this particular case, the credit was of the second type, and that this was the normal situation.¹⁰ Accordingly, the buyers were liable for damages for breach.¹¹ It has been submitted that the buyer’s contractual obligations, with regard to payment in the case of a documentary credit, are different from the case in which he contracts to make payment directly. With regard to the former case which involves the opening of a letter of credit, the buyer’s obligation is to procure the opening of such a credit in conformity to the seller’s demand. Having done so, the buyer is deemed to have fulfilled his obligations.¹²

1.2. The Importance of the Buyer’s Co-operation in Relation to Opening of a Credit

The buyer’s cooperation may be required for the credit to operate, for instance, where the credit provides that shipment is to be on a vessel nominated by the buyer. Where the seller cannot make the shipment and thus is unable to operate the credit because no vessel is nominated, the buyer will be in breach of contract by reason of his failure.

The credit may require the buyer to inform the bank of the nomination of vessel. If the shipping documents show shipment on the vessel and otherwise conform to the

⁸ [1952] 2 Q.B. 297, 304.

⁹ Todd, P., *Bills of Lading & Bankers’ Documentary Credits* p. 61.

¹⁰ [1952] 2 Q.B. 297, Lord Denning observed that “it is clear that the stipulation for a credit was not a condition precedent to the formation of any contract at all. It was a condition which was an essential term of a contract actually made”. at 305.

¹¹ [1952] 2 Q.B. 297, 305.

¹² Ventris, F.M., ‘New Problems of Financing Oil Shipments’ *LMCLQ* (1975) p. 38 at 42.

credit, the bank will have to pay. It may otherwise be necessary for the seller to provide documentary evidence to the bank, that the vessel named in the shipping documents has been nominated by the buyer.¹³

Another example where the cooperation of the buyer may be necessary, is in the completion of the documentation to be tendered under the credit. Thus, the buyer or his representative may be required to sign a certificate of inspection of the goods. If he fails to do so, he will again be in breach of the contract with the seller, and he will have rendered the credit inoperable. The buyer may be ordered by the court, if an appropriate situation arises, to complete the document, and should he fail to comply, a third party, usually a court official, may be empowered to do so in his place.¹⁴

1.3. Type of Credit to be Opened, and Problems where Contract is Silent

The type of credit which the buyer opens in favour of the seller, must be the exact type of credit¹⁵, conforming in both form and substance, as specified under the documentary credit clause. A confirmed credit was called for in the case of Wahbe Tamari & Sons Ltd. v. Colprogeca Sociedade Geral de Fibras, Cafes e Produtos Coloniais Lda.¹⁶ In the course of his alleged confirmation, the correspondent reserved right of recourse against the seller, in relation to the total bills drawn and negotiated under the documentary credit, which was not a requirement at the time when the contract of sale was formulated. It was therefore agreed, that in doing so,

¹³ Cf *Banque de l'Indochine et de Suez SA v JH Rayner (Mincing Lan) Ltd.* [1983] Q.B. 711 where the requirement in the credit provided: "Shipment to be effected on vessel belonging to Shipping Company that member of an International Shipping Conference". It was held that reasonable documentary proof was required (p. 719B), confirmed by the CA on this point at [1983] Q.B. 728, 729.

¹⁴ See *Astro Exito Navegacion SA v Chase Manhattan Bank NA* [1983] 2 AC 787; See also Jack, R., *Documentary Credits*, at § 3-42 p. 54.

¹⁵ If, for instance, a confirmed credit was agreed upon, the furnishing of a revocable credit (as in *Panoutsos v. Raymond Hadley Corporation* [1917] 2 KB 473) or of an irrevocable but unconfirmed credit (see *Soproma S.p.A v. Marine and Animal By-Products Corporation* [1966] 1 Lloyd's Rep. 367, 386.) is insufficient. If an irrevocable credit was agreed to be opened in London, the opening of a credit in another place does not discharge the buyer's duty, see *Enrico Furst & Co. v. WE Fischer Ltd.* [1960] 2 Lloyd's Rep 340.

¹⁶ *Wahbe Tamari & Sons Ltd. v Colprogeca Sociedade Geral de Fibras, Cafes e Produtos Coloniais Lda*[1969] 2 Lloyd's Rep. 18.

the buyer had failed to provide the type of credit that was initially prescribed¹⁷. If the contract is silent as to the type of documentary credit, the courts tend to accept the presumption that an irrevocable credit was agreed upon¹⁸, as indicated in the case of Giddens v. Anglo-African Produce Co. Ltd.¹⁹ In that case, there was a provision in the contract of sale that a letter of credit was to be 'established' with a certain bank. When the buyers furnished the sellers with a revocable credit, the seller, not being very happy about the type of credit, refused to deliver the goods. Commenting on Bailhache J.'s judgment, as previously discussed under section 1.1.), Benjamin offers his interpretation of the outcome by initially clarifying the meaning of the term 'established'. In clarifying the judge's interpretation, he confirmed that Bailhache J., "read the word 'established' as describing the word 'credit' and explained that the revocable credit furnished by the buyers could not be considered an 'established credit'"²⁰. In doing so, his Lordship dismissed the buyers' application. In other words, Bailhache J. perceived the term 'established credit' as equivalent to an 'irrevocable credit, and since a revocable credit does not constitute good security, it cannot be regarded as 'established'. However, it should be noted that finalisation of a sales contract has not occurred in cases where the nature of the credit to be provided or the documents against which payment is to be made has not been determined.

1.4. Time of the Availability of the Credit and Related Problems with Regard to Ambiguous Clauses. The Implication of C.I.F. and F.O.B. Contracts

The buyer has a duty to furnish the documentary credit in time; he is responsible even for the delay which is caused by factors out of his control.²¹ The time as to

¹⁷ Ibid at 19.

¹⁸ Cf. UCP art 6(c), under which a credit is assumed to be irrevocable if not stated to be revocable; See also Appendix C for update of the related section of UCC.

¹⁹ *Giddens v. Anglo-African Produce Ltd* (1923) 14 Ll.L. Rep. 230.

²⁰ *Benjamin's Sale of Goods*, at § 23-066 p. 1685.

²¹ In *Lindsay (AE) & Co Ltd v Cook* [1953] 1 Lloyd's Rep 328, where a delay was caused by the inter-bank communication, the seller was held entitled to repudiate the contract of sale. Cf *Baltimex Baltic Import and Export Co Ltd v Metallo Chemical Refining Co Ltd* [1955] 2 Lloyd's Rep, 438, where the parties contemplated a delay. See also *Benjamin's Sale of Goods*, at § 23-074 p. 1688.

when the credit is to be available should be followed according to the date indicated on the contract of sale.²² Usually the sales contract should contain a provision regarding the time within which the credit is to be available, although no problems will arise in its absence. If a situation arises where time, for instance, is not stipulated, or in using the term, it remains unclear as to how it will be implemented within the contract agreement, it is left to the courts to determine whether or not the seller is relying on the provision of the credit in order to finance the transaction and if so, the buyer would be required to open the credit within a reasonable period of time.²³ If, rather than specifying a clear date, it is required that a credit be opened immediately, the buyer must have such time, as is needed by a person of reasonable diligence, to get such a credit established.²⁴ Alternatively, if a credit is to be opened within a few weeks, then it must be opened within a reasonable time, the period of which is to be judged on the facts of individual cases.²⁵ If it is agreed that the opening of the credit is to be conditional upon the seller fulfilling his role and responsibilities, such as informing the relevant party of the readiness of the goods for shipment, then as soon as the event has occurred, it is compulsory that the credit is opened.²⁶ Sometimes the shipment is agreed to be over an expanded period; in such cases, the credit must be available over the whole period of shipment.²⁷ In

²² Hedley, W., *Bills of Exchanges and Bankers' Documentary Credits* pp. 286-7.

²³ Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 61.

²⁴ *Garcia v Page & Co. Ltd.* (1936) 55 Ll LR 391, 392. See generally, Hedley, p. 286.

²⁵ See generally, *Etablissements Chainbauz SARL v Harbormaster Ltd.* [1955] 1 Lloyd's Rep 303; see also *Sinason Teicher Inter-American Grain Corp v Oilcakes and Oilseeds Trading Co Ltd.* [1954] 1 WLR 1394. See also *Benjamin's Sale of Goods*, at § 23-068 p. 1685.

²⁶ Hedley, W., *Bills of Exchanges and Bankers' Documentary Credits*, (Lloyd's of London Press Ltd., 1997) p. 286. See generally, Jack, R., *Documentary Credits* (Butterworths, London, 1993), at § 3-26 p. 46. *Plasticmoda SpA v Davidson Manchester* [1952] 1 Lloyd's Rep 527. See also *Knotz v Fairclough Dodd & Jones Ltd.* [1952] 1 Lloyd's Rep 226, In this case a provisional invoice was sent as a prerequisite to a credit being opened. These cases must be distinguished from those where the opening of a credit is a condition precedent to the existence of a contract of sale. In such a case, in the absence of a credit facility, there is no contract at all. *Trans Trust SPRL v Danubian Trading Co Ltd.* [1952] 2 Q.B. 297.

²⁷ *Pavia & Co SpA v Thurmann-Nielsen* [1952] 2 Q.B. 84; See also, Hedley, W., *Bills of Exchanges and Bankers' Documentary Credits* p.287.

Garcia v. Page & Co Ltd²⁸ there was no express stipulation of time of opening of the credit in the contract itself. Porter J. was of the view that three months was an unreasonably long time for the buyer to establish the credit²⁹. Regarding the reasonability of time, the courts have adopted Lord Watson's test from Hick v. Raymond & Reid.³⁰

“When the language of a contract does not expressly, or by implication, fix any time for the performance of a contractual obligation, the law implies that it shall be performed within a reasonable time. The rule is of general application, and is not confined to contracts for the carriage of goods by sea. In the case of other contracts the condition of reasonable time has been frequently interpreted; and has invariably been held to mean that the party upon whom it is incumbent duly fulfils his obligations, so long as such delay is attributable to causes beyond his control, and he has neither acted negligently nor unreasonably.”³¹

When addressing ambiguous clauses, it appears that clauses which encompass a time specification, but are vague as to their requirements for opening of a documentary credit, can be potentially problematic. This is evident in the Sohio Supply Co. v Gatoil (USA) Inc³² case, where the buyer was asked to provide a documentary credit 10 days before the expected date of loading, as a requirement stipulated by the contract of sale. The argument was based on the exact interpretation of the ‘10 day period’, where the seller understood it to mean 10 days prior to the commencement of the shipping period, unlike the buyer who believed it ought to be calculated from either the last day or based on the buyer's estimation of the day when the ship would arrive. The Court of Appeal found this particular point irrelevant, but Staughton L. J. demonstrated his preference with the sellers proposition. His Lordship observed that:

“I have no doubt that the sellers show a good arguable case on that point; I do not think it would be right for me to say more than that. That makes it unnecessary to consider whether the affidavit which they produced sufficiently displays a good arguable case on

²⁸ *Garcia v Page & Co Ltd* (1936) 55 Ll L Rep 391.

²⁹ *Ibid* at 392.

³⁰ *Hick v. Raymond & Reid* [1893] A.C. 22.

³¹ *Ibid* at pp 32-33. In this regard, it was said that this case is not a banking case, but concerns the obligations of a consignee under a carriage contract. However, the test is of general application. Cited by Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 61.

³² *Sohio Supply Co. v Gatoil (USA) Inc.* [1989] 1 Lloyd's Rep 588.

the point of custom”.³³

Another example which can be offered to illustrate an ambiguous term, regarding the time within which the credit is to be opened, can be seen in Etablissements Chainbaux S.A.R.L. v. Harbormaster Ltd.³⁴ It was a condition in the contract of sale, that the credit was to be “opened in London within a few weeks”. Devlin J., in the course of his judgment, treated this as too ambiguous a term regarding time. He therefore, allowed a reasonable time for opening of the credit. Devlin J. observed that the requirement to open a credit, within a reasonable time prevails, even where, under the contract, delivery is postponed until a considerable time into the future. In the above case, where the delivery was not to take place for eight months, he said:

“It is to be observed that the provision as to the letter of credit is to be contrasted with the provision as to delivery. Delivery is not to start until the lapse of eight months; the letter of credit, on the other hand, is to be ‘opened in London within a few weeks’. It is plain, therefore, that although the letter of credit is to provide for payment against shipping documents, and therefore payment could not in any event be due until some eight months, when deliveries started, the buyers offered to establish the letter of credit before that. One can well understand the business reason for that. Sometimes a letter of credit is wanted merely because the seller is unwilling to make arrangements for shipment, which may involve him in expense, unless he knows he is going to be paid. That might be the normal case where the seller has got the goods and the only expense he has to incur in relation to them is to put them on board ship or otherwise arrange for their transport, but in this case it plainly is not so: the seller had to manufacture the goods, and what he desires is to have the letter of credit for it is plainly so that he will have assurance, within a few weeks and before he begins manufacture, that he is certain to be paid and that the labour of manufacture will not therefore be done in vain.”³⁵

The documentary credit clause, as put to use in Transpetrol Ltd. v. Transöl Olieprodukten Nederland BV³⁶, was significantly more perplexing, where the buyer agreed to provide the letter of credit within a period of one day, following his receipt of the seller’s appointment in relation to a vessel. The ambiguity arose when it was provided that the seller should give an additional three days to the buyer, of his notice of intention to nominate. Phillips J. observed that:

“It seems to me that the concept of being required to give a minimum of three days’ notice of intention to nominate is nonsensical. Prima facie such a notice is of no value to

³³ Ibid at 591.

³⁴ *Etablissements Chainbaux S.A.R.L. v. Harbormaster Ltd* [1955] 1 Lloyd’s Rep. 303.

³⁵ Ibid at 305 (col. 2).

³⁶ *Transpetrol Ltd. v Transöl Olieprodukten Nederland BV* [1989] 1 Lloyd’s Rep 309.

the buyer for it is implicit that there is the intention to nominate in any event”³⁷ Therefore, it was held that the seller’s failure to comply with the stipulation could not be used as an excuse for the delay in the furnishing of a letter of credit and the seller had the right to repudiate the contract of sale.³⁸

1.4.1. Application to C.I.F. Contracts

Most c.i.f. contracts of sale do not specify a time for the furnishing of the credit, but a date or period for the shipment of goods is usually provided.³⁹

If an actual date, as opposed to a period, of shipment is specified in the contract, it is well established⁴⁰ that the buyer is obliged to furnish the documentary credit at a reasonable time before that date. The rationale behind this is that, the seller is entitled to have the credit before he actually prepares the goods for shipment. Nevertheless, different provisions concerning the time for opening the credit can be made. For example, if the parties agreed by contract that the buyer’s duty to furnish a credit is dependent on the prior receipt of explicit instructions from the seller, then the buyer is not obliged, in the meantime, to furnish a letter from the issuing bankers indicating that the documentary credit will be established as soon as these instructions are received.⁴¹

When the contract provides a period of shipment, there is an ambiguity over whether the documentary credit must be furnished on the first day of shipment or at a reasonable time before that. In the case of Pavia & Co. S.p.A. v. Thurmann-Nielsen⁴² where a sale of groundnuts was concerned, a period of shipment, namely February-April 1949, was provided for in the contract, but the required

³⁷ Ibid at 310-311..

³⁸ Ibid at 309.

³⁹ Jack, R., *Documentary Credits* at § 3-16 p. 42. See also *Benjamin’s Sale of Goods*, at § 23-069 pp. 1686-7.

⁴⁰ *Plasticmoda Societa per Azioni v Davidsons (Manchester) Ltd.* [1952] 1 Lloyd’s Rep 537, 538

⁴¹ *Nicolene Ltd. v Simmonds* [1952] 2 Lloyd’s Rep 419, affd. [1953] 2 Q.B. 543.; See also *Benjamin’s Sale of Goods*, at § 23-069 pp. 1686-7.

⁴² *Pavia & Co. S.p.A. v. Thurmann-Nielsen* [1952] 2 Q.B. 84; For notes of the case, see Chorley & Smart, *Leading Cases in the Law of Banking*, 6th ed., (Sweet & Maxwell, London, 1990) pp. 265-268.

documentary credit was not furnished until April 22, which was held by the court to be too late. Denning L.J. said that if there is no express stipulation, the credit must be opened at the beginning of the shipment period “because the seller is entitled, before he ships the goods, to be assured that, on shipment, he will be paid. The seller is not bound to tell the buyer the precise date when he is going to ship; and whenever he does ship the goods, he must be able to draw on the credit. He may ship on the very first day of the shipment period.”⁴³ It is possible to draw two perspectives from this assertion, one of which is at the very latest, a letter of credit must be opened on the first day of shipment. Secondly, this in effect also suggests that the documentary credit should be opened at the very latest, at a reasonable time before commencement of the shipping period, since the seller is entitled to be assured of payment before he actually initiates the shipment.⁴⁴

Two years later, in the case of Sinason-Teicher Inter-American Grain Corporation v. Oilcakes and Oilseeds Trading Co. Ltd.⁴⁵, Lord Denning expressly supported the second view. In this particular case, a contract for the sale of barley called for shipments during October-November 1952, but the sellers cancelled the contract when the buyers failed to furnish a bank guarantee by September 10, which was long before the shipping period. The Court of Appeal held that the buyers had not been in default. Lord Denning said “The correct view is that, if nothing is said about time in the contract, the buyer must provide the letter of credit within a reasonable time before the first date for shipment. The same applies to a bank guarantee”.⁴⁶

1.4.2. Application to F.O.B. Contracts

In an f.o.b. contract, the buyer often has the right to determine the date of

⁴³ Ibid at pp. 88-89.

⁴⁴ *Benjamin's Sale of Goods*, at § 23-069 p. 1686.

⁴⁵ *Sinason-Teicher Inter-American Grain Corporation v Oilcakes and Oilseeds Trading Co. Ltd.* [1954] 1 WLR 1394.

⁴⁶ Ibid at 1400.

shipment⁴⁷ (though an f.o.b. contract allows the seller to make a shipping arrangement). It was argued in Ian Stach Ltd. v. Baker Bosley Ltd.⁴⁸ that, the documentary credit had to be opened at a reasonable time before the date nominated by the buyer in the shipping instruction. Diplock L.J. in that case disagreed with such a rule since;

“the buyer would not know how long it would take to bring the goods from the place where they were and transport them to the port: he would not know in a case of this kind, and did not know, whether or not the goods had to be rolled to order or whether they were in stock or whether they were partly rolled. It seems to me that in a case of this kind, and in the case of an ordinary f.o.b. contract financed by a confirmed banker’s credit, the prima facie rule is that the credit must be opened at latest...by the earliest shipping date”⁴⁹.

To sum up, no hard and fast rule can so far be drawn from the study of the cases involving either c.i.f. or f.o.b. contracts on when the buyer should open the documentary credit in cases where the sales contract only provides for a period of shipment without an exact date for furnishing the documentary credit. The rule expressed by Lord Denning in Sinason-Teicher⁵⁰ was that the documentary credit should be opened at a reasonable time before the first day of the shipment period is to be welcomed by the seller. This view enables the seller to prepare the goods for on-time shipment.⁵¹

2. Agreed Variation and the Effect of Non-Compliance by the Buyer where the Seller Accepts a Non-Conforming Letter of Credit

2.1. The Amendment of the Credit. Both the Buyer’s and Seller’s Consent are Necessary

The amendment of a credit is possible, if it is proposed by the buyer (the applicant of the credit) either with the seller’s (the beneficiary’s) agreement or at his request. The amendment itself is a matter between the issuing bank and the seller, perhaps

⁴⁷ Jack, R., *Documentary Credits*, at § 3-20 p. 43.

⁴⁸ *Ian Stach Ltd. v Baker Bosley Ltd* [1958] 2 Q.B. 130. This is a case where a sale of steel plates on f.o.b. terms was concerned.

⁴⁹ *Ibid* at 143-4.

⁵⁰ *Sinason-Teicher Inter-American Grain Corporation v Oilcakes and Oilseeds Trading Co. Ltd.* [1954] 1 WLR 1394.

⁵¹ *Ibid* at 1400.

via an advising bank and the seller.⁵²

2.1.1. The Legal Position

A bank's undertaking embodied in a letter of credit, constitutes a binding contract between the bank and the beneficiary. In the same way that a contract can only be altered by the consent of all parties to it, a bank's undertaking contained in a documentary credit can only be amended by the bank giving the undertaking and the seller. The consent of the advising bank is required, if it needs to confirm the credit. For the obvious reason, that the credit is issued on the buyer's instruction, it is implicitly necessary to have his agreement for any amendment to the credit.⁵³

In practice, the applicant initiates the amendment of the credit by instructing the issuing bank of such amendment. Such amendment may also be initiated by the seller. The seller will make such a request, if he is unhappy about the terms and conditions of the credit at the time the credit is advised to him. Amendment could also take place where the seller is in need of extension of the shipping period or where the type of certificate that is required in the credit is not obtainable. If the seller finds the terms of the credit, as advised to him, are unacceptable, very often, it will amount to a rejection of the credit. In practice, the seller is often reluctant to object to an amendment that has been initiated by him, and it may be the case that he is not even entitled to do so, depending on the merits of each case. Where a seller is faced with an amendment to a credit, which is unacceptable, he is entitled to inform the bank that it is unacceptable to him, stating that he intends to comply with the credit as originally advised in accordance with Article 9(d) of the UCP, which provides that the bank's undertaking cannot be amended without the consent of the other parties concerned i.e. banks and the beneficiary. Without the consent of those who are involved in the credit transaction, the credit remains unchanged.⁵⁴

⁵² Jack, R., *Documentary Credits*, at § 3-33 p.49.

⁵³ See Article (9)(d) of the UCP.; see also, Rosenblith, R.M., 'Modifying Letters of Credit: The Rules and the Reality' 19 *Uniform Commercial Code Law Journal* (1987) 245, at 246, n.3.

⁵⁴ For an example of amendments being accepted and rejected, see *Ficom SA v Sociedad Cadex Ltda* [1980] 2 Lloyd's Rep 118 at 127 and of amendments simply not being accepted, see *United City*

2.1.2. Problems in Practice

After the buyer instructs the issuing bank to make an amendment, if the issuing bank agrees with it, it will instruct the advising bank of the amendment. Finally, the amendment will be advised to the seller, usually in the form of a statement, confirming that the credit has been amended. It is not always the case that the seller will be requested to inform the bank of the acceptance of the amendment. It is not surprising to note that it is frequently not so, and it is then for the seller himself to object to the amendment of his own accord, assuming that he is aware of his right to reject amendments.⁵⁵ This is particularly the case, when it is evident that the document neglects to suggest that it is an offer from the bank to the seller that the credit should be amended as such⁵⁶. Following rejection of the amendment on the part of the seller, it is conceivable that the seller can regard any insistence by the bank in relation to such an amendment, as a repudiation of the credit and thus claim damages against the bank. Or another option is that the buyer may be specifically requested, by the seller to withdraw the instructions for the amendment. Should the buyer refuse to accept such a request, then taking both positions into consideration, it is evident that the sellers' would prevail. It has been suggested that in compliance with the unamended credit, the seller could alternatively present the documents

Merchants v Royal Bank of Canada [1979] 1 Lloyd's Rep 267 at 275, *per Mocotta J*; See also Jack, R., *Documentary Credits*, at § 3-34 p. 49.

⁵⁵ For the seller to have a right to reject amendment is quite an odd and excessive right as the seller is required to do nothing for the credit to be established, why should not the same rules apply upon an amendment? But as suggested by an American commentators, Rosenblith, *supra* note 53, p.245, at 248. "where all parties are proceeding in good faith, there is no problem... But parties may not always proceed 'in good faith' or their interest in performance of the underlying sales contract may change, and that is where resort to legal niceties leads". In the United States, the legal position is that the applicant's consent is not necessary for the amendment to bind issuer and beneficiary, as long as these two players both consent. Consideration is not essential to support a modification to issuer's engagement under a letter of credit. (UCC § 5-105) (see Givray, A.J.; Chapman, C.J.; Doub, J.C; Gabriel, H.D; Hisert, G.A; Luttrell, R.T., III; Wunnicke, B., 'UCC Survey: Letters of Credit' 46 *The Business Lawyer* (1991) p.1579, at 1621.

⁵⁶ The position was illustrated by the standard form for amendments issued by the ICC (ICC Publication No. 416, page 47. The new forms, Publication No. 516, which says, "[t]he above mentioned credit is amended as follows", and "this amendment is to be considered as part of the above mentioned credit and must be attached thereto". As an example of an amendment which beneficiaries felt bound to accept even though it was strongly against their interest to do so, see *Astro Exito Navegacion SA v Chase Manhattan Bank NA* [1983] 2 AC 787, headnote. Cited by Jack, R., *Documentary Credits*, at § 3.36 p. 51.

directly to the bank and should the bank thereupon refuse to accept them, it would follow that the bank would then be held liable to the seller.⁵⁷

The new Article 9 d (iii) of the UCP, covers the situation where the seller is silent following receipt of an amendment. The position is the same as that established by legal principle. If the seller does not indicate his acceptance or rejection of amendment, either by words or conduct, the Article provides that his silence is not to be taken as an acceptance of it.⁵⁸ This sounds justifiable when advice of the amendment is to be construed as an offer from the bank to the beneficiary: unless something can be found which is to be taken as indicating his acceptance of that offer, it remains simply an offer.⁵⁹

In accordance with Article 9(ii) of the UCP, it is provided that although the credit itself appears not to have been amended following acceptance of it by the beneficiary, it is not down to the issuing bank to revoke an amendment which it has advised.⁶⁰ From this, it is evident that a confirming bank will be found to be obliged by an amendment, which it has merely passed on, without making it specifically clear upon doing so, that they have no intention of adding to its confirmation, but are merely advising it. A consequence of it adding its confirmation is that, until such amendment is accepted, the credit remains unamended and the bank continues as a confirming bank in regard to it. Upon acceptance of such amendment, the credit can then be amended, and it is a requirement that the bank ceases to be bound by its

⁵⁷ See Jack, R., *Documentary Credits*, at § 3-36 p. 51. See same source for seller's remedies at p. 105.

⁵⁸ The same position holds in the US as well, see *Atari, Inc. v Harris Trust and Savings Bank*, 559 F. Supp. 592 (N.D. Ill. 1984) [Note, Rosenblith, *supra* note 53 at 252 criticised that "[t]he Atari court ... made a correct conclusion but for a possibly incorrect reason".].

⁵⁹ Compare *Opinions (1980-1981) of the ICC Banking Commission*, ICC Publication No.399, Reference 71, where the Commission decided by a majority that the beneficiary's consent to an amendment had to be an express acceptance and could not be implied merely from his silence. See also, Rosenblith, *supra* note 53 p.245, at 249.

⁶⁰ Jack, R., *Documentary Credits*, at § 3-39 p. 52.

confirmation.⁶¹ Consequently, the seller has the choice of whether or not to continue with a confirmed credit.

It is also evident from Article 9 d (iv) of the UCP, that the seller cannot be selective of which amendments to accept and which to disregard, where several options are initially offered in one advice. This is based on the legal theory of 'offer and acceptance'. In cases where there are a number of amendments within one advice, if the buyer accepts certain amendments, this would constitute a counter offer in which it is up to the bank to accept or not. Where the beneficiary demonstrates such selective choices in relation to which amendments to accept and to reject, this constitutes a counter offer and the bank can subsequently decide on whether to accept it or not. Yet, such an amendment may become binding if all parties concerned have agreed to it. However, one cannot assume from Article 9 d (iv) of the UCP, that a partial acceptance necessarily signifies that the amendments have been totally refused. Conversely, such partial amendment will not be given any significance. Therefore, after partial acceptance, the seller's position, will be similar to that if he had kept silent, in that his options would remain open⁶².

2.2. The Seller's Waiver of Non-Furnishing the Credit

It is submitted that it is open to the seller to accept a different type of credit, where that accepted type provides less security. It sometimes happens that a seller raises no objection to a credit which does not conform but proceeds as if it was a conforming credit. There are three potential possibilities which can arise as a result of this situation⁶³. Firstly, it may be possible that the seller is observed as having waived the irregularity. Another possibility is that he may be held to be estopped from objecting at a later date. However, in practice, it is apparent that little distinction is made between the above mentioned two possibilities, and there is a tendency to focus on the former. The final possibility is that a variation may be held

⁶¹ Ibid.

⁶² Ibid at 53.

⁶³ Ibid at 48.

in relation to the underlying contract. In other words, from viewing the actions of the parties, where they are seen to be in agreement of utilising the same format of credit as they had when they had initially opened it, it can be presumed that they are open to utilising a flexible and varied approach.

The seller may, by his conduct, be assumed to have waived his right to demand another type of credit which is of greater security even without giving reasonable notice. This can be seen in the case of Panoutsos v. Raymond Hadley Corporation,⁶⁴ where the seller accepted payments for a number of shipments by means of a credit which was not confirmed instead of the one agreed upon in the sales contract which was by confirmed credit. The seller was held not to have the right to repudiate such payment since he had apparently waived the buyer's breach of condition, in failing to provide a confirmed credit. In this regard, Viscount Reading CJ. observed:

“In Bentsen v. Taylor, Sons & Co.⁶⁵ Bowen L.J. stated the law as to waiver thus: ‘Did the defendants by their acts or conduct lead the plaintiff reasonably to suppose that they did not intend to treat the contract for the future as at an end, on account of the failure to perform the condition precedent?’ Reading sellers for defendants and buyer for plaintiff in that passage, it applies exactly to the present case. The sellers did lead the buyer to think so, and when they intended to change that position it was incumbent on them to give reasonable notice of that intention to the buyer so as to enable him to comply with the condition which up to that time had been waived.”⁶⁶

With reference to the doctrine of estoppel, it is apparent that it shares similar features to that of the doctrine of waiver. To illustrate this, it is evident in situations where the seller has made representation to the effect of claiming his strict legal rights, upon which the buyer has relied at his expense.⁶⁷ In this case the seller will be estopped. In addition to this, when considering the waiver, representation could still be implied from words or behaviour, and the estoppel would thus act as a

⁶⁴ *Panoutsos v. Raymond Hadley Corporation* [1917] 2 K.B. 473.

⁶⁵ *Bentsen v. Taylor, Sons & Co* [1893] 2 Q.B. 283, a case on a sales contract.

⁶⁶ [1917] 2 K.B. 473, at p. 478.

⁶⁷ Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 67. However, Lord Denning MR., in *WJ Alan & Co. Ltd. v El Nasr Export and Import Co* [1972] 2 Q.B. 189, at 213 stressed that a person was entitled to rely on the waiver despite no detriment having occurred as a result of acting on it.

preventative mechanism by stopping the seller from later going back on his word with relation to representation, without giving adequate notice.⁶⁸ In Soproma S.p.A v. Marine and Animal By-Products Corporation⁶⁹, McNair J. clearly emphasised that there was no apparent difference when the matter was addressed as either waiver, variation or estoppel. He said:

“the material question is as to the effect of the seller’s acceptance of the letters of credit. On the assumption stated, the sellers could, I think, plainly have treated the buyer’s failure to open proper letters of credit as a breach of condition entitling them to rescind and claim damages.... In my judgment, by so acting, the sellers must be taken to have accepted the position that their letters of credit were in order, and not having at any time given notice to the buyers that they required letters of credit in strict conformity with the contract, they are precluded (whether the matter is put as waiver, variation or estoppel) from now saying that the letters of credit were not in order and did not accurately define the contractual mode of obtaining payment including the period of availability.... Unless the concession asked for by the sellers had been granted, the sellers would have been in plain default since by shipping the whole 600 tons under one bill of lading they had put it out of their power to tender two bills of lading, namely, a separate bill of lading under each letter of credit. Accordingly, they can only succeed in the present case if they can establish that in law they made a valid tender of documents under the letters of credit as modified and within the period of availability of these letters...”⁷⁰

It is practically important, especially when a series of shipments are involved in a contract, to consider whether the seller has waived the breach or has agreed to a variation of the contract. If the seller waives an objection concerning a documentary credit furnished regarding one shipment, he is entitled to give notice to insist on strict compliance regarding the remaining shipments. However, if the acceptance of a non-conforming credit involves a variation of the contract of sale, it may affect the entire transaction. Very often, the courts treat the seller’s acceptance of a non-conforming credit as waiver.⁷¹ In the leading case of waiver, Panoutsos v. Raymond Hadley Corporation⁷², the sellers did not insist on the confirmed credit after the first

⁶⁸ See the judgment of Balihache J. in *Panoutsos v. Raymond Hadley Corporation* [1917] 1 K.B. 767, at pp. 769-770.

⁶⁹ *Soproma S.p.A v Marine and Animal By-Products Corporation* [1966] 1 Lloyd’s Rep 367.

⁷⁰ [1966] 1 Lloyd’s Rep. 367, 386 (col. 2).

⁷¹ For more authorities on waiver, see *Panoutsos v Raymond Hadley Corporation* [1917] 2 KB 473, 477-478. See also *Plasticmoda Societa Per Azioni v Davidsons (Manchester) Ltd* [1952] 1 Lloyd’s Rep 527; *Ian Stach Ltd v Baker Bosley Ltd* [1958] 2 Q.B. 130; *Frust (E) & Co v WE Fischer Ltd* [1960] 2 Lloyd’s Rep 340; *Soproma S.p.A. v Marine and Animal By-Products Corporation* [1966] 1 Lloyd’s Rep 367.

⁷² *Panoutsos v Raymond Hadley Corporation* [1917] 2 KB 473.

of a number of shipments. The sellers were held to have waived their right to a confirmed credit, not only in relation to the shipment in question, but also in relation to the subsequent shipments. To avail themselves of a confirmed credit, the sellers are required to lodge the buyers with reasonable notice before any confirmation takes place. However, waiver of a right in respect of the first shipment will not necessarily preclude the seller from reasserting his right in respect of a subsequent shipment. It was made clear in Cape Asbestos Co Ltd v. Lloyds Bank Ltd,⁷³ that the bank was able to revoke a revocable credit even without notice. The defence raised by the bank was that the bill of lading tendered did not conform to the terms of the credit because it (the bill of lading) was made out to the order of the buyers instead of being to the order of the defendant bank. The sellers had argued that since the bank had accepted the bill of lading, it had waived its right to reject on those grounds regarding the following shipment. Bailhache J. said,

“That case [*Panoustos*] was an authority for the proposition that where an act had to be done by the buyer of goods, such, for instance, as the opening of a confirmed banker’s credit, and he did not perform that act, and the seller nevertheless went on delivering the goods with knowledge that the act had not been performed, the seller could not suddenly cancel the contract and refuse to make further deliveries without giving the buyer reasonable notice of his intention so as to give the buyer an opportunity of putting himself right. That case was no authority for the proposition, that *where an act had to be done periodically, as, for instance, the delivery of a bill of lading in such a case as the present, the fact that it had been done irregularly in the past justified the assumption that the irregularity would be waived in the future.* The *Panoustos* case had only reference to an act which had to be done once and for all, and not to an act which had to be done periodically.”⁷⁴

From the above mentioned cases, it can be gathered that there appear to be two ways in prescribing how the waiver act is to be accomplished. The first method prescribes that the act should be done “once-and-for-all” as was the case in the confirmation of the credit in Panoustos⁷⁵. The other method which has to be done in a periodical fashion, can be illustrated in the case where tendering bills of lading takes place for each shipment, as in Cape Asbestos.⁷⁶

⁷³ *Cape Asbestos Co Ltd v Lloyds Bank Ltd* [1921] W.N. 274.

⁷⁴ *Cape Asbestos Co Ltd v Lloyds Bank Ltd*[1921] W.N 257 (col.2).[emphasis added].

⁷⁵*Panoutsos v Raymond Hadley Corporation* [1917] 2 KB 473).

⁷⁶ As explained by Todd. P., *Bills of Lading & Bankers' Documentary Credits* p. 69.

The Court of Appeal in W.J Alan & Co. Ltd. v. El Nasr Export and Import Co.⁷⁷, had a difference of opinion. It was evident in this case that the buyers were in agreement, under the contract of sale, to provide a confirmed credit which would cover the sale on the terms of f.o.b. of two cargoes of coffee priced at 262 Kenyan shs, per ton. When the buyers offered sterling, in order to represent their confirmed credit, no objection was voiced. At the same period of time, an extension was requested on the part of the sellers once they had started to utilise the credit. Following the second shipment, but prior to the documents being presented, the pound sterling was devalued, whilst the Kenyan currency did not alter. Subsequent to the payment being made in sterling under the confirmed credit, the court refused the seller's application, which attempted to claim damages based on the difference in the exchange rate. The court said "the sellers, by their conduct, waived the right to have payment by means of a letter of credit in Kenyan currency and accepted instead a letter of credit in sterling"⁷⁸. Lord Denning MR., stressed that a person was entitled to rely on the waiver even though no consideration had moved from him and despite no detriment having occurred as a result of acting on it.⁷⁹ Megaw L.J. offers the following judgment which appears to support the above, but based on a different foundation; "As I see it, the necessary consequence of that offer and acceptance of a sterling credit is that the original term of the contract of sale as to the money of account was varied from Kenyan currency to sterling"⁸⁰. In offering his point of view, his Lordship went on further to say that; "if there were no variation, the buyers would still be entitled to succeed on the ground of waiver"⁸¹.

In the case of Glencore BV v. Lebanese⁸², a sale of 25,000 tons of wheat at the

⁷⁷ *WJ Alan & Co. Ltd. v El Nasr Export and Import Co* [1972] 2 Q.B. 189.

⁷⁸ *Ibid*, at 214, per Lord Denning MR.

⁷⁹ *Ibid* at 213.

⁸⁰ *Ibid* at 217.

⁸¹ *Ibid*, at 218.

⁸² *Glencore BV v Lebanese* [1997] 4 All ER 514.

price of US\$135 per tons was concluded. The buyers undertook to pay an addition of \$7 per tons if they failed to accept the quantity as contracted. The terms of the contract specified f.o.b. shipment on a vessel chartered by the buyers and that payment was to be by an irrevocable and confirmed letter of credit. The buyers stipulated that payment under the letter of credit would be made based on the terms that the sellers presented bills of lading issued as 'freight pre-paid' in order to comply with the requirements imposed on them by the principal. The buyers' vessel was late arriving at the loading port and gave notice of readiness one day later than the agreed date. Due to the delay, the sellers refused to load and made extra-contractual demands for pre-payment of the price and for an additional payment of \$7 per tons. The buyers claimed for damages for the sellers' act. The Court of Appeal held in favour of the seller. Evans L.J. commented *obiter* that:

"what may be called the classic rules of estoppel and waiver can apply in circumstances such as these (the acceptance of non-contractual goods delivered under a sales contract), so as to prevent a party who fails or refuses to perform the contract from relying upon conduct by the other party which would otherwise justify his doing so. The occasions when these rules may be involved in these circumstances are limited, for example, by the fact that it is rarely if ever possible to imply an unequivocal representation of fact from a party's silence on the relevant issue."⁸³

In the absence of any unequivocal representation by the sellers that they relinquished or would relinquish their rights arising out of the buyers' failure to open a letter of credit in the form required by the sales contract, the sellers could not be said to have misled the buyers into believing that the freight pre-paid requirement was no longer important to them.

In conclusion, it can be established that both the waiver and estoppel doctrine are only considered effective in situations where, the stipulation has only been added for the purpose of directly benefiting the party who initially waived it, or who has been estopped from relying on it.⁸⁴ It should be noted that whether the seller's conduct amounts to waiver or evidences a variation of contract, depends on the

⁸³ Ibid at 527. Since the buyers in that case did not suggest that these rules apply there, and therefore Evans LJ just left it at that.

⁸⁴ Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 69.

circumstances of individual cases.⁸⁵ A variation cannot be effective unless it is supported by consideration.⁸⁶

3. The Seller's Remedies for the Buyer's Failure of Duty

3.1. The Seller's Right to Terminate the Sales Contract if the Credit is Not Opened

No doubt, the seller is under no obligation to ship the goods until a credit conforming to the sales contract has been opened. Since "time is of the essence", the seller is entitled to terminate the contract if the credit is not opened by a date as stated in the contract or by a time which may be determined from it. Very often, the time for the opening of the credit can only be determined by the interpretation of "reasonable time".⁸⁷ The seller can terminate the contract by serving a notice giving the buyer a reasonable date by which the credit must be provided. If the buyer defaults, the seller may then cancel the contract and claim damages.

Sir Nicholas Browne-Wilkinson V-C said in British and Commonwealth Holdings plc v. Quadrex Holdings Inc.⁸⁸ that, "where, if a time for completion had been specified in the contract, time would have been of the essence, the innocent party can make time of the essence by serving a reasonable notice to complete even though the guilty party has not been guilty of improper or undue delay".⁸⁹

The seller's right to repudiation is justified where, upon the buyer being allowed to open a credit within a specified time, the seller must equally hold a right to end the contract.⁹⁰ This is because the behaviour of the buyer merely signifies a repudiation of the contract.

⁸⁵ See *Siporex v Banque Indosuez* [1986] 2 Lloyd's Law Rep 146, at 163-164, where the buyer failed to establish a waiver nor an estoppel; See also *Benjamin's Sale of Goods*, at § 23-076 pp. 1688-89.

⁸⁶ See Chitty, J., *Chitty on Contracts: General Principles* Vol. 1 (28th ed) (Sweet & Maxwell, London, 1999) at § 23-034 p 1156.

⁸⁷ See, Section, (1.3) *supra*.

⁸⁸ *British and Commonwealth Holdings plc v. Quadrex Holdings Inc*[1989] Q.B. 842.

⁸⁹ *Ibid* at 858.

⁹⁰ Jack, R., *Documentary Credits*, at § 3-25 p. 46.

3.2. The Seller's Remedies Against the Buyer for Damages

The seller holds the right to claim damages from the buyer, if the nonperformance of the contract is due to the buyer's failure in opening a conforming credit.⁹¹ The assessment of the seller's loss in these cases, stems from the same fundamental principles that are applicable in situations in which a buyer is found to have rejected a sale contract. However, it is claimed that other relevant rules concerning damages are referred to.⁹² In summary, the damages will usually be assessed by deducting the contract price from the market price of the goods.⁹³ If the buyer knows of some special circumstances during the conclusion of the contract, an alternative measure of damages will be applied. For instance, it is evident from Trans Trust SPRL v. Danubian Trading Co. Ltd.⁹⁴, that the buyers were already aware that the sellers would not be able to buy in the goods if they, the buyers, had failed to open the credit. The plaintiffs were awarded "a sum equal to the profit which they would have made if the credit had been opened and the successive sales had gone through".⁹⁵

Section 2-325(2) of the UCC states that issuance of the credit discharges the applicant only if the credit is not dishonoured.⁹⁶ Therefore, the seller is entitled to sue the issuer on the credit and sue the buyer on the underlying obligation⁹⁷, if the credit is dishonoured.

⁹¹ For more on the question of damages, see the case of *Heisler v Anglo-dal Ltd.* [1954] 2 All ER 770. See on damages generally, Schmitthoff, C.M., *Schmitthoff's Export Trade: The Law & Practice of International Trade* 9th ed (London, Stevens & Sons, 1990) p. 421.

⁹² Jack, R., *Documentary Credits*, at § 3-28 pp. 47-48.

⁹³ See *Sale of Goods Act 1979*, s.50. In *Ian Stach Ltd. v Baker Bosley Ltd.* [1958] 2 Q.B. 130, the plaintiff sellers were entitled to recover the difference between the contract price and the market price, which they had already obtained on a re-sale of the goods.

⁹⁴ *Trans Trust SPRL v Danubian Trading Co Ltd* [1952] 2 Q.B. 297.

⁹⁵ *Ibid* at 300.

⁹⁶ For more authorities, see *Bank of United States v Seltzer* (233 AD 255 NY 637 (1931)); *Greenough v Munroe* (46 F2d 537 (SDNY), aff'd, 53 F2d 362 (2d Cir.), cert. Denied sub nom; *Irving Trust Co. v Oliver Straw Goods Corp.*, 284 US 672 (1931)). See also § 5-117 of the UCC.

⁹⁷ Cf UCC § 3-310 (similar rule for transactions involving negotiable instruments).

According to Dolan, it is argued that, the duty of the buyer to pay the seller on the banker's default is justifiable. "If the applicant is a general depositor, he loses his deposit and becomes a general creditor and must then pay the beneficiary; yet there is no double loss. The applicant, even though he must pay the beneficiary, faces only one loss – that of his deposit. The money he pays the beneficiary is in return for the benefit the applicant receives out of the underlying contract".⁹⁸

3.3. Consequences of Failure to Open Credit, or Failure to Provide Reliable and Solvent Paymaster⁹⁹

3.3.1. The Seller's Right to Claim Loss of Profit on Transaction

The provision of a credit is more than simply a way of paying the price, since the seller may use such a credit as security to raise finance for the transaction, for instance by purchasing the goods. Thus, if the buyer fails to open such a credit he is, then, in breach of contract. The seller, therefore, will be entitled to claim damages that are available under ordinary principles applicable to contractual damages. This can be seen in the case of Trans Trust S.P.R.L. v. Danubian Trading Co. Ltd.¹⁰⁰ The buyers failed to open the credit related to the sales contract. The sellers subsequently used the loss of profit, which they could have potentially made following the sale, as the basis to their claim of damages. The buyers were held¹⁰¹ to be in breach of contract. The buyers' argument was that the sellers could have resold at a profit since the steel market was rising.¹⁰² Thus, the damages should be nominal only. The sellers for their part, claimed that they had not resold the steel at profit because in the absence of a credit, they were unable to purchase it from the manufacturers. That is to say, they were relying on the provision of the credit to

⁹⁸ Dolan, *The Law of Letters of Credit. Commercial and Standby Credits*. Revised edition. (Warren, Gorham and Lamont, 1996) p. (12-18).

⁹⁹ Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 69.

¹⁰⁰ *Trans Trust SPRL v Danubian Trading Co Ltd* [1952] 2 Q.B. 297; see also Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 71.

¹⁰¹ *Trans Trust SPRL v Danubian Trading Co Ltd* [1952] 2 Q.B. 297, 298.

¹⁰² *Ibid* at 305.

finance the transaction. Denning L.J., regarding treating the provision of the credit as simply an alternative way of paying the price, said:

“This argument reminds me of the argument we heard in Pavia & Co. v. Thurmann-Nielsen.¹⁰³ It treats the obligation to provide a credit as the same thing as the obligation to pay the price. That is, I think, a mistake. A banker’s confirmed credit is a different thing from payment. It is an assurance in advance that the seller will be paid. It is even more than that. It is a chose in action which is of immediate benefit to the seller. It is irrevocable by the banker, and it is often expressly made transferable by the seller. The seller may be relying on it to obtain the goods himself. If it is not provided, the seller may be prevented from obtaining the goods at all. The damages he will then suffer will not in fact be nominal. Even if the market price of the goods has risen, he will not be able to take advantage of the rise because he will not have any goods to resell. His loss will be the profit which he would have made if the credit had been provided. Is he entitled to recover that loss? I think he is [subject to the normal rules of remoteness of damage in contract]...”¹⁰⁴

Upon the same ruling, this could be applied to a falling market. In the case of Ian Stach Ltd. v. Baker Bosley Ltd.¹⁰⁵, the sellers repudiated the sales contract due to the fact that the credit had not been opened in time. Diplock J., in the course of his judgment, explained that the measure of damages was the difference between the contract price and market price at the time of repudiation¹⁰⁶.

3.3.2. Position Where There are a Number of Shipments¹⁰⁷

In the case of Urquhart Lindsay & Co. v. Eastern Bank Ltd.,¹⁰⁸ the sales contract was for a number of shipments of machinery by installments. It was agreed that payment for each installment was to be by irrevocable letter of credit. The buyer, upon completion of two installments and having paid for them, disputed the amount payable on the third installment. The bank, on the buyer’s instructions, refused to pay. When the seller sued the bank, the main question was in relation to the measure of damages. In the main course of judgment, the bank was of the view that

¹⁰³ *Pavia & Co SpA v Thurmann-Nielsen* [1952] 2 Q.B. 84.

¹⁰⁴ [1952] 2 Q.B. 279, 305 (bottom).

¹⁰⁵ *Ian Stach Ltd. v Baker Bosley Ltd* [1958] 2 Q.B. 130.

¹⁰⁶ *Ibid* at 145. Diplock L.J. said “The measure of damages is the loss of profit on the transaction, since the defendants must have known that their failure to provide the letter of credit would make it impossible for the plaintiffs to carry out the transaction. I think, therefore, that probably the right basis is loss of profit”. 145.

¹⁰⁷ Todd, P., *Bills of Lading & Bankers’ Documentary Credits* p. 71.

¹⁰⁸ *Urquhart Lindsay & Co. v. Eastern Bank Ltd* [1922] 1 K.B. 318.

they had merely undertaken to pay money, and that the amount of damages for non-payment of money was only the amount of the money itself. The sellers, on the other hand, were of the view that the position was the same as if the buyers had themselves refused to pay for the goods. Rowlatt J. expressed concern to the consequences of the buyers' refusing to pay on the installment. He reached the conclusion that the sale by installments would entitle the sellers to cancel the entire transaction. That is to say, the sellers were able to deem the non-payment of the one installment as a ground for bringing the entire sales contract to an end. By doing so, the sellers would be released from any obligation, not only under this particular shipment, but under any further shipment as well. Indeed, the sellers' loss was therefore their loss of profit on the entire transaction, not only non-payment for one shipment. Similarly, on the same grounds, the sellers could have recovered this in an action against the buyers. Rowlatt J. said:

“Now if a buyer under a contract of this sort declines to pay for an installment of the goods, the seller can cancel and claim damages upon the footing of an anticipatory breach of the contract of sale as a whole. These damages are not for non-payment of money. It is true that non-payment of money was what the buyer was guilty of; but such non-payment is evidence of a repudiation of the contract to accept and pay for the remainder of the goods; and the damages are in respect of such repudiation.”¹⁰⁹

To conclude, the buyer is seen to be in breach of the sales contract in cases where he fails to open a credit, or if the credit fails to operate. Moreover, if the breach has occurred, it should not be regarded as simply being non-payment of money. It is submitted that the credit means much more than simply payment of money. Thus, as summarised by Todd, “the damages are not limited to the payment of the price, but will be anything that is recoverable under ordinary principles applicable to contractual damages”.¹¹⁰

4. The Seller's Duties Once a Credit Has Been Opened

4.1. Seller's Duty of Warranty

Under s.5-111(1)¹¹¹ of the UCC the seller has a duty of warranty (that the

¹⁰⁹ Ibid at 323 (bottom)- 324 (top).

¹¹⁰ Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 72.

¹¹¹ See Appendix C for update, Section 5-110.

documents actually comply with the terms of the credit), an obligation that is usually neglected by commercial lawyers and courts. Dolan suggested that warranty should play an important role in letter of credit disputes, in which the account party alleges that the seller (the beneficiary¹¹²) has engaged in fraud.¹¹³

First of all, what does the warranty do? The warranty often gives the complaining buyer (the account party¹¹⁴), an adequate remedy at law which deprives him of the equitable relief. It also gives independent significance to the seller's certificate (common in standby letter of credit transactions) and thereby overcomes the implication that the purpose of the certificate is to give the buyer a fraud defence to a claim for payment under the credit. Furthermore, the warranty relieves the buyer from the sometimes burdensome proof problems in his action for damages against a seller who has obtained payment under the credit with latently defective documents.

4.1.1. The Nature of the Warranty

4.1.1.1. "Conditions of the Credit"

To understand the nature of the warranty, first of all, knowing the meaning behind the term "conditions of the credit"¹¹⁵ is vital, since only under those "conditions" should the warranty apply. In letter of credit law, that term signals the independence principle, i.e. the concept that the credit and the transaction, out of which it grows, are independent.¹¹⁶ It is of utmost importance that the warranty does not extend to

¹¹² See the beneficiary's duty of warranty under § 5-111(1) when it transfers or presents the documents. See also Dolan, J.F., 'Letters of Credit, Article 5 Warranties, Fraud, and the Beneficiary's Certificate' 41 *The Business Lawyer* (1986) 347 at 351.

¹¹³ Dolan, *supra* note 112 at 347. See also, Ballen, R., and Diana, N., 'UCC Article 5 (Letters of Credit)', 45 *The Business Lawyer* (1990) 1521, at 1590; Givray, A.J.; Chapman, C.J.; Doub, J.C; Gabriel, H.D; Hisert, G.A; Luttrell, R.T., III; Wunnicke, B., *supra* note 55 at 1682; Barnes, J.G., and Byrne, J.C., 'Letters of Credit: 1995 Cases' 51 *The Business Lawyer* (1996) 1417 at 1430.

¹¹⁴ The § 5-111(1) warranty runs to "all interested parties", which means people other than the account party can enforce the warranty. See also, Givray, 'Letter of Credit' 44 *The Business Lawyer* (1989) 1567, at 1651; Dolan, *The Law of Letters of Credit. Commercial and Standby Credits* p. (4-15).

¹¹⁵ UCC § 5-111(1) provides: "Unless otherwise agreed the beneficiary by transferring or presenting a documentary draft or demand for payment warrants to all interested parties that the necessary conditions of the credit have been complied with. This is in addition to any warranties arising under Article 3, 4, 7 and 8.

¹¹⁶ In an American case of *Wichita Eagle & Beacon Publishing Co v Pacific Nat'l Bank*, 493 F.2d 1285, 1286 (9th Cir. 1974), it was noted that: "the basic purpose of letters of credit [is] ... providing a

the “condition of the underlying transaction”.¹¹⁷ (See Appendix D, Section (5), for more on ‘warranty’ under the revised Article 5 of the UCC).

The seller’s warranty, under article 5, does not extend to obligations under the sales agreement between himself and the buyer.¹¹⁸ Section 5-111 relates only to the beneficiary’s (seller’s) obligations under the credit. The obligations under the credit, imposed on the seller, may be harsher or less harsh than the ones under the sales contract depending on each individual case.¹¹⁹ The buyer will often stipulate that the seller should present a commercial invoice, bill of lading, certificates of origin and insurance, and a draft in negotiable form. The seller may not have any obligation under the sales contract to provide some of those documents to the buyer, but the seller must tender those documents to the bank (the issuer of the credit) in order to fulfill his obligations under the credit, and thus to get paid.¹²⁰ This independency of the letter of credit is dealt with under section 5-114(1) of the UCC and Article 3 of

means of assuring payment cheaply by eliminating the need for the issuer to police the underlying contract.” Because the letter of credit is independent of the underlying transaction, it can operate quickly to achieve payment and can avoid involving the issuer in underlying contract disputes. Without the independence principle, the letter of credit would be simply a surety arrangement. “If a conforming presentation of documents is made, the issuer of a credit is obligated to pay without reference to the rights and obligations of the parties to the underlying contract.” *Republic Nat’l Bank v Northwest Nat’l Bank*, 578 S.W.2d 109, 114 (Tex. 1978) (holding that the independence principle distinguished a bank letter of credit from an impermissible bank surety contract). “[I]t is important to stress that the letter of credit arrangement is completely independent of the underlying contract between the beneficiary of the letter of credit and the issuing bank’s customer who has procured the letter of credit.” *New York Life Ins. Co. v Hartford Nat’l Bank & Trust Co.*, 173 Conn. 492, 498-99, 378 A.2d 562, 566 (1977) (holding that a defence to the underlying contract is no defence in the letter of credit transaction). See Dolan, *supra* note 112 at 347.

¹¹⁷ This is supported by the independence principle. See *Overseas Trading Corp. v Irving Trust Co.*, 82 N.Y.S.2d 72 (Sup. Ct. 1984); *Imbrie v D. Nagase & Co.*, 196 AD 380, 187 NYS 692 (1921); *Bank of East Asia, Ltd. v Pang*, 140 Wash. 603, 249 P.1060 (1926). See also, Dolan, *The Law of Letters of Credit. Commercial and Standby Credits* p. (9-57).

¹¹⁸ Givray, *supra* note 114 p. 1567, at 1652: “By seeking payment under the letter of credit, beneficiary warrants that the ‘necessary conditions of the credit have been complied with’ (UCC § 5-111) Does beneficiary warrant that all the ‘conditions’ of his own performance have been met in the underlying contract with customer? No, most would agree that § 5-111(1) refers to the ‘conditions’ (requirements) of the letter itself, *not* to conditions of the customer-beneficiary contract. This accords squarely with the independence principle, which isolates the letter of credit from all underlying deals.”

¹¹⁹ In commercial credit transactions, for instance, the sales agreement may call for a confirmed letter of credit and may make no reference to the documents the credit will require. See Dolan, *supra* note 112 at 348.

¹²⁰ See the American authority, *AMF Head Sportswear, Inc. v Ray Scott’s All-American Sports Club*, 448 F. Supp. 222 (D. Ariz. 1978). See Dolan, *supra* note 112 at 348.

the UCP.¹²¹

4.1.1.2. Patent and Latent Defects

Secondly, it is important to distinguish patent defects from latent defects in the documents. When applying the independence principle to the seller's (beneficiary's) warranty, the rules for the banker's examination of the seller's documents are presumably employed. The UCC (5-109) requires the banker to examine the documents to see if, on the face of it¹²², they comply with the terms of the credit. Bank document examiners are only competent to decide the facial conformity of the documents not the *de facto* compliance¹²³, and the UCC excuses them from having to do so.¹²⁴ The bank's duty to examine the documents, according to above section, puts the buyer at risk. One of the critical features of the credit is that it provides for prompt payment and thus promotes commercial efficacy. In other words, to require the document examiner to determine whether documents are genuine, where he has a duty to discover latent defects, would utterly jeopardise that critical feature. The warranty, which is imposed by the Code, is to let the buyer (the account party) have an unfailing remedy in the event of latent defects. The warranty requires the seller's documents to comply with the terms of the credit, not just on their face, but in fact. The buyer may be entitled to obtain damages (under the seller's warranty), if the bank pays against an invoice in which the goods are not properly described¹²⁵ or against a document which does not have the a required signature.¹²⁶ However, the

¹²¹ The leading American case on this point is *Maurice O'Meara Co. v National Park Bank*, 239 NY 386, 146 NE 636 (1925). It was held that the issuer cannot refuse payment under a letter of credit even though it has reason to believe that the goods shipped pursuant to the underlying contract were defective and even though the issuer might have an interest in those goods. See Dolan, *supra* note 112 at 348.

¹²² UCC § 5-109(2). See Appendix C for the related section 5-109(a) for update.

¹²³ See *Board of Trade v Swiss Credit Bank*, 728 F.2d 1241 (9th Cir. 1984).

¹²⁴ UCC § 5-109, cmt 2: "The fact that the documents may be false or fraudulent or lacking in legal effect is not one for which the issuer is bound to examine."

¹²⁵ UCP Article 41(c) requires the commercial invoice submitted under a credit to describe the goods as they are described in the credit.

¹²⁶ See, e.g., *Eximetals Corp. v Pinheiro Guimares, SA*, 73 AD 2d 526, 422 NYS 2d 684 (1979), *aff'd*, 51 NY 2d 865, 414 NE 2d 399, 433 NYS 2d 1019 (1980).

issuer will be free from liability if it pays in good faith against a false invoice or a forged document.¹²⁷

Patent defects often exist in a seller's document. The banker should obtain the buyer's (the account party's) waiver of the defects or notify the sellers of the defects and return the documents to or hold them for the sellers.¹²⁸ Very often, the buyer will waive a defect and the banker will pay the seller without mentioning the waiver to the seller.¹²⁹ If the seller is not informed about the defects promptly, the banker is arguably estopped to assert them.¹³⁰ If the banker pays, it is natural and thus justifiable for the seller to assume either that the presentation was conforming or that patent defects have been waived. In an American case, which was later considered as an "unfortunate decision"¹³¹, the defects of the documents that the sellers presented could be spotted without any extrinsic investigation, i.e. the defects were patent. The Fifth Circuit held that the beneficiary's warranty extends to patent defects, which is contrary to the position of the Code and industry practices for document examination, and which state that the duty of detecting patent defects should be on the bank (the credit issuer). Dolan is of the opinion that section 5-111(1) warranty "relates only to the performance of the credit transaction, not the underlying transaction, and that it covers defects in the documents that are latent, not patent"¹³².

¹²⁷ See UCC § 5-109, cmt 2.

¹²⁸ See UCC § 5-112, cmt 2; UCP., art 16(d).

¹²⁹ See Dolan. *supra* note 112, at 347, n.14.

¹³⁰ See UCP Art.16(e). Most of the cases require a showing of detrimental reliance on the issuer's silence before they will invoke an estoppel rule under the Code. See, e.g., *United Commodities-Greece v Fidelity Int'l Bank*, No. 513 (NY Apr 4, 1985); *cf. Bank of Cochin Ltd. v Manufacturers Handover Trust Co.*, No. 83 Civ. 1767 (JMC) (SDNY July 9, 1985) (adopting a similar rule for credits subject to the 1974 version of the Uniform Customs).

¹³¹ *Philadelphia Gear Corp v Central Bank* 717 F.2d 230 (5th Cir. 1983) Dolan, *supra* note 1112 at 350. Dolan commented (at p.351) that this case "stands the beneficiary-issuer relationship on its head ... The court did not give adequate weight to the efficiencies the Code, the Uniform Customs, and credit practices have achieved."

¹³² Dolan, *supra* note 112 at 351.

The proper functioning of letters of credit depends on prompt payment under them, when seller's documents are well in order, otherwise they will lose their economic viability. Although courts are well aware of the high costs of fraud in the commercial sphere and concerned about the credit being a device for perpetrating fraud, they are not in a position to know the validity of the buyer's claim of fraud, and usually reluctant to entertain the fraud defence of a bank or of a buyer seeking to enjoin honour of the credit. The fraud inquiry entails considerable time for extensive investigation¹³³. If courts routinely delay honour of a credit until the parties have litigated the fraud issue, then the credit cannot serve as an efficient commercial device. If banks are to investigate into fraud claims concerning letters of credit, this would jeopardise the two main functions that the credit serves. Namely, (i) the forum-shifting function and (ii) the litigation cost-shifting function. With regard to the former, one of the main reasons why the seller insists on a letter of credit is to ensure that they are paid prior to any disputes in the underlying contract commencing. With regard to the latter, it is to ensure that the buyer will have to start that action. Very often, parties to a sale contract are located in distant forums. This demonstrates that the buyer will have to bring an action in the seller's forum, "in which the court has jurisdiction of the seller, rather than that of the buyer".¹³⁴ Yet, courts have fabricated an important threshold for this kind of equitable relief. As a general rule, before the buyer can be granted an injunction against honour of the credit, he must demonstrate that he has no adequate remedy at law.¹³⁵

¹³³ See *Dynamics Corp. of Am v Citizens & S. Nat'l Bank*, 356 F. Supp. 991 (ND Ga 1973); *Intraworld Indus., Inc. v Girard Trust Bank*, 461 Pa. 343, 336 A.2d 316 (1975).

¹³⁴ Dolan, *supra* note 112, n.41 p. 356.

¹³⁵ See, e.g., *Enterprise Int'l, Inc v Corporacion Estatal Petrolera Ecuatoriana*, 762 F.2d 464 (5th Cir. 1985); *Warner v Central Trust Co.*, 715 F.2d 1121 (6th Cir. 1983); *KMW Int'l v Chase Manhattan Bank, NA*, 606 F.2d 10 (2d Cir. 1979); *Foreign Venture Ltd. Partnership v Chemical Bank*, 59 App. Div. 2d 352, 356, 399 NYS2d 114, 116 (1977); See also Harfield, H., 'Identity Crises in Letter of Credit Law' 24 *Arizona Law Review* (1982) 239 at 251: "if the account party (applicant for the injunction) seeks the remedy in the context of a commercial dispute with the beneficiary, e.g., a claim for breach of contract, the injunction will not issue."

4.2. Seller's Duty to Claim Payment From the Bank

In accordance with the contract of sale, it is stipulated that payment should be made by the provision of a letter of credit. In applying this to practice, the seller would therefore have to initially, claim payment from the banker, however, his right to claim payment directly from the buyer is conditional upon him first presenting the documents rejected by the banker.¹³⁶ If the seller fails in his duty in providing the appropriate documentation to the banker, he is then accountable for the loss of security in relation to the payment by credit. Consequently, the buyer is also relieved from his duty to pay¹³⁷.

In situations where the confirming banker refuses documents tendered by the seller under a confirmed credit, the question which arises is whether or not the seller should claim payment from the buyer or whether he should initially offer the documents to the issuing banker. This position has to date, not been determined. It has been claimed by Benjamin¹³⁸, however, that both the confirming bank and the issuing bank, work in collaboration, whereby the confirming bank acts as the agent, and that any decision made by the confirming bank, can be considered by the seller, as the final.

5. The Buyer's Rights

5.1. Buyer's Remedies Upon Realisation that the Seller has Tendered False Documents

Once the bank discharges the credit, in most cases this would result in the termination of the transaction. Regardless of the application of the independency rule¹³⁹, the bank's payment [honouring] of the credit, does not in all cases, infer that mutual rights and duties of the parties to the underlying contract are discharged. The buyer is therefore entitled to bring an action in deceit, or in cases where the

¹³⁶ See *Benjamin's Sale of Goods*, at § 23-078 p 1690, n 46.

¹³⁷ *Ibid*, n 47; See also Ventris, F., *supra* note 12 at 42.

¹³⁸ See *Benjamin's Sale of Goods*, at § 23-155 p 1733.

¹³⁹ *Benjamin's Sale of Goods*, § 23-120 p.1712.

contract has been breached, where it is evident that the seller has presented forged documents¹⁴⁰. Thus, the buyer can utilise a quasi-contractual action, based on total failure of consideration, as a tool to sue the seller in cases where documents are regarded as 'waste paper'¹⁴¹.

5.2. Buyer's Right to Repudiate the Contract of Sale Upon Failure of the Seller to Tender the Required Documents

If the seller fails to tender the required documents, the buyer is entitled to repudiate the contract of sale and to reject the goods as decided in the case of Shamsher Jute Mills v. Sehtia (London)¹⁴². In this case, it was a provision in the sale contract that the seller was to tender a set of documents complying with the terms of the irrevocable credit opened at the buyer's request. When the seller failed to present the bank with the required documents, it was held that since the seller failed to tender the required documents, he was not only refused entitlement to have the credit honoured, but he was also unable to recover the price from the buyer.¹⁴³

Notwithstanding that there was no evidence to show that the goods were defective.

6. Short-Circuiting and Conditional/Absolute Payment¹⁴⁴

6.1. No Short-Circuiting of Credit

Given the mutual nature of the credit, it is not open to the seller to short-circuit the credit by tendering the documents directly to the buyer and demanding payment directly from him. In the case of Soproma S.P.A. v. Marine & Animal By-Products Corporation¹⁴⁵, the sales contract (of fishmeal c. & f.) stipulated that payment was to be made by an irrevocable letter of credit. The bank rejected the first tender of

¹⁴⁰ See, eg *Famouri v Dialcord Ltd* (1983) 133 NLJ 153.

¹⁴¹ *Benjamin's Sale of Goods*, at § 23-090 p. 1696.

¹⁴² *Shamsher Jute Mills v. Sehtia (London)* [1987] 1 Lloyd's Rep 388; See also *Darg Offshore Ltd v Emerald Field Contracting Ltd* [1992] 2 Lloyd's Rep 142 at 155.

¹⁴³ *Shamsher Jute Mills v. Sehtia (London)* [1987] 1 Lloyd's Rep 388, 393.

¹⁴⁴ Jack ,R., *Documentary Credits*, at § 5-17 p. 84; Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 73.

¹⁴⁵ *Soproma S.P.A. v. Marine & Animal By-Products Corporation* [1966] 1 Lloyd's Rep. 367. See Schmitthoff, C.M., *Schmitthoff's Export Trade: The Law & Practice of International Trade* 9th ed (London, Stevens & Sons, 1990) p. 439.

documents following valid instruction from the buyers. The sellers made a second tender directly to the buyers but the buyers refused to accept the documents. McNair J. held that the buyers were entitled to do so, because the presentation of documents directly to the buyer were not valid.¹⁴⁶ In his course of delivering judgment, his Honour observed that:

“It seems to me to be quite inconsistent with the express terms of a contract such as this to hold that the sellers have an alternative right to obtain payment from the buyers by presenting the documents direct to the buyers. Assuming that a letter of credit has been opened by the buyer for the opening of which the buyer would normally be required to provide the bank either with cash or some form of authority, could the seller at his option disregard the contractual letter of credit and present the documents direct to the buyer? As it seems to me, the answer must plainly be in the negative”.¹⁴⁷

Todd’s analysis of McNair J.’s decision suggests that it was advantageous to both parties when payment was made by documentary credit, and that it was not a right unique to the seller which he could “unilaterally waive”.¹⁴⁸ McNair J. said:

“[Documentary credit is] of advantage to the seller in that by the terms of the contract [of sale] he is given... ‘a reliable paymaster’ generally in his own country whom he can sue, and of advantage to the buyer in that he can make arrangements with his bankers for the provision of the necessary funds, his banker retaining the drafts and the documents as his security for making payment to the seller and the buyer being freed from the necessity of having to keep the funds available to make payment against presentation of documents to him at an uncertain time which is no further defined in the authorities [on c.i.f. contracts] than being at a reasonable time after shipment by the seller of documents covering goods which he has shipped or are already afloat.”¹⁴⁹

That is to say, if the seller is to be allowed to short-circuit the credit, the result would be unfair as the buyer would be denied his advantages of the credit, while the seller is still allowed to retain his.¹⁵⁰ McNair J. continued:

“Under this form of contract, as it seems to me, the buyer performs his obligation as to payment if he provides for the sellers a reliable and solvent paymaster from whom he can obtain payment-if necessary by suit- although it may well be that if the banker fails to pay by reason of his insolvency the buyer would be liable; but in such a case, as at present advised, I think that the basis of the liability must in principle be his failure to provide a proper letter of credit which involves (inter alia) that the obligee under the letter of credit is financially solvent. (This point as to the buyer’s liability for the insolvency of the bank was not fully argued before me and I prefer to express no concluded opinion upon it as I

¹⁴⁶ Another reason for the tendering of documents being invalid in that case was that the presentation was outside the time stipulated in the credit.

¹⁴⁷ *Soproma S.P.A. v. Marine & Animal By-Products Corporation* [1966] 1 Lloyd’s Rep. 367, at 386.

¹⁴⁸ Todd, P., *Bills of Lading & Bankers’ Documentary Credits* p. 73.

¹⁴⁹ [1966]1 Lloyd’s Rep. 367, 385 (col. 2).

¹⁵⁰ Todd, P., *Bills of Lading & Bankers’ Documentary Credits* p.73.

understand that it may arise for decision in other cases pending in this Court.)”¹⁵¹ It is a common practice, in some parts of the world (e.g. India), for credits to involve drafts drawn on the applicant¹⁵², and it is also apparent that they appear not to function any better in practical terms than a draft drawn on a bank. It is, moreover, proposed that it would be undesirable to introduce a draft drawn by either the beneficiary or the applicant, within the operation of the credit, which aims to act as a source of obligation between them. In accordance with the 1993 Revision, it is provided therefore, that the credit should not be drawn on the applicant¹⁵³. It is clear that upon a credit being issued and which allows a draft to be drawn on an applicant, problems surface. Articles 9 (a) (iv) and 9 (b) (iv) of the UCP state that if this situation happens, such documents will be perceived as additional documents, on the part of the bank. It is provided that banks are presumed to regard the document as a draft, to be offered in conjunction with other documents required by the credit. However, it should not be perceived to be involved in any component of the payment system or being involved in any of the bank’s obligations¹⁵⁴. Sometimes, the banks may have to further consider the term of the credit provided for drafts on applicants. An example which demonstrates how Article 10(b)(iii) in the 1983 Revision was applied, is evident in the case of Forestal Mimosa Ltd. v. Oriental Credit Ltd¹⁵⁵. The basis on which the defendant bank was believed liable, was that the bills, which had been drawn on the buyers, had not been accepted by them.¹⁵⁶

¹⁵¹ [1966]1 Lloyd’s Rep. 367, 385 (col. 2).

¹⁵² The 1983 Revision Articles 10.a.iii and 10.b.iii provided for this kind of drafts. See Jack, R, *Documentary Credits*, at § 5.17 p. 84.

¹⁵³ Article (9)(a)(iv) and (9)(b)(iv) makes it clear that the credit should not be drawn on the applicant.

¹⁵⁴ Jack, R, *Documentary Credits*, at § 5.17 p. 84.

¹⁵⁵ *Forestal Mimosa Ltd. v. Oriental Credit Ltd* [1986] 1 WLR 631.

¹⁵⁶ *Ibid* at 632.

6.2. The Seller's Right of Recourse When he Cannot Obtain Payment From the Bank and the Issue of Whether Payment by Letter of Credit is Conditional or Absolute. Possible Conflict With the Independency Principle

If the seller is unable to obtain payment from the issuing bank in the case of a confirmed credit or either the confirming or issuing banks for non-confirmed credit, the crucial question faced by the seller is whether he has a right of recourse against the buyer.

The answer to the above question depends on the following conditions:

- “(i) the reason for which the seller is unable to obtain payment;
- (ii) the drafting of the ‘payment’ clause in the main contract between buyer and seller”.¹⁵⁷

6.2.1. Whether the Seller has a Right of Recourse?

6.2.1.1. The Reason for Which the Seller is Unable to Obtain Payment

If the seller is unable to tender the required documents or is late in presenting them, then he has no right of recourse against the applicant for the credit. The seller has no real grounds for complaint since he has himself breached the contract, in which he is obliged to tender the very documents prescribed by the “credit”.¹⁵⁸ In fact, “he will be no worse off than he would have been under the rules of the common law had he sold c.i.f. or f.o.b. on the basis of payment by the seller by telegraphic transfer on reception of the relevant documents”.¹⁵⁹ Then, does this mean that a seller (beneficiary under a credit arrangement) should be better treated than he would be if there were no credit, when there is a question of tendering the correct documents? If the seller proves that he has tendered exactly the required documents, but the bank, being unreasonable, rejected them, the bank should be regarded as in breach of its obligations. In such instances, it is open to the seller to

¹⁵⁷ Ventris, F.M., *Bankers' Documentary Credits*, 3rd ed (Lloyd's of London Press Ltd, 1990) pp. 85-86.

¹⁵⁸ *Soproma S.p.A v Marine and Animal By-Products Corporation* [1966] 1 Lloyd's Rep. 367, 385, per McNair J.

¹⁵⁹ Ventris, *Bankers' Documentary Credits* p. 86.

dispose of the goods at the best price he can, in order to mitigate his loss, and then an action against the bank for its breach of contract may be followed.¹⁶⁰

This is, however, a lengthy, expensive and unreliable process. The seller can therefore, in practice, appeal to the buyer (the applicant of the credit).¹⁶¹ “This is of course an extra-contractual action”.¹⁶² However, if the buyer requires the materials or goods urgently, he may nonetheless be prepared to waive the non-conformity in the documents and instruct the bank to accept the documents. Nowadays, for commercial efficacy, the practice is usually that the confirming bank, upon finding trivial discrepancies, would consult the issuing bank as to whether it should accept such documents. The issuing bank will then naturally repeat such messages to the buyer.¹⁶³

An example of a trivial irregularity is where the seller’s commercial invoice was made out to “ABC” instead of “ABC Ltd.”, and the issuing bank refused to pay. The case would be considered worse if the seller had already lost physical control of the cargo, where it had been discharged into the buyer’s storage without production of the bill of lading. What the seller can do is either start an action for breach of contract against the bank, but that would be quite time consuming and difficult; alternatively, he can appeal to the buyer for the payment. The buyer in this kind of case, can often delay the payment for a few months and thus take the advantage of the most trivial of irregularities.¹⁶⁴

6.2.1.2. The Drafting of the ‘Payment’ Clause in the Main Contract Between Buyer and Seller

Another circumstance when the seller would like to have recourse is where the bank is unable to pay, i.e., they have stopped payment. The possibility of the seller’s recovery of payment on the banker’s default depends upon the interpretation of the

¹⁶⁰ Ibid. 87.

¹⁶¹ Ibid.

¹⁶² Ibid

¹⁶³ Ibid.

¹⁶⁴ Ventris, *Bankers’ Documentary Credits* p. 87.

payment clause in the sales contract: whether the buyer's procurement of the letter of credit is "absolute payment" or "conditional payment" of the purchase price.¹⁶⁵ Normally, the contract is silent on that specific issue, and therefore it will be a matter of deduction for a court or arbitrator, to determine what the intentions of the parties should be taken to be in all circumstances.¹⁶⁶

It is a principle of letter of credit law that the letter of credit is completely independent of the underlying sale of goods contract, which supports the view that payment by credit is absolute. Where a credit is absolute payment and is correctly established or is accepted by the seller, the seller would normally have no rights against the buyer if the seller presents conforming documents but nonetheless remains unpaid. His only remedy is against the bank or banks. There may be two exceptions to this. Firstly, if the buyer induces the banks not to pay, the buyer may be liable for inducing breach of contract, depending on his appreciation that a breach was involved. Secondly, if the buyer has received the goods, this may give rise to remedies against him. So far no case has touched on the problem of what should happen if the bank fails before the documents could be tendered. The analysis presented here does not read terms from the sale of goods contract into the letter of credit, but asks how the letter of credit should be interpreted, to give a certain result under the sale of goods contract.

Where the effect of the payment clause is that the buyer has taken the contractual obligation that he will have a credit issued which will permit the seller to obtain payment, if he tenders the prescribed documents in time, then this is a double engagement that:

- (i) he will have the "credit" issued; and
- (ii) if the seller fulfils his own contractual obligations, i.e. to tender the specified

¹⁶⁵ *W J Alan & Co v El Nasr Export and Import Co* [1972] 2 Q.B. 189.

¹⁶⁶ *Re Charge Card Services Ltd.* [1987] Ch 150 at 165 et seq (Millett J) and [1989] Ch 497 at 511-512. (CA).

documents, then he will definitely get his money.¹⁶⁷

Which sounds exactly like payment by credit is conditional, i.e. if the seller does fulfill the obligations and nonetheless fails to obtain payment from the banks, then the buyer is in breach of his contractual undertaking. In fact, it is well established that the opening of credit does not discharge the buyer's obligation to pay.¹⁶⁸ In the leading case of Newman Industries Ltd v. Indo-British Industries¹⁶⁹, where the plaintiffs were to supply a generator through an intermediary (Indo-British, the defendant) to Govindram Brothers Ltd., in India, the Queen's Bench held that the defendant's procurement of a letter of credit was merely a conditional payment, and implied that the absence of any express terms to the contrary in the sale of goods contract, indicated the parties' intent not to vary the prevalent trade custom. Furthermore, the court stated that very clear contractual provisions would be necessary for the letter of credit to constitute absolute payment.¹⁷⁰

It was suggested by the High Court of Australia, that this was specific to situations involving credits which were revocable and 'irrevocable but unconfirmed', but that confirmed credits were excluded. This distinction is pretty hard to appreciate, since the only difference between a 'confirmed' and an 'irrevocable but unconfirmed' credit is that, in the first instance, the seller is assured payment by both banks, unlike in the other, where the seller can only be assured of payment by the issuing bank.

Lord Denning¹⁷¹ M R. endeavoured to address this issue, with specific reference to

¹⁶⁷ Ventris, *Bankers' Documentary Credits* p. 88.

¹⁶⁸ Gutteridge and Megrah, *The Law of Bankers' Commercial Credits*, (Europa Publications Ltd., 1984,) p.35 et seq.

¹⁶⁹ *Newman Industries Ltd v Indo-British Industries* [1956] 2 Lloyd's Rep 219; [1957] 1 Lloyd's Rep 211; See also *Soproma S.p.A. v Marine and Animal By-Products Corporation*, *supra*. In the U.S.A. see: *Lamborn v Allen Kirkpatrick*, 135 A 541 (1927); *Greenough v Munroe*, 53 F. 2d 362 (1931).

¹⁷⁰ *Newman Industries Ltd v Indo-British Industries* [1956] 2 Lloyd's Rep 219, 236.

¹⁷¹ *WJ Alan & Co v El Nasr Export and Import Co* [1972] 2 Q.B. 189.

normal circumstances, where there was agreement by both parties, by stating that; “when the contract of sale stipulates for payment to be made by confirmed irrevocable letter of credit, then when the letter of credit is issued and accepted by the seller, it operates as a conditional payment of the price. It does not operate as absolute payment”.¹⁷² He went on to say that “if the letter of credit is honoured by the bank when documents are presented to it, the debtor is discharged. If it is not honoured the debt is not discharged”.¹⁷³

It is evident when examining certain documentary credits, that the banker prefers to accept a draft payable within a specified period of time, after sight, instead of assuring cash payment or honouring a sight draft¹⁷⁴ It can be illustrated, from reviewing specific cases, that the buyer is not relieved, irrespective of whether the bank actually accepts such a draft, and the seller remains entitled to request payment from the buyer in cases where the draft is dishonoured by the banker. In this case the buyer may find that he has to pay twice, to both the seller and then to the issuing bank¹⁷⁵. Although such practice appears to be unusual, in reality it is more common than actually perceived¹⁷⁶.

¹⁷² Ibid at 212.

¹⁷³ Ibid.

¹⁷⁴ *Benjamin's Sale of Goods*, at § 23-080 p. 1691.

¹⁷⁵ The court may, however, release the buyer from any obligation assumed by him towards the defaulting issuing banker. See *Sale Continuation Ltd v Austin Taylor & Co. Ltd.* [1968] 2 Q.B. 849; see also the American case, *Vivacqua Irmaos, SA v Hickerson* 193 La. 195, 190 So. 657 (1939), where the court held that “to hold defendant (buyer) liable to plaintiff (seller) under these circumstances (insolvency of the bank) would force defendant to pay a second time for coffee which defendant has already paid for in accordance with the custom of trade and as contemplated by the parties under the terms of their contract.” (at 503, 190 Sp. At 659).

¹⁷⁶ In the case of *Donne v Cornwall* back in 1485, the defendant had signed a bond for money he owed to the plaintiff. Having paid his debt and having the bond back, the defendant forgot to destroy the bond, which came again into the hands of the plaintiff by some devious means. The plaintiff sued on the bond and the court held that the defendant had to pay again. A verbal statement that he had already repaid the money, even if it were truthful, cannot strike down the existence of the bond. See Ventris, *Bankers' Documentary Credits* p. 89.

In W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co.,¹⁷⁷ a non-conforming letter of credit was opened. One of the discrepancies of it was that it provided for payment in U.K. sterling rather than Kenyan currency. Since the bank failed to meet its obligations, the Court of Appeal held that the seller could claim payment from the buyer directly, unless express provision to the contrary was made in the contract of sale. Regarding this case, it was said to be a conditional, rather than an absolute payment of the price.¹⁷⁸ Lord Denning M.R. said:

“In my opinion a letter of credit is not to be regarded as absolute payment, unless the seller stipulates, expressly or impliedly, that it should be so. He may do it impliedly if he stipulates for the credit to be issued by a particular bank in such circumstances that it is to be inferred that the seller looks to that particular banker to the exclusion of the buyer... If the letter of credit is conditional payment of the price, the consequences are these: The seller looks in the first instance to the banker for payment: but if the banker does not meet his obligations when the time comes for him to do so, the seller can have recourse to the buyer. The seller must present the documents to the banker. One of the two things may then happen: (1) the banker may fail or refuse to pay or accept drafts in exchange for the documents. The seller then, of course, does not hand over the documents. He retains dominion over the goods. He can resell them and claim damages from the buyer. He can also sue the banker for not honouring the credit: see Urquhart Lindsay & Co. Ltd. v Eastern Bank Ltd.¹⁷⁹ But he cannot, of course, get damages twice over. (2) The bank may accept time drafts in exchange for the documents, but may fail to honour the drafts when the time comes. In that case the banker will have the documents and will usually have passed them on to the buyer, who will have paid the bank for them. The seller can then sue the banker on the drafts: or if the banker fails or is insolvent, the seller can sue the buyer. The banker’s drafts are like any ordinary payment for goods by a bill of exchange. They are conditional payment, but not absolute payment. It may mean that the buyer (if he has already paid the bank) will have to pay twice over. So be it. He ought to have made sure that he employed a ‘reliable and solvent paymaster’.”¹⁸⁰

Similarly, the Queen’s Bench adopted the same view in Maran Road Saw Mill v. Austin Taylor Ltd¹⁸¹. Here, upon failure by the issuing bank, the seller succeeded in an action against its agent, whose position was of a buyer under the commercial credit. Ackner J. said:

“Can it then be said that [the defendants] have discharged their contractual obligation, when, although they have established a letter of credit, payment has not been made under it? To my mind, the answer is a simple one and is in the negative. I respectfully adopt

¹⁷⁷ *W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co* [1972] 2 Q.B. 189 at p. 220.

¹⁷⁸ Similarly, see the case of *Greenough v Munroe* (53 F.2d 362 (2nd Cir. 1931), cert. Denied, 284 US 672 (1931)).

¹⁷⁹ *Urquhart Lindsay & Co. Ltd. v Eastern Bank Ltd* [1922] 1 K.B. 318.

¹⁸⁰ *W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co* [1972] 2 Q.B. 189 at p. 210.

¹⁸¹ *Maran Road Saw Mill v. Austin Taylor Ltd* [1975] 1 Lloyd’s Rep. 156.

and slightly adapt the language used by Stephenson L.J. in W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co.¹⁸² The agents promised to pay by letter of credit not to provide by a letter of credit a source of payment which did not pay.”¹⁸³

Todd has submitted that the principles set out in the above mentioned cases of El-Nasr and Maran Road create only a “rebuttable presumption”.¹⁸⁴ Thus, it is open to the courts to decide, according to the surrounding circumstances, whether the credit is to be regarded as absolute rather than conditional payment.

However, some authorities have taken the view that the seller could be regarded to have impliedly stipulated that the credit payment is to be absolute. This is so if the seller “stipulates for the credit to be issued by a particular bank, in such circumstances that it is to be inferred that the seller looks to that particular banker to the exclusion of the buyer”.¹⁸⁵ McNair J. in the case of Soproma S.p.A v. Marine and Animal By-Products Corporation¹⁸⁶, was of the view that, only in the event of the issuing bank’s insolvency, may the seller be able to tender documents to the buyer directly. Normally, the choice of issuing bank is left to the buyer, and therefore the seller should not be required to take the consequences of its failure.¹⁸⁷

Also, in the case of E.D. & F. Man Ltd. v. Nigerian Sweets & Confectionery Co. Ltd.,¹⁸⁸ the buyer argued that the opening of the credit should be treated as absolute payment because the sellers had agreed on the identity of the issuing bank. In this case, the issuing bank went into liquidation after being reimbursed and before payment had been made to the seller under 90-day drafts drawn on it. The seller sued the buyers directly instead. Ackner J. was of the opinion that the buyers were

¹⁸² *W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co* [1972] 2 Q.B. 189 at p. 220.

¹⁸³ *Maran Road Saw Mill v. Austin Taylor Ltd* [1975] 1 Lloyd’s Rep. 156, 159 (col. 1).

¹⁸⁴ Todd, P., *Bills of Lading & Bankers’ Documentary Credits* p. 75.

¹⁸⁵ [1972] 2 Q.B. 189, at p. 220 (per Lord Denning, M.R.). See also *Soproma S.p.A v Marine and Animal By-Products Corporation* [1966] 1 Lloyd’s Rep 367, where the banker was chosen by the seller.

¹⁸⁶ *Soproma S.p.A v Marine and Animal By-Products Corporation* [1966] 1 Lloyd’s Rep 367.

¹⁸⁷ *Ibid* at 386.

¹⁸⁸ *E.D. & F. Man Ltd. v. Nigerian Sweets & Confectionery Co. Ltd* [1977] 2 Lloyd’s Rep. 50.

liable. He relied on Alan v. El Nasr¹⁸⁹, when he decided that the seller's agreement, as to choice of bank was merely one factor and not in any way conclusive:

"Mr Evans [for the buyers] sought to submit as a proposition of law, that where the identity of the bank is agreed between the parties, and not left to the choice of the buyers, it must follow that the sellers impliedly agree that the liability of the issuing bank has been accepted by them in place of that of the buyers. I do not think that this is correct. The fact that the sellers have agreed on the identity of the issuing bank is but one of the factors to be taken into account when considering whether there are circumstances from which it can be properly inferred that the sellers look to that particular bank to the exclusion of the buyer. It is in no way conclusive. In this case..., there were other circumstances which clearly supported the presumption that the letters of credit were not given as absolute payment but as conditional payment...

The sellers remedy in such circumstances is to claim from the buyers either the price agreed in the contract of sale or damages for breach of their contractual promise to pay by letter of credit."¹⁹⁰

In considering a situation where the seller, in selecting a specific bank, has made such a choice against the initial wishes of buyer, reference should be made to the American case of Vivacqua Irmaos SA v. Hickerson.¹⁹¹ In this case, with regards to the scenario mentioned above, it was acceptable, as long as the buyer had been perceived to have done all he could, by utilising the selected bank's services¹⁹². Moreover, it is a case whereby the selection of the issuing bank was effected by the seller, therefore, the presumption that a documentary credit constitutes conditional rather than absolute payment is rightly rebuttable in this case.¹⁹³ Such a conclusion is commercially sound as a buyer who is specifically required to utilise a bank, other than his usual bankers, may have to remit to that bank the required funds in advance or at least to provide a security, such as a back-to-back credit, of his own bank.¹⁹⁴ This view is against the prevailing line of the English authorities, however, it can be applied in relevant cases¹⁹⁵.

¹⁸⁹ *W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co* [1972] 2 Q.B. 189, he relied on the obiter dicta of Lord Denning M.R., at 210.

¹⁹⁰ *E.D. & F. Man Ltd. v. Nigerian Sweets & Confectionery Co. Ltd* [1977] 2 Lloyd's Rep. 50, 56.

¹⁹¹ *Vivacqua Irmaos SA v Hickerson* 190 So. 657 (1939).

¹⁹² *Ibid* at 659.

¹⁹³ It should be noted that the choice of bank is merely one factor, and is in no way conclusive. *E.D. & F. Man Ltd. v. Nigerian Sweets & Confectionery Co. Ltd* [1977] 2 Lloyd's Rep. 50, at 56.

¹⁹⁴ *Benjamin's Sale of Goods*, at § 23-088 p. 1696.

¹⁹⁵ *Ibid* at § 23-085 p. 1694.

The English decisions are based on attributing to the parties to the underlying sale of goods transaction, an intention to treat the furnishing of the documentary credit, and thus the subsequent acceptance of drafts, as conditional rather than absolute payment. But is this presumption rebuttable? As we have seen, the answer is that it is possible in some circumstances according to the judgment of Lord Denning M.R. in El Nasr case¹⁹⁶.

Conversely, the situation is clearer in cases concerning credit cards or charge cards. It has always been held that payment by credit cards constitutes absolute rather than conditional payment. The case of Re Charge Card Services Ltd.¹⁹⁷, illustrates this scenario. In this case, a company engaged in the issuing of credit cards went into liquidation. One of the issues was whether dealers, who had supplied goods or services to card-holders upon their executing a sales docket on which the details of their respective card were imprinted by the use of the dealer's machine, had the right to fall back on such holders when the company suspended payment.

Millet J. said, "the word 'pay', like the word 'payment', is ambiguous - it may refer to conditional or absolute payment - and its meaning in any given case cannot be determined merely by its use."¹⁹⁸ His Honour went on to talk about the distinction between a transaction involving the furnishing of a documentary credit and a credit card transaction. He said:

"the sole purpose of the letter of credit is to provide security to the seller to replace that represented by the shipping documents which he gives up in exchange of the credit ... By contrast, credit and charge cards are used mainly to facilitate payment of small consumer debts arising out of transactions between parties who may well not be known to each

¹⁹⁶ see *W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co.* [1972] 2 Q.B. 189, 210A. per Lord Denning. However, it should be noted that the choice of bank is merely one factor, and is in no way conclusive. *E.D. & F. Man Ltd. v. Nigerian Sweets & Confectionery Co. Ltd* [1977] 2 Lloyd's Rep. 50, at 56.

¹⁹⁷ *Re Charge Card Services Ltd* [1987] Ch 150, affd. [1989] Ch 497. See generally, Bridge, M.G., *The Sale of Goods* (Clarendon Press: Oxford, 1997) p. 34; *Benjamin's Sale of Goods*, at § 23-085 p. 1694.

¹⁹⁸ [1987] Ch 150 at p.168.

other, and the terms of which are not usually the subject of negotiation.”¹⁹⁹
 In his Honour’s view, the special type of credit card transaction was sufficient “not only to displace any presumption that, payment by such means [was] conditional payment only, but to support a presumption to the contrary.”²⁰⁰

When this case went to the Court of Appeal, as well as it being confirmed that payment by credit cards constituted absolute rather than conditional payment, a distinction was also made between payment by credit cards and letters of credit²⁰¹. Browne-Wilkinson V-C, referring to the above mentioned judgment of Lord Denning M.R. in El Nasr case, additionally emphasised, in the course of his judgment, that the presumption that payment by letter of credit was conditional may be rebutted. His Lordship commented that where the selection of the issuing bank was effected by the seller, the presumption that a documentary credit constitutes conditional rather than absolute payment is rebuttable. According to Sir Nicholas Browne-Wilkinson V-C :

“It is normally the buyer, not the seller, who selects the bank issuing the letter of credit: if, unusually, the seller does select the bank, this factor may rebut the presumption of conditional payment by letter of credit”.²⁰²

This is a good reason for holding the presumption that conditional payment may be rebutted. Nonetheless, the comparison of letter of credit as a conditional or absolute payment is, in fact, mainly of academic interest. The court has never been so rigid as to conclude that payment by letter of credit is an absolute payment.

6.3. Position on Banker’s Bankruptcy²⁰³

Real difficulties arise in cases of the banker’s bankruptcy, where the buyer has not yet paid the banker before its bankruptcy. However, according to Berger, if

¹⁹⁹ Ibid.

²⁰⁰ Ibid at 169.

²⁰¹ [1989] Ch, 497 at 516-517.

²⁰² [1989] Ch, 497 at 516.

²⁰³ See Jack, R, *Documentary Credits*, at § 3-43 et seq p. 54; Todd, P., *Bills of Lading & Bankers’ Documentary Credits* p.69. For Canadian position on this issue, see Sarna, ‘Letters of credit: Bankruptcy, Fraud and Identity of Parties’ 65-66 *Canadian Bar Review* (1986-87) 303 at 307; see also, Sarna, “*Letters of Credit: The Law and Current Practice*, 3rd ed., (Carswell, Canada, 1989), at § 2 p. (6-2).

payment by letters of credit is absolute, the result is;

“a loss to the seller equal to the difference between the sales price and the liquidating dividend. The general creditors of the bank would reap a benefit to the extent that the buyer’s payment of funds to the bank prior to the bank’s insolvency exceeds the pro rata liquidating dividend received by the seller as one general creditor”.²⁰⁴

However, where payment by letter of credit is conditional, neither the seller nor the buyer lose or gain anything and the seller can sue the buyer for breach of contract if he does not pay.

Sometimes the buyer places the issuing banker in funds before the seller is paid the amount of credit or honours a draft drawn under it. In this situation, if payment by letter of credit is absolute, the seller, as a general creditor, gets only the pro rata liquidating dividend. Whereas the buyer here, neither gains or loses anything, and the seller gets less than the contracted price. If however, payment by letter of credit is conditional, the seller does not gain or lose anything because he receives (partly from the bank and partly from the buyer), the entire purchase price for the goods shipped. The buyer has already pre-paid the purchase price to the bank, and now he will also have to pay almost the entire amount to the seller. See Chart 1, at the end of the Chapter, for detail.

It seems to be proper, because the buyer himself chose the bank to issue the letter of credit, and he should be in a better position to evaluate its financial soundness than the seller.²⁰⁵

6.4. Technical Defects in the Documents

Where technical defects are discovered within the documents, and the bank subsequently refuses to honour the credit, the issue which needs to be addressed is whether this permits the seller to have a direct recourse against the buyer.

In order to answer this question, we have to initially take into consideration the following two points. Firstly, what standard of compliance is to govern? Secondly, is payment by a letter of credit conditional or absolute? Upon the payment by a

²⁰⁴ Berger, S.R., ‘The Effects of Issuing Bank Insolvency on Letters of Credit’ 21 *Harvard International Law Journal* (1980) 161, at. 175.

²⁰⁵ See *ED. And F Man Ltd. v Nigerian Sweets and Confectionery Co. Ltd.* [1977] 2 Lloyd’s Rep 50.

letter of credit being determined as absolute, the seller would then have no direct right of claim against the buyer, in cases where the bank legitimately refuses payment. The bank is regarded as having legitimately refused payment if it has complied with the applicable compliance test. The matter between the seller and buyer is thus closed. But if the bank's reason for refusing payment was considered as unreasonable, i.e. rejection was contrary to the compliance standard test in place, then the seller may claim recourse against the bank.

Unlike the former situation, if payment by a letter of credit is conditional, then, there are two situations that need to be tackled. First, if the bank legitimately refused to pay, it would be absurd if the seller had recourse against the buyer. For example, supposing that the strict compliance standard was the adopted test, the bank's rejection of the documents on the grounds of technical defects would be in line with the requirements of such test. Secondly, if the bank wrongfully refuses to honour the credit, for example where the qualified strict compliance test is in place, under which trivial defects in the documents are tolerated, then the question which arises is whether the seller has a direct recourse against the buyer. Now, under conditional payment, the seller has a right to have recourse against the buyer if he, the seller, has exhausted all possible routes in order to recover his money from the bank. If the seller then fails, he would have a direct claim against the buyer.

7. Suggestions for Buyers and Sellers to Safeguard Their Interests

7.1. Seller's Protections

The commentaries²⁰⁶ suggest that the seller should protect himself by preparing a checklist that stipulates the conditions that the buyer should include in the letter of credit. Firstly, the port of export should be specified,²⁰⁷ and a precise description of the goods, preferably in the words of the seller, should be provided so that there

²⁰⁶ Samuel, H.A., 'Letter of Credit Can Protect Both Sellers and Purchasers' 401 *The Journal of Commerce and Commercial*, (Friday, Aug. 19, No. 28) (1994), 293 at 293; See also, Cooke, J.A., 'What You Should Know About Letters of Credit' 29 *Traffic Management* (1990) (No.9 Sept) 44, at pp. 47-52; Dolan, *The Law of Letters of Credit. Commercial and Standby Credits* pp (1-47), (1-48).

²⁰⁷ Samuel, H.A., 'Letter of Credit Can Protect Both Sellers and Purchasers' 401.

will be no confusion to the buyer. This enables the seller's normal invoice procedure to be followed. Further, it is also important to agree to the shipment date and 45-60 days period can be added to this. This flexibility in the shipment time should give the exporter an adequate time for the production and the shipment of the goods so that an extension will not be needed. It is important to agree on who will cover the insurance arrangement and costs. A simple sale term c.i.f., does not always make it clear. A seller is also advised to check the conformity between the full amount of the letter of credit and the other conditions. It happens sometimes in practice that a letter of credit includes only the merchandise value stated in it, but some other charges such as freight are ignored. It is noteworthy to specify in the credit itself, by whom the freight is to be paid and to agree on the consignment's destination. In addition, specification of the method of shipment, whether by air or surface from point of origin or port of export, is also important.²⁰⁸ Also, the seller is advised to request the letter of credit to be advised through his own bank, so that his account will be credited immediately and without delay. It is important for the seller to have the letter of credit reviewed by his banker to ensure its accuracy before shipping. It is also worth having it reviewed by the seller's freight forwarder, in order to confirm whether the terms of the credit are easy to meet.

For further protection, the seller must demand that the letter of credit be irrevocable so that the buyer cannot cancel the credit if the seller made the shipment, no later than the date as agreed in the sales contract.²⁰⁹ When dealing with a buyer from a foreign country, a wise seller should request the buyer to have the letter of credit confirmed by a bank in which the seller has confidence.

7.2. Buyer's Protections

Given the two functions that a letter of credit serves (the forum-shifting function²¹⁰ and the litigation cost-shifting function²¹¹, examined under section 4.1.1.2.), the

²⁰⁸ This must conform with the value of the letter of credit.

²⁰⁹ Ortmann, H.J., 'The Pitfalls of Letters of Credit' 92 *Business Credit*, Nov/Dec (1990) 24 at 24.

²¹⁰ Dolan, *The Law of Letters of Credit. Commercial and Standby Credits* p.(3-34).

²¹¹ See Note, 'The Trade Embargo and the Irrevocable Letter of Credit' 1 *Ariz J Int'l & Comp.L* (1982) 213

buyer is advised to follow certain safety measures to safeguard his interests. The buyer himself is advised to ask for a sale contract, which demands a letter of credit payable against an inspection certificate, to be carried out by an independent inspector.²¹² Further, the buyer is recommended to require the seller to procure the opening of a standby letter of credit, in order to be secured against the seller's defaults.²¹³ Moreover, a reduction in the purchase price to take account of the forum cost should be negotiated. It is also important that the buyer tries to agree to avoid funding the sale contract by a letter of credit. To safeguard his interests against seller's fraud, a buyer is required to insert detailed and complex conditions and documentary requirements in the credit itself.²¹⁴ In addition, the buyer is advised to use non-negotiable drafts (Bills of Exchange). In case of forgery of shipping documents, holders in due course can still recover from the issuer or confirming bank in spite of the fact that the documents were forged. By using such non-negotiable Bills of Exchange, the alleged holder in due course may fail to prove his status, and therefore, the fraudulent transaction may be frustrated.²¹⁵ The buyer should insist on the use of time drafts rather than sight drafts. The rationale behind this is to allow some time before payment of the credit until the arrival and inspection of the goods. Thus, fraud can be detected before payment.²¹⁶ He should also put a condition which provides for sale "on approval". The root of this condition is found in the English Sale of Goods Act 1979, which provides for sales on approval in which the property in the goods does not pass to the buyer until he approves the goods. In case of payment by letters of credit, payment will not be

(1982).

²¹² Samuel, *supra* note 206 at 293. See also, Dolan, *The Law of Letters of Credit. Commercial and Standby Credits* p. (3-33).

²¹³ This practice of insisting on standby credits to secure the sellers compliance with the underlying contract is evident in the American case of *City of Philadelphia v American Coastal Indus., Inc.*, 704 F.Supp. 578 (ED. Pa. 1988).

²¹⁴ McLaughlin, G.T., 'Structuring Commercial Letter-of-Credit Transaction to Safeguard the Interests of the Buyer' 21 *Uniform Commercial Code Law Journal* (1989) 318 at 318-332.

²¹⁵ Murray, D.E., 'Letters of Credit and Forged and Altered Documents: Some Deterrent Suggestions' 98 *Commercial Law Journal* (1993) 504 at 508.

²¹⁶ *Ibid* at 509.

effected till the buyer approves the quality of goods.²¹⁷

Since transmission of shipping documents between the seller and issuing bank is direct, buyers are advised to require carriers to send facsimile copies of bills of lading immediately to the issuing banks. Issuing banks, therefore, would state that the letter of credit would not be honoured without the bill of lading facsimile having been received. This decreases the chance of forged shipping documents by unscrupulous carriers and sellers.²¹⁸

²¹⁷ Ibid at 510.

²¹⁸ Ibid at 511.

Section Two: Evaluation of the Conditional-Absolute Payment Issue in Light of the Basic Principles of Commercial Law

1. “Conditional” Payment vs. “Absolute” Payment

Parties to the underlying contract are free to expressly or impliedly agree on whether payment by letter of credit is absolute or conditional. Since the underlying contract is usually silent on the issue of whether payment by letter of credit is absolute or conditional, it will be a matter of deduction for a court to decide what the intentions of the parties should be taken to be in all circumstances. However, in English law if the contract is silent as to this issue, there is a rebuttable presumption that it is conditional rather than absolute.

Despite its theoretical “independence”, the buyer’s procurement of the letter of credit is treated by the courts, more often than not, as conditional payment.²¹⁹ Although considering a letter of credit as a conditional payment goes against the principle of independency, the resulting fairness, certainty and flexibility which it brings about is judged to outweigh non-conformity with the independency principle.

Other than the seller’s default or being late in tendering the correct documents, there are two situations whereby the seller might not get paid while he is entitled to: one is when the bank rejects the seller’s documents due to technical discrepancies, another is on the banker’s bankruptcy. These two situations will be dealt with separately below.

2. What Position Does the Law Take in Relation to Absolute-Conditional Payment Issue?

What is the position in the three legal regimes with which we are concerned (English law, the UCP and the UCC) with regard to the absolute-conditional

²¹⁹ See generally, *Newman Industries Ltd v Indo-British Industries* [1956] 2 Lloyd’s Rep 219; [1957] 1 Lloyd’s Rep 211 and *Maran Road Saw Mill v. Austin Taylor Ltd* [1975] 1 Lloyd’s Rep. 156; *W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co.* [1972] 2 Q.B. 189 at 220; *Newman Industries Ltd v Indo-British Industries* [1957] 1 Lloyd’s Rep 211, at 236.

issue?

Under English Law, if the contract is silent as to the payment clause, there is a strong presumption that payment by letters of credit is a conditional payment.²²⁰ Both the UCP and the UCC are silent upon the issue.

3. Technical Defects in the Documents

In determining whether a seller is allowed to have a direct recourse against the buyer upon the bank finding technical defects in the documents, it is important primarily to establish whether payment is conditional or absolute and the standard of compliance in place. The impact of the applicable compliance standard on whether payment by a letter of credit is conditional or absolute, upon finding technical defects in the documents will be examined below under section 3.1.2.

3.1. Evaluation of Absolute-Conditional Payment Issue With Reference to the Five Criteria

3.1.1. Party Autonomy in Relation to Absolute-Conditional Payment

Parties should be free to explicitly agree that payment by letter of credit is either absolute or conditional. Where the parties so agree, the principle of party autonomy dictates that such terms should be held sacred. Hence, the law may adopt either of the two doctrinal options, conditional payment or absolute payment, as default positions. Either way, party autonomy is respected because the contracting parties can alter the default position by express agreement. This conclusion can be inferred only from Common Law cases. The UCP is silent upon the issue but since the UCP rules are default rules, there is no reason why parties cannot agree to whether payment is absolute or conditional. The UCC rules are silent upon the issue too but since Article 5 allows variation of its sections if the contracting parties so agree, then the principle of party autonomy is also preserved.

3.1.2. Fairness in Relation to Absolute-Conditional Payment

Treating the payment by letter of credit as absolute, may, according to the

²²⁰ See, Section One, (1.7.).

distributive theory, produce unfairness, since the seller has no rights against the buyer for payment in case of the banker's default even if the tender was rejected due to minor or immaterial defects. Under these circumstances, although the seller is, no doubt, entitled to appeal to the buyer, if he (seller) has lost control over goods, the buyer can often delay the payment for a few months and thus take advantage of the most trivial irregularities. Now where the applicable compliance rule is the "strict compliance" rule, the bank is right to reject the seller's documents, even if the discrepancies are trivial. The problem then lies with the absolute payment rule *in conjunction with* a strict compliance rule. In contrast, treating a letter of credit as conditional payment is fair (more in line with the distributive theory), since in most cases the seller will have recourse to the buyer should he fail to obtain payment from the bank, provided that he has performed and there is no fault on his part.

3.1.3. Good Faith in Relation to Absolute-Conditional Payment

By treating a letter of credit as a conditional payment, good faith, in its objective sense, is promoted because the law then reflects the reasonable expectations of commercial people. It is important, at this point, to justify why the 'objective sense' has been used here. In the underlying contract, since it is not governed by the law of letter of credit, i.e. the UCC Article 5, but governed by applicable law whereby the concept of fair dealing is incorporated. By contrast, treating a letter of credit as an absolute payment overlooks good faith. The buyer can take advantage of the most trivial irregularities in the goods to delay payment if goods are delivered. A case which is even worse is when the goods have not yet been shipped to the buyer and the price of goods in the market has fallen, the buyer simply rejects the goods. The only thing the seller can do is to sell the goods in the market at the best price he can in an effort to mitigate his loss, and then sue the banker for damages for breach of contract, which is a lengthy, expensive and unreliable process²²¹.

²²¹ See, Section Two, (1.1.),

3.1.4. Certainty in Relation to Absolute-Conditional Payment

If the law holds that where the contract is silent as to the payment clause, there is a strong presumption that payment by letters of credit is conditional, then, commercial people know where they stand. Likewise, if a letter of credit payment is to be regarded as absolute, unless otherwise expressly or impliedly agreed to, the law is also certain.²²²

Certainty is apparent from the clear statement of law which was put by Lord Denning MR. where he stated that; “a letter of credit is not to be regarded as absolute payment, unless the seller stipulates, expressly or impliedly, that it should be so.”²²³

In fact, it is well established that the opening of a credit does not discharge the buyer’s obligation to pay. As Ackner J. put it clearly in Maran Road Saw Mill v. Austin Taylor & Co. Ltd.²²⁴, providing a ‘source of payment’ by letter of credit is different from the promised ‘paying by letter of credit’, and what the bank promised was to pay by letter of credit, not to provide by a letter of credit a source of payment which did not pay²²⁵. In the leading case of Newman Industries Ltd v. Indo-British Industries²²⁶, payment was merely conditional. The same line of judgments was also followed in El Nasr²²⁷ and Maran Road Saw Mill v. Austin Taylor Ltd²²⁸.

In other words, the law governing letters of credit (English law) is certain as to payment because commercial people would be certain that payment by a letter of credit is, without doubt, not absolute at all unless otherwise expressly or impliedly

²²² See, Ibid.

²²³ *W.J. Alan & Co. Ltd. v. El Nasr Export and Import Co.* [1972] 2 Q.B. 189 at 220; See also *Newman Industries Ltd v Indo-British Industries* [1957] 1 Lloyd’s Rep 211, at 236.

²²⁴ *Maran Road Saw Mill v. Austin Taylor Ltd* [1975] 1 Lloyd’s Rep. 156 at 159.

²²⁵ Gutteridge, H.C., and Megrah, M., *The Law of Bankers’ Commercial Credits* p. 35.

²²⁶ *Newman Industries Ltd v Indo-British Industries* [1956] 2 Lloyd’s Rep 219; [1957] 1 Lloyd’s Rep 211; See also *Soproma S.p.A. v Marine and Animal By-Products Corporation*, *supra*. In the U.S.A. See: *Lamborn v Allen Kirkpatrick*, 135 A 541 (1927); *Greenough v Munroe*, 53 F. 2d 362 (1931).

²²⁷ *WJ Alan & Co v El Nasr Export and Import Co* [1972] 2 Q.B. 189.

²²⁸ *Maran Road Saw Mill v. Austin Taylor Ltd* [1975] 1 Lloyd’s Rep. 156.

agreed to. So, if the beneficiary agreed that payment by a credit was to be absolute, he would know beforehand that in case of the issuing bank being unable to pay, he could not claim payment from the applicant.

As has been discussed above, the position of English law is certain on this issue, whereas it appears that the UCP is silent. This feature of silence may be construed as uncertainty. Although the UCP takes an international approach, it is evident that individual practices vary and therefore such individualised practices play a part in determining the way in which it is interpreted. As far as the UCC is concerned, it is also silent upon the issue. This also may be construed as uncertainty.

3.1.5. Flexibility in Relation to Absolute-Conditional Payment

The common law is flexible as to the nature of payment under letters of credit (whether absolute or conditional). There is more than one position that the law may take. Under common law parties are free to explicitly agree that payment by letter of credit is either absolute or conditional payment. In other words, the law here can be perceived as flexible. Thus, in between the expanded reliance upon the existing common law rule in relation to the nature of the payment clause as a default rule and the ordinary ability of the parties to vary that rule, the common law grants commercial people the maximum flexibility to tailor their relationships under letters of credit. Likewise, since almost the entirety of Article 5 of the UCC in its revised or original form is variable by agreement, and the provisions of the UCP are default rules, parties may agree to whether payment by letters of credit be absolute or conditional.

4. What Position Should the Law Take With Regard to the Nature of Payment Clause Issue?

As a matter of general principle, what position should the law take with regard to the nature of payment clause whether absolute or conditional? In other words, what option should be adopted?

Having examined the position of absolute-conditional payment clause under the laws governing letters of credit, and having illustrated how each option interacts

with the five basic principles, the answer will be reserved to the Concluding Chapter in which a proposal for reform will be made.

Table 1: Comparison between Letter of Credit as Conditional and Absolute Payment in light of the basic principles of commercial law

	Conditional payment	Absolute payment
Party Autonomy	Parties are free to explicitly agree that payment by letter of credit is conditional payment. Where the parties so agree, the principle of party autonomy dictates that such terms should be held sacred. That is to say, the law might adopt the two doctrinal options: conditional payment or absolute payment as default positions. Thus if the default position is conditional payment, then conditional payment applies unless the contracting parties explicitly provide for absolute payment.	Parties are also free to explicitly agree that payment by letter of credit is absolute payment. However, if the contract is silent as to this issue, there is a strong presumption that it is conditional rather than absolute. Thus, if the default position is absolute payment, then absolute payment applies unless the contracting parties explicitly provide for conditional payment. Either way, party autonomy is respected because the contracting parties can alter the default position by express agreement.
Fairness	Fairer, since in most cases, the seller does have recourse to the buyer should he fail to obtain payment from the bank, provided that he has performed and there is no fault on his part.	Unfair, since seller has no rights against the buyer for payment in case of banker's default.
Good Faith	Good faith is promoted because conditional payment reflects the reasonable expectations of commercial people.	Buyer can take advantage of the most trivial irregularities to delay payment if goods are delivered. If goods are not yet delivered, buyer can reject goods and leave seller to sue the banker for damages for breach of contract.
Certainty	The law regulating letters of credit is certain on the issue that, if the contract is silent to payment clause, there is a strong presumption that payment by letters of credit is conditional. Therefore, commercial people would know where they stand. As Ackner J has put it clearly in <i>Maran Road Saw Mill v. Austin Taylor & Co. Ltd.</i> ²²⁹ that, providing a 'source of payment'	Certainty is promoted because commercial people would be certain that payment by a letter of credit is, without doubt, absolute unless otherwise expressly or impliedly agreed. So, unless the beneficiary agreed that payment by a credit is to be conditional, he would know beforehand that in case of the issuing bank being unable to pay, he cannot claim payment from the applicant.

²²⁹ Ibid at 159.

	by letter of credit is different from the promised 'paying by letter of credit', and that the bank promised to pay by letter of credit, not to provide by a letter of credit a source of payment which did not pay.	
Flexibility	<p>Under common law, the parties are free to explicitly agree that payment by letter of credit is either absolute or conditional payment. Thus, the common law grants commercial people the maximum flexibility to tailor their relationships under letters of credit.</p> <p>Since almost the entirety of Article 5 of the UCC in its revised or original form is variable by agreement, and the provisions of the UCP are default rules, parties may agree to whether payment by letters of credit be absolute or conditional.</p>	<p>Under common law, the parties are free to explicitly agree that payment by letter of credit is either absolute or conditional payment. Thus, the common law grants commercial people the maximum flexibility to tailor their relationships under letters of credit.</p> <p>Since almost the entirety of Article 5 of the UCC in its revised or original form is variable by agreement, and the provisions of the UCP are default rules, parties may agree to whether payment by letters of credit be absolute or conditional.</p>

5. Banker's insolvency

In section one, the way in which the court treats the parties where the seller has not been paid before the banker's insolvency has been outlined. Here, two situations have to be distinguished: the first situation is whereby the bank has become insolvent before the buyer pays the bank, and the second is where the buyer places the bank in funds before its insolvency.

In the first situation, according to the distributive theory, gross unfairness is apparent if the payment by letter of credit is treated as absolute, since the buyer can then escape payment, leaving the seller to claim his liquidating dividend as a general creditor of the bank which would not make up the purchase price. By treating the letter of credit as a conditional payment, however, in accordance with the distributive theory, the result will be fair; and both the buyer and seller will neither lose nor gain anything.

The second situation is where the court is forced to do an injustice as shown clearly from Chart 1. The dilemma is that, where the payment by letter of credit is conditional rather than absolute and the seller is usually held to be a general creditor, that is to impose the loss due to the bank's insolvency on the buyer rather than on the seller. This makes the buyer pay twice: once to the banker and once to the seller, which is, according to the distributive theory, grossly unfair to the buyer. By treating the payment by letter of credit as absolute, the seller will be left with getting less than the contracted price, as being a general creditor, he gets only the pro rata liquidating dividend, which is unfair to the seller.

McNair J.²³⁰ was of the view that, only in the event of the issuing bank's insolvency may the seller be able to tender documents to the buyer directly. However, that would make the buyer who has already paid the bank pay twice. There is a sound argument supporting this position if the bank is chosen by the buyer, which is what happens in the majority of the cases because he should be in a better position to

²³⁰ *Soproma S.p.A v Marine and Animal By-Products Corporation* [1966] 1 Lloyd's Rep 367, 386.

know the financial soundness of the banker than the seller.²³¹

A better solution is by considering the seller a preferred creditor of the bank to the extent of the buyer's payment, as suggested by Berger.²³² In doing so, it becomes easier to determine which party is to suffer the loss which resulted from the insolvency on the part of the issuer.²³³ Neither of the parties will incur any loss in that case since the buyer has already settled the amount due upon receiving the merchandise and the seller has been paid in full, for the draft "which measured his claim against the bank or the buyer".²³⁴ Consequently, this would ensure that the documentary credit provides guarantee of the payment to the seller, as well as ensuring that the documentary character of the transaction continues to clearly define the duty of the buyer in terms of its meaning and specificity.

In the US, the issuing bank's insolvency problem is dealt with under Section 5-117 of the UCC.²³⁵ It is well-established that once the bank opens the credit it acts as a principal, not as agent. Thus, when the bank becomes insolvent before the credit transaction is completed, the outstanding liabilities, the security held by the bank and funds provided to indemnify against those liabilities are regarded as separate from deposit liabilities and general assets. Nonetheless, the beneficiary is not to receive a preferred treatment unless the applicant has earmarked a deposit to pay the credit or has pledged collateral to secure payment. The beneficiary is given a

²³¹ See *ED. And F Man Ltd. v Nigerian Sweets and Confectionery Co. Ltd.* [1977] 2 Lloyd's Rep 50.

²³² Berger, S.R., *supra* note 204 pp 174-80.

²³³ It should be noted that Article 5-117 of the Uniform Commercial Code deals specifically with the circumstance of an issuer, and advising or confirming bank becoming insolvent before the final payment of the credit. The drafts or demands are entitled to payment in preference over depositors or other general creditors of the issuer or confirming bank to the extent of any funds turned over after or before the insolvency as indemnity against drafts or demands for payment drawn under the designated credit. These provisions would be applicable where the Code does not have the force in law. See Sarna, L., *supra* note 203 at 307; see also, Gutteridge and Megrah, *The Law of Bankers' Commercial Credits* p. 36.

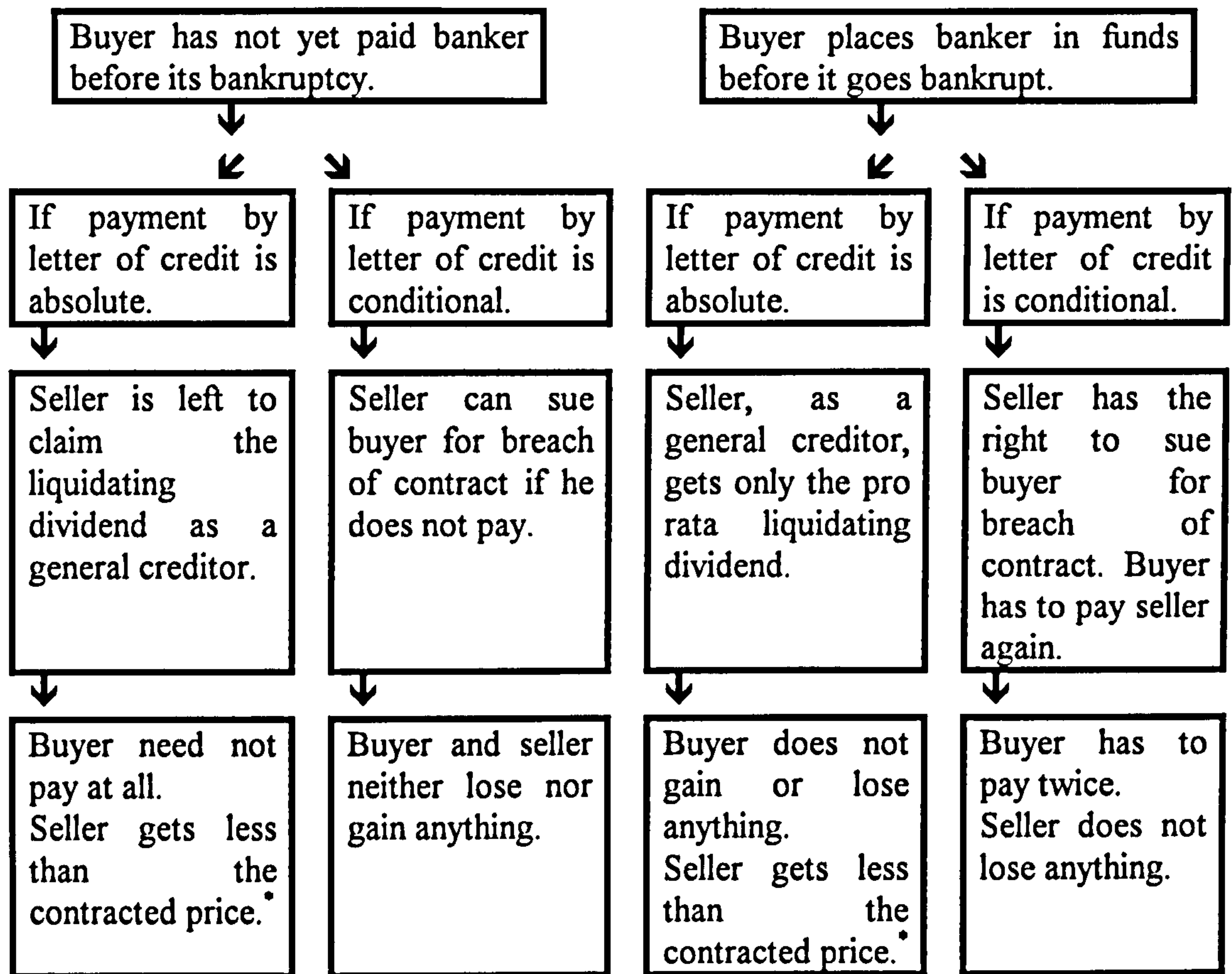
²³⁴ Berger, S.R., *supra* note 204 at 180.

²³⁵ It is to be noted here that this insolvency Section (5-117) of the (pre-1995 version) has not been added to the (1995) version of the UCC. See Appendix D, for update, Section (15).

preferred treatment by virtue of (pre-1995) UCC and the common law.²³⁶

²³⁶ See Section 5-117 UCC, cmt; Dolan, *The Law of Letters of Credit. Commercial and Standby Credits* p. (12-12) et seq.

Chart 1: The Positions of Buyer and Seller on Banker's Insolvency



* The loss to the seller is equal to the difference between the sales price and the liquidating dividend.

Conclusion

Where parties to the underlying sales contract agree that payment is to be made by a letter of credit, then it should only be effected by furnishing of that credit by the buyer. Given the mutual nature of the credit, it is not open to the seller to short-circuit the credit by tendering the documents directly to the buyer and demand payment directly from him. The type of credit which the buyer opens in favour of the seller must be the exact type of credit agreed upon. In other words, if the buyer fails to open a credit, or if he opens a different credit from that contracted (unless waived by the seller), he is in breach of the sales contract. If the breach has occurred, the damages should not be limited to the payment of the price, but will be anything that is recoverable under ordinary principles applicable to contractual damages.²³⁷

If the seller is unable to obtain payment from the bank, the crucial question faced by the seller is whether he has a right of recourse against the buyer. The reason for which the seller is unable to obtain payment, and the drafting of the 'payment' clause in the main contract between buyer and seller are important considerations.

If the seller is unable to tender the required documents or is late in presenting them, then he has no real grounds for complaint since he has himself breached the contract in which he is obliged to tender the very documents prescribed by the credit.

The possibility of the seller's recovery of payment on the banker's default is the key issue examined in this chapter. Other than the seller's failure or late presentation of the correct documents, the reason why the seller cannot get the payment is usually either because the banker refuses to accept documents due to trivial or technical discrepancies²³⁸ or the banker's bankruptcy. The seller's right of recourse depends upon whether the letter of credit is "absolute payment" or "conditional payment" of the purchase price which depends upon the interpretation of the payment clause in

²³⁷ Todd, P., *Bills of Lading & Bankers' Documentary Credits* p. 72.

²³⁸ See Chapter Five for the issue of what is considered as trivial and technical discrepancies.

the sales contract. It is usually a matter for the court to decide, under circumstances of individual cases, what the intentions of the parties should be.

It is a principle of letter of credit law that the letter of credit is completely independent of the underlying sale of goods contract. Nonetheless, as examined in section one, according to the line of well-established case law, in the absence of an express stipulation to the contrary, there appears to be a strong presumption in favour of construing letters of credit as conditional payment. So, in most cases, the seller does have recourse to the buyer should he fail to obtain payment from the banks, provided that he has performed and there is no fault on his part. So, it is presumed that the intention of the parties to a sales contract is to treat the furnishing of the documentary credit, and thus the subsequent acceptance of drafts, as conditional rather than absolute payment.

In most cases, the transaction comes to an end when the bank discharges the credit. However, following the principle of independency²³⁹, the payment effected by the bank does not necessarily discharge the mutual rights and duties of the parties to the contract of sale. Therefore, there remains a right of an action in deceit²⁴⁰ or a breach of contract against the seller if it is later discovered that the documents the seller has tendered are not genuine.

²³⁹ *Benjamin's Sale of Goods*, at § 23-120 p. 1712 *et seq.*

²⁴⁰ *See, eg Famouri v Dialcord Ltd* (1983) 133 NLJ 153.

Chapter Eight: Conclusion

Chapter Eight: Conclusion

Introduction

In this concluding chapter, it is appropriate to start by emphasising the distinctive nature of the certainty versus fairness problem in the context of letters of credit which can be expressed as follows:

(1) It is generally agreed that the two cornerstone principles of the law governing letters of credit are (i) the independency (autonomy) principle and (ii) the doctrine of strict compliance.

(2) The function of the independency (autonomy) principle is to protect the interests of the *seller*. It means that the buyer cannot raise issues arising from the underlying transaction to interfere with payment to the seller under the letter of credit arrangement.

(3) The function of the doctrine of strict compliance is to protect the interests of the *buyer*. It means that the seller does not get paid without strictly meeting the buyer's conditions for payment.

(4) Both these principles are designed for certainty. The seller knows that compliance with the terms of the credit should produce payment and that problems relating to the underlying transaction cannot give the bank an excuse for non-payment. The only good reason for non-payment is if the documents do not comply.

(5) In both cases, however, the protection given by these two principles can be abused. The fraudulent seller can hide behind the independency principle; and the bad faith buyer can insist upon strict compliance.

(6) So, looking at the two cornerstone principles from the perspective of fairness, two exceptions or qualifications to the principles invite consideration. One

exception (to the independency principle) is for fraud by the seller; and the other exception (to the principle of strict compliance) is for bad faith by the buyer (or by the bank).

(7) The central problematic in this area of law, therefore, is how far (if at all) the two cornerstone principles (representing the interests of certainty) should be qualified (in the interests of fairness) by exceptions for fraud by the seller and bad faith by the buyer.

Whereas under current English law, the strict compliance test is potentially unfair to the seller, the narrow interpretation of the fraud exception is potentially unfair to the buyer. In light of this, one may argue that unfairness to the buyer (narrow fraud) is balanced by unfairness to the seller (strict compliance). Although it is true that both parties (buyer and seller) are exposed to unfairness under English law, this however, does not mean that two wrongs make a right. The position taken under English law is completely in favour of certainty. What we propose is that the law should be adjusted marginally, to make corrections in favour of some fairness to both sides, but in doing so without jeopardising certainty. Having argued for such marginal adjustment to legal doctrine in favour of fairness, it is to be noted that both parties would still be at risk but not as much as under the present regime. In sum, under the present regime, there is a high risk of unfairness with complete certainty. Thus, in the proposals which will be advanced below, it is felt that there is less risk of unfairness without jeopardising certainty.

In this study, we have examined the tension between certainty and fairness not only in relation to the independency principle (and its fraud exception) and strict compliance but also in relation to a number of other doctrinal issues. They are (i) the prevailing standard of compliance in the reimbursement contract (whether

“strict compliance” or “bifurcated compliance”); (ii) the nature of payment clause (whether absolute or conditional); and finally (iii) punitive damages.¹

Generally speaking, relative to the tension between certainty and fairness, there are three options that the law can take in relation to each issue discussed under the law governing letters of credit. Option one is to maximise doctrinal certainty. In other words, certainty is the main and only concern of doctrine. Conversely, option two attempts to gear the law towards fairness. Thus, fairness can be perceived as the primary and fundamental concern of legal doctrine. Option three seeks a balance between certainty and fairness. In principle, this balance could be struck anywhere between certainty and fairness. However, in what follows, this third option will be concerned only with marginal adjustments to doctrine that is primarily geared for certainty.

As we have seen in each chapter, the problematic issues which have been subjected to evaluation, have been more concerned with certainty than with the principle of fairness. In all these matters, as will be demonstrated later in the recommendations, the general position taken will be to respect certainty but, in doing so, to ensure that fairness is not neglected. Therefore, it is apparent that there is a call for *marginal* adjustment to the classical doctrine of letters of credit, the main aim of which adjustment is to inject some fairness — fairness which would not affect certainty of legal doctrine.

In these concluding remarks an attempt is made to formulate a number of proposals (recommendations) which are designed to make the law more sensitive to questions of fairness but without sacrificing the certainty that is essential for

¹ In light of the discussion, examined earlier in Chapter Six, Section Two (3), concerning the impact of fraud (bad faith actions) committed by the seller (beneficiary) on both innocent bank and buyer in relation to the reimbursement contract, it is felt that the balance between the considerations of certainty and fairness is rightly struck, in the current law governing letters of credit. Thus, there will be no proposal for reform in this Concluding Chapter.

commercial dealing. The improvements concern particularly (i) the compliance standard (in the letter of credit context); (ii) the compliance standard in the reimbursement agreement context; (iii) the fraud exception; (iv) punitive damages; and (v) the nature of the payment clause (whether absolute or conditional).

1. The Compliance Test

So far as the question of the documentary compliance test is concerned, there are three factors to be taken into consideration. First, the test must be sufficiently certain to be commercially workable; secondly, it must not operate unfairly (by e.g. unfairly depriving the beneficiary of payment where documents have trivial discrepancies); thirdly, it must not invite bad faith/abuse of right/a lack of good faith by either bankers or buyers.

In fact, the doctrine of strict compliance, although meeting the test of certainty, may give rise to unjust results. The principle of good faith is the only chip the court has in hand to let in commercial fair dealing considerations when applying the doctrine of strict compliance. Most of those familiar with documentary credits have expressed the view that it is wrong and unjust to leave the applicant with no remedy due to the inflexibility of the doctrine. If the beneficiary is left with no remedy due to a mere technicality, documentary credit will be seen as an instrument which hinders rather than helps international trade. There is also the risk with strict compliance that trivial non-compliance can be used in bad faith as a pretext for non-payment. Thus, the application of the principle of good faith in some form or another is vital to fair dealing in documentary credit transactions.

Accordingly, the author suggests that the law should incorporate a good faith test in some form. It could do this *directly*, by adopting an explicit requirement of good faith, which the seller could then plead where he suspected that the bank was using the strict compliance standard for bad faith purposes (either to benefit the bank or

the buyer). Or, good faith could be introduced *indirectly*, by dropping the strict compliance test in favour of either substantial compliance or qualified strict compliance. Theoretically speaking, the direct test of good faith sounds more plausible and may seem to tackle the issue of bad faith resulting from misapplying the strict compliance test straightforwardly. Nonetheless, the author suggests that this test may prove difficult to put into practice. The fact that the law adopts a direct test of good faith (along with the strict compliance standard being retained) may produce some problems as it would be a matter of evidence to prove bad faith actions committed either by buyer or bank. In other words, it is difficult to apply in practice, firstly, precisely because it asks difficult questions about motives, reasons, states of mind etc. Secondly, as a result, there might be some cases of bad faith that a direct test fails to pick up (i.e. many bad faith actions whether by the bank or the buyer may not be caught) if there is not sufficient evidence of bad faith. Both bank and buyer may, by virtue of the strict compliance test, practise some bad faith actions when their sole motive is to escape the consequences of a bad bargain. i.e. they may be shielded behind the strict compliance test. Thus, if the direct test is to be adopted, there is no guarantee that it will be possible to detect bad faith actions, particularly in cases of lack of evidence concerning motives, reasons, states of mind etc.—and, what is more, the uncertainty involved in such enquiries into alleged bad faith threatens the calculability of letters of credit.

By contrast, the indirect test of good faith may seem to be preferable to a direct test because one of the strong arguments in favour of an indirect test is that it is easier to apply in practice than a direct test, precisely because, first of all, it avoids asking difficult questions about motives, reasons, states of mind etc. Secondly, as a result, an indirect test of good faith might actually succeed in picking up more cases of bad faith.

Having suggested that both the substantial and qualified strict compliance tests represent an indirect test of good faith, and having suggested that an indirect test is preferable to a direct test, the author's preference is to adopt the qualified strict compliance test. This is supported by the following factors:

First, any test based on "substantial" compliance raises the question of how the line between substantial and non-substantial will be drawn. In other words, in its application, this test is likely to prove unpredictable and uncertain. Neither the seller nor the buyer will know where they stand.

Secondly, unlike qualified strict compliance, substantial compliance involves looking beyond the documents and asking about the impact on the buyer. But, what precisely is the question that substantial compliance asks? Again, the test is not as clear as one might wish. If the test is vague, it again leaves the law uncertain.

Thirdly, even if the question that substantial compliance asks is about the consequences of the particular *documentary* non-compliance in relation to the impact on the buyer, there is a temptation to start dealing in goods. If this happens, the independency principle is broken. Quite apart from raising concerns about certainty, this leads to an unexpected twist in the following way. We start looking at the doctrine of substantial compliance as a way of protecting the seller against abuse by the buyer; however, if substantial compliance invites departure from the independency principle, it might end up working against the seller's interests.

Thus, the preference is for the qualified strict compliance test because, first of all, banks are entitled to honour the credit despite trivial discrepancies. Secondly, since banks do not have to look beyond the documents to decide the question of compliance, the consideration of certainty is not jeopardised. This would respect the rule of independency by being more certain than the substantial compliance test

as well as maintaining good faith, though not as much as the substantial compliance test does. It is to be noted that if the concern here is to move towards good faith and fairness only and not to focus on certainty, the substantial compliance test would be the answer. Yet, since the objective of the thesis is to strike the right balance between considerations of certainty and fairness, it is suggested that the right balance in relation to the standard of compliance is the qualified strict compliance test.

2. The Fraud Exception

Should the law ever allow fraud, both in the underlying sale transaction and fraud by a third party, to be a good defence for a bank's refusal to pay the beneficiary?

The answer to this question lies in accommodating two considerations: first, from a certainty point of view, fraud in the underlying sale transaction as well as by a third party, should not be allowed as a defence for the bank to reject payment to the beneficiary. This is simply because the law should not encourage the bank to look for reasons to dishonour the letter of credit arrangement. Secondly, from the good faith and fairness perspective, the answer is positive at least where the beneficiary has knowledge of fraud and thus, acts in bad faith.

In order to find the right balance between certainty and fairness, it is important to consider three possible approaches to a fraud exception: (i) mere allegation of fraud suffices; (ii) actual knowledge of fraud is required; and (iii) reasonable ground for suspecting fraud suffices. Starting with the first case, mere allegation of fraud suffices, it is too risky to the seller since both the bank and the buyer, acting in bad faith, can allege such fraud and thus prevent the beneficiary from drawing on the credit thereby affecting fairness and certainty too. So far as actual knowledge by the bank of the fraud is concerned, it may be also too risky to both the bank and

the buyer's interests because even though they strongly suspect fraud but for some reason cannot prove it, the seller is still entitled to payment in which case fairness is also jeopardised. This is the position under English law. The suggested compromise thus is applying the third approach, refusing payment if there is reasonable ground to suspect fraud. By insisting on this approach, both certainty and fairness can be well balanced. This means the bank could legitimately not pay if there is a reasonable ground of suspecting fraud. Thus, so far as English law is concerned, the balance between certainty and fairness may be achieved if the confines of the fraud exception are broadened to entitle the bank to reject payment on reasonable grounds of suspecting fraud instead of insisting on the bank's actual knowledge.

Following this suggestion, the seller will have no claim against the bank for wrongful refusal to pay, if:

- (1) the seller has committed fraud; and
- (2) the bank has reasonable grounds to suspect fraud by the seller.

So, if the bank refuses to pay on the grounds of fraud, its defence hinges on it establishing reasonable grounds for suspicion of fraud. The question which emerges now is: how then does the question of actual fraud get settled? Obviously, it cannot be that the bank must prove actual fraud; because the suggestion is that reasonable suspicion is enough. The effect of this is that it is up to the seller to disprove fraud. In other words, the bank makes out its defence on the basis of reasonable grounds and that is a good defence unless the seller can then prove an absence of fraud.

Having softened the rigours of the existing English law by letting the bank have the right to refuse payment if the bank has reasonable grounds to suspect fraud by the seller, the result is fair since if there has actually been fraud by the seller and since

actual fraud is part of the test, then whatever the rest of the test the seller can hardly complain about unfairness.

3. Punitive Damages

In the interests of certainty, the author favours adopting a clear rule within the sections of Article 5 of the UCC itself as well as the UCP in relation to punitive damages (i.e. as to whether or not they may be allowed). The most difficult question is whether punitive damages should be made available to innocent parties (whether the beneficiary, bank, or applicant) and if so, in what circumstances penal awards should be allowed.

Should the law ever allow the beneficiary to recover punitive damages against the bank where the bank has wrongly failed to pay? First, if the law is concerned with considerations of party autonomy (sanctity), then the answer is in the positive because the threat of punitive damages should encourage the bank to honour the letter of credit arrangement in which case certainty of payment is preserved. Moreover, so far as freedom of contract is concerned, the answer is in the positive too since this provides that parties should have the power to set their own remedial regime. Secondly, if punitive damages are never awarded, it creates an open-ended excuse to contract breachers for them not to fulfil their contractual obligations thereby jeopardising fairness.

On the other hand, if punitive damages are always awarded, it is extremely unfair because it goes completely against the compensatory policy of contract law. This would also encourage unbridled claims for such damages in all cases.

Having admitted that the award of punitive damages is unfair, as a general rule, allowing punitive damages may be justified if the harm done by one of the contracting parties is so severe as to fall within one of the exceptional categories for allowing them, as suggested by some American authorities.

Thus, the compromise would be that punitive damages should be awarded in some cases. This option, in order to be applied efficiently, requires a definite and categorised list of prohibited conduct upon the occurrence of which such damages would be awarded. Regardless of the controversy over the award of punitive damages in the US (as to whether such damages are to apply to insurance contracts only)², the author suggests that punitive damages should be awarded in some certain cases and to all types of contracts but only upon the occurrence of a specified (definite) category of conduct such as (i) where the guilty party acts in bad faith (maliciously, fraudulently) and (ii) where the guilty party acts in a grossly negligent way. Such an itemised category of prohibited conduct could be laid down by either courts or legislatures. Having accomplished such a list of specified wrongs, certainty would be preserved. Each party would be aware of such prohibited actions before entering into a contractual relationship no matter whether this wrong conduct is a contract-based liability or a tort-based liability. This would bring fairness to the innocent party and thus the balance between certainty and fairness may be best struck.

The reason why the above two categories of conduct are suggested as possible grounds for awarding punitive damages in letters of credit cases can be explained as follows. So far as both bad faith acts (fraud and malice) and grossly negligent acts are concerned, the reason for taking a hard line here is that a letter of credit (as a special commercial device having its own character) makes international trade possible regardless of the fact that distant buyers and sellers do not know each other. Both distant parties to a letter of credit enter into this relationship in the belief that the correct documents are to be presented and the right sum of money will be paid. Any compromise to such certainty of letters of credit would

² See, Nehf, J., 'Bad Faith Breach of Contract in Consumer Transaction' in *Good Faith in Contract: Concept and Context*, edited by Brownsword, R., Hird, N., and Howells, G. (Dartmouth Publishing Company Limited, London, 1999) 115, 131-136.

jeopardise international trade. In other words, if fraud and malice as well as grossly negligent acts go unpunished, the credibility of documentary credits is undermined and the original problem of lack of trust threatens to re-emerge.

Although introducing punitive damages may seem to be a radical step, the award of such damages can be further justified as follows. Firstly, it is suggested that punitive damages are to be awarded only in exceptional cases. i.e. as an exception not as a rule. Secondly, it is submitted that punitive damages are to be awarded in the letter of credit context in order to protect the whole institution of letters of credit and thus provide certainty. Regardless of the unfair nature of such damages, the reason for their award is justified in cases where trust is threatened in a letter of credit. If there is lack of confidence or even abuse within a letter of credit, the whole institution of letters of credit would be jeopardised. Instead of ordinary awards of compensation, punitive damages is one way of clamping down on such harm. In sum, although it might be argued that such damages are to be awarded to attain fairness to the aggrieved party, this would actually result in over-compensation: thus, the most important reason for their award is to strengthen faith and confidence in the institution of letters of credit in order to attain certainty. Thirdly, punitive damages should not be extended to the reimbursement contract or the underlying sale contract because such arrangements are considered as normal contracts and should therefore be governed by the normal contract law rules which are already said to prohibit such damages. Finally, in relation to bad faith acts (fraud and malice) and grossly negligent acts as grounds for punitive awards, the argument is that banks have a special responsibility in relation to letters of credit. If banks act fraudulently or in a grossly negligent way, without a penal system being set up to protect innocent parties, certainty of international trade would be jeopardised.

4. The Standard of Compliance in Relation to the Reimbursement Agreement

Since the UCP is silent upon the standard of compliance between the bank and the applicant, and the UCC is silent upon the issue too (though some US courts have applied the bifurcated compliance standard), the author contends that as the relationship between the applicant and the issuing bank is governed partially by the laws governing letters of credit, and partially by contract law, any standard of compliance set by the law is merely a default rule. That is to say, the compliance standard for reimbursement purposes (between bank and applicant) should be determined by ordinary contractual principles. So, the rule here is a default rule (whether it is for strict compliance or a bifurcated standard) which the bank/buyer can bargain around if they wish.

It is hoped that this issue will be dealt with explicitly in the next review of both the UCP and UCC rules. An explicit rule regarding this issue would remove any uncertainty and make the law more calculable.

Which rule should be adopted? Should it be a rule for strict compliance or bifurcated compliance?

In the interests of fairness, certainty, flexibility and good faith, they are all preserved under the bifurcated standard but not under the strict compliance standard as the study revealed (in sections 6.2.1, 6.2.2, 6.2.3, and 6.2.4.). So far as certainty here is concerned, it is to be noted that this is to do with certainty of the legal position. However, in relation to certainty of the bifurcated standard itself (which resembles the substantial compliance standard discussed in the letter of credit contract) the test is uncertain in its application because each case will be judged on its own merits.

Now, since the aim of this thesis is to preserve certainty, one may argue that it would be a mistake to adopt such a bifurcated standard because it would jeopardise certainty

and pull too strongly towards fairness. Surely though this is not the case, simply because, although the author suggests the adoption of the bifurcated compliance standard in the reimbursement agreement context, the suggestion takes into consideration two points which ensure certainty. First, the reimbursement agreement is not governed fully by the law of letters of credit. The general principles of contract law also govern in this regard. Thus, allowing some room for fairness would not jeopardise the law of international trade (i.e. the law relative to letters of credit) which thrives on certainty. Secondly, this test of compliance, in order to work with a sufficient degree of certainty, should only be applied upon the occurrence of some specific conditions. This, on the one hand, would preserve certainty. Parties would then know where they stand. On the other hand, it would guard against cases of unfairness to banks as a result of bad faith actions conducted by their customers. It is suggested, therefore, that the better explicit rule is that the bifurcated compliance standard (in association with the two common law conditions for its application, in order to attain certainty) is the default position. The two common law conditions, it will be recalled, are (i) “whether the issuer’s misconduct damaged the customer, and (ii) whether the issuer acted in good faith”.³

5. Absolute/Conditional payment

The author contends that although both the UCP and the UCC are silent upon the issue of absolute-conditional payment, since they express the independency principle, it could be inferred that absolute payment is to prevail. It is hoped that this issue will be dealt with explicitly in the next review of both the UCP and UCC rules. An explicit rule regarding this issue would remove any misunderstanding and make the law transparent.

³ Dolan, ‘Letter-of-Credit Disputes Between the Issuer and its Customer: The Issuer’s Rights under the Misnamed “Bifurcated Standard”’ 105 *The Banking Law Journal* (1988) 380, pp. 383-4.

Which rule should be adopted? Should it be a rule for absolute or conditional payment?

In the interests of good faith and fairness, both good faith and fairness are preserved under conditional payment, as the study revealed (in sections 3.1.2. and 3.1.3. above). It is suggested, therefore, that the better explicit rule is that conditional payment is the default position. Having suggested the conditional payment option, it is to be emphasised that conditional payment does not in any way jeopardise certainty.

6. Recommendations Summarised

Bearing in mind the need to maintain certainty in letters of credit arrangements, it is proposed that:

- a test of qualified strict compliance be adopted.
- the fraud exception should operate where the bank has reasonable grounds to suspect fraud and there has actually been fraud.
- punitive damages are to be awarded in two exceptional cases, bad faith and gross negligence.
- the bifurcated compliance standard is to be adopted in the reimbursement agreement context, but only where the issuer has acted in good faith and has not harmed the customer.
- conditional payment is to be adopted in relation to payment under letters of credit.

7. The Purpose and Significance of the Research

The primary purpose of this study, as set out in the introduction, is to assess the adequacy of the law relating to letters of credit in relation to the five basic

principles which, arguably, should govern Commercial Law doctrine. These principles are (i) party autonomy (freedom and sanctity of contract) (ii) certainty (iii) flexibility (iv) fairness and (v) good faith. Although it can be concluded that the principles are, all, to some extent, applicable, it seems that the laws of letters of credit are more particularly concerned with considerations of certainty than fairness. This is explained due to the special character of the letter of credit device under which banks deal in documents not in goods. Together with the independency and strict compliance principles, this serves to enhance certainty more than fairness.

The potential contribution of this study can be summarised in the following terms: it examines the relevant literature in order to explain and develop a better understanding of the five basic principles and the way they interact. The theoretical contribution of the study comes from the attempt to integrate those five basic principles of commercial law into the law governing letters of credit, as part of the commercial law doctrine, in relation to specific issues, where the literature says little regarding such a relationship between those principles and the law of letters of credit.

8. Suggestions for the Future Researchers

Owing to the fact that there are many unresolved problems (questions) in the Common Law, the UCP rules and the UCC rules in relation to letters of credit, each of them can be undertaken as a subject for further study. However, in relation to this work as a comparative research, a study with similar features is more desirable. This research has identified some gaps and deficiencies in three legal regimes governing letters of credit law. Therefore, the discussion and the argument of this thesis as well as its conclusion may be implemented for further research on striking the balance between the considerations of certainty and fairness in relation to other problematic issues which this work has not touched on—for instance,

disputes emerging from the lack of a legal relationship between buyer and intermediary bank (advising, confirming), or difficulties arising out of the lack of a legal relationship between the advising bank and the beneficiary. Further, as this work has been conducted in line with the Common Law rules, a comparative study of the application of these five basic principles in a civil law system compared with either of the UCP or UCC rules, might be more desirable because good faith is viewed in a different way in civil legal systems.

Appendices

Appendix A: Uniform Customs and Practice for Documentary Credits (1993 Revision) of the International Chamber of Commerce

Appendix B: Original Version of Article (5) of the Uniform Commercial Code

Appendix C: U.C.C. - Article 5 - Letters of Credit (Revised 1995)

**Appendix D: Uniform Commercial Code Revised Article 5 (1995)
Compared With the Original Version—Letters of Credit**

Appendix: A

**Appendix A: Uniform Customs and Practice for Documentary
Credits (1993 Revision) of the International Chamber of
Commerce¹**

GENERAL PROVISIONS AND DEFINITIONS

ARTICLE 1

Application of UCP

The Uniform Customs and Practice for Documentary Credits, 1993 Revision, ICC Publication No.500, shall apply to all Documentary Credits (including to the extent to which they may be applicable, Standby Letter(s) of Credit) where they are incorporated into the text of the Credit. They are binding on all parties thereto, unless otherwise expressly stipulated in the Credit.

ARTICLE 2

Meaning of Credit

For the purposes of these Articles, the expressions "Documentary Credit(s)" and "Standby Letter(s) of Credit" (hereinafter referred to as "Credit(s)"), mean 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 (Draft(s)) drawn by the Beneficiary, or
- ii. authorizes another bank to effect such payment, or to accept and pay such bills of exchange (Draft(s)), or

¹ *ICC Uniform Customs and Practice for Documentary Credits – 1993 Revision* (ICC Publication No 500 – ISBN 92.842.1155.7 (E)). Published in its official English version by the International Chamber of Commerce. Copyright © 1993 – International Chamber of Commerce (ICC), Paris. Available from: *ICC Publishing SA.*, 38 Court Albert 1er, 75008 Paris, France or *ICC United Kingdom*, 14/15 Belgrave Square, London SW1X 8PS, United Kingdom.

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iii. authorizes another bank to negotiate, against stipulated document(s), provided that the terms and conditions of the Credit are complied with.

For the purposes of these Articles, branches of a bank in different countries are considered another bank.

ARTICLE 3**Credits v. Contracts**

A. Credits, by their nature, are separate transactions from the sales or other contract(s) on which they may be based and banks are in no way concerned with or bound by such contract(s), even if any reference whatsoever to such contract(s) is included in the Credit. Consequently, the undertaking of a bank to pay, accept and pay Draft(s) or negotiate and/or to fulfill any other obligation under the Credit, is not subject to claims or defenses by the Applicant resulting from his relationships with the Issuing Bank or the Beneficiary.

B. A Beneficiary can in no case avail himself of the contractual relationships existing between the banks or between the Applicant and the Issuing Bank.

ARTICLE 4**Documents v. Goods/Services/Performances**

In Credit operations all parties concerned deal with documents, and not with goods, services and/or other performances to which the documents may relate.

ARTICLE 5**Instructions to Issue/Amend Credits**

A. Instructions for the issuance of a Credit, the Credit itself, instructions for an amendment thereto, and the amendment itself, must be complete and precise.

In order to guard against confusion and misunderstanding, banks should discourage any attempt:

i. to include excessive detail in the Credit or in any amendment thereto;

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ii. to give instructions to issue, advise or confirm a Credit by reference to a Credit previously issued (similar Credit) where such previous Credit has been subject to accepted amendment(s), and/or unaccepted amendment(s).

B. All instructions for the issuance of a Credit and the Credit itself and, where applicable, all instructions for an amendment thereto and the amendment itself, must state precisely the document(s) against which payment, acceptance or negotiation is to be made.

FORM AND NOTIFICATION OF CREDITS**ARTICLE 6****Revocable v. Irrevocable Credits**

A. A Credit may be either

i. revocable, or

ii. irrevocable.

B. The Credit, therefore, should clearly indicate whether it is revocable or irrevocable.

C. In the absence of such indication the Credit shall be deemed to be irrevocable.

ARTICLE 7**Advising Bank's Liability**

A. A Credit may be advised to a Beneficiary through another bank (the "Advising Bank") without engagement on the part of the Advising Bank, but that bank, if it elects to advise the Credit, shall take reasonable care to check the apparent authenticity of the Credit which it advises. If the bank elects not to advise the Credit, it must so inform the Issuing Bank without delay.

B. If the Advising Bank cannot establish such apparent authenticity it must inform, without delay, the bank from which the instructions appear to have been received that it has been unable to establish the authenticity of the Credit and if it elects

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nonetheless to advise the Credit it must inform the Beneficiary that it has not been able to establish the authenticity of the Credit.

ARTICLE 8**Revocation of a Credit**

A. A revocable Credit may be amended or canceled by the Issuing Bank at any moment and without prior notice to the Beneficiary.

B. However, the Issuing Bank must:

i. reimburse another bank with which a revocable Credit has been made available for sight payment, acceptance or negotiation for any payment, acceptance or negotiation made by such bank prior to receipt by it of notice of amendment or cancellation, against documents which appear on their face to be in compliance with the terms and conditions of the Credit;

ii. reimburse another bank with which a revocable Credit has been made available for deferred payment, if such a bank has, prior to receipt by it of notice of amendment or cancellation, taken up documents which appear on their face to be in compliance with the terms and conditions of the Credit.

ARTICLE 9**Liability of Issuing and Confirming Banks**

A. An irrevocable Credit constitutes a definite undertaking of the Issuing Bank, provided that the stipulated documents are presented to the Nominated Bank or to the Issuing Bank and that the terms and conditions of the Credit are complied with:

i. if the Credit provides for sight payment to pay at sight;

ii. if the Credit provides for deferred payment to pay on the maturity date(s) determinable in accordance with the stipulations of the Credit; iii. if the Credit provides for acceptance;

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a. by the Issuing Bank to accept Draft(s) drawn by the Beneficiary on the Issuing Bank and pay them at maturity, or

b. by another drawee bank to accept and pay at maturity Draft(s) drawn by the Beneficiary on the Issuing Bank in the event the drawee bank stipulated in the Credit does not accept Draft(s) drawn on it, or to pay Drafts(s) accepted but not paid by such drawee bank at maturity;

iv. if the Credit provides for negotiation to pay without recourse to drawers and/or bona fide holders, Draft(s) drawn by the Beneficiary and/or document(s) presented under the Credit. A Credit should not be issued available by Draft(s) on the Applicant. If the Credit nevertheless calls for Draft(s) on the Applicant, banks will consider such Draft(s) as an additional document(s).

B. A confirmation of an irrevocable Credit by another bank (the "Confirming Bank") upon the authorization or request of the Issuing Bank, constitutes a definite undertaking of the Confirming Bank, in addition to that of the issuing Bank, provided that the stipulated documents are presented to the Confirming Bank or to any other Nominated Bank and that the terms and conditions of the Credit are complied with:

i. If the Credit provides for sight payment to pay at sight;

ii. if the Credit provides for deferred payment to pay on the maturity date(s) determinable in accordance with the stipulations of the Credit;

iii. if the Credit provides for acceptance:

a. by the Confirming Bank to accept Draft(s) drawn by the Beneficiary on the Confirming Bank and pay them at maturity, or

b. by another drawee bank to accept and pay at maturity Draft(s) drawn by the Beneficiary on the Confirming Bank, in the event the drawee bank stipulated in the Credit does not accept Draft(s) drawn on it, or to pay Draft(s) accepted but not paid by such drawee bank at maturity;

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iv. if the Credit provides for negotiation to negotiate without recourse to drawers and/or bona fide holders, Draft(s) drawn by the Beneficiary and/or document(s) presented under the Credit. A Credit should not be issued available by Draft(s) on the Applicant. If the Credit nevertheless calls for Draft(s) on the Applicant, banks will consider such Draft(s) as an additional document(s).

C. i. If another bank is authorized or requested by the Issuing Bank to add its confirmation to a Credit but is not prepared to do so, it must so inform the Issuing Bank without delay.

ii. Unless the Issuing Bank specifies otherwise in its authorization or request to add confirmation, the Advising Bank may advise the Credit to the Beneficiary without adding its confirmation.

D. i. Except as otherwise provided by Article 48, an irrevocable Credit can neither be amended nor canceled without the agreement of the Issuing Bank, the Confirming Bank, if any, and the Beneficiary.

ii. The Issuing Bank shall be irrevocably bound by an amendment(s) issued by it from the time of the issuance of such amendment(s). A Confirming Bank may extend its confirmation to an amendment and shall be irrevocably bound as of the time of its advice of the amendment. A Confirming Bank may, however, choose to advise an amendment to the Beneficiary without extending its confirmation and if so, must inform the Issuing Bank and the Beneficiary without delay.

iii. The terms of the original Credit (or a Credit incorporating previously accepted amendment(s)) will remain in force for the Beneficiary until the Beneficiary communicates his acceptance of the amendment to the bank that advised such amendment. The Beneficiary should give notification of acceptance or rejection of amendment(s). If the Beneficiary fails to give such notification, the tender of documents to the Nominated Bank or Issuing Bank, that conform to the Credit and to not yet accepted amendment(s), will be deemed to be notification of acceptance by the Beneficiary of such amendment(s) and as of that moment the Credit will be amended.

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iv. Partial acceptance of amendments contained in one and the same advice of amendment is not allowed and consequently will not be given any effect.

ARTICLE 10**Types of Credit**

A. All Credits must clearly indicate whether they are available by sight payment, by deferred payment, by acceptance or by negotiation.

B. i. Unless the Credit stipulates that it is available only with the Issuing Bank, all Credits must nominate the bank (the "Nominated Bank") which is authorized to pay, to incur a deferred payment undertaking, to accept Draft(s) or to negotiate. In a freely negotiable Credit, any bank is a Nominated Bank.

Presentation of documents must be made to the Issuing Bank or the Confirming Bank, if any, or any other Nominated Bank.

ii. Negotiation means the giving of value for Draft(s) and/or document(s) by the bank authorized to negotiate. Mere examination of the documents without giving of value does not constitute a negotiation.

C. Unless the Nominated Bank is the Confirming Bank, nomination by the Issuing Bank does not constitute any undertaking by the Nominated Bank to pay, to incur a deferred payment undertaking, to accept Draft(s), or to negotiate. Except where expressly agreed to by the Nominated Bank and so communicated to the Beneficiary, the Nominated Bank's receipt of and/or examination and/or forwarding of the documents does not make that bank liable to pay, to incur a deferred payment undertaking, to accept Draft(s), or to negotiate.

D. By nominating another bank, or by allowing for negotiation by any bank, or by authorizing or requesting another bank to add its confirmation, the Issuing Bank authorizes such bank to pay, accept Draft(s) or negotiate as the case may be, against documents which appear on their face to be in compliance with the terms and conditions of the Credit and undertakes to reimburse such bank in accordance with the provisions of these Articles.

ARTICLE 11**Teletransmitted and Pre Advised Credit**

A. i. When an Issuing Bank instructs an Advising Bank by an authenticated teletransmission to advise a Credit or an amendment to a Credit, the teletransmission will be deemed to be the operative Credit instrument or the operative amendment, and no mail confirmation should be sent.

Should a mail confirmation nevertheless be sent, it will have no effect and the Advising Bank will have no obligation to check such mail confirmation against the operative Credit instrument or the operative amendment received by teletransmission.

ii. If the teletransmission states "full details to follow" (or words of similar effect) or states that the mail confirmation is to be the operative Credit instrument or the operative amendment, then the teletransmission will not be deemed to be the operative Credit instrument or the operative amendment. The Issuing Bank must forward the operative Credit instrument or the operative amendment to such Advising Bank without delay.

B. If a bank uses the services of an Advising Bank to have the Credit advised to the Beneficiary, it must also use the services of the same bank for advising an amendment(s).

C. A preliminary advice of the issuance or amendment of an irrevocable Credit (pre advice), shall only be given by an Issuing Bank if such bank is prepared to issue the operative Credit instrument or the operative amendment thereto. Unless otherwise stated in such preliminary advice by the Issuing Bank, an Issuing Bank having given such pre advice shall be irrevocably committed to issue or amend the Credit, in terms not inconsistent with the pre advice, without delay.

ARTICLE 12**Incomplete or Unclear Instructions**

If incomplete or unclear instructions are received to advise, confirm or amend a Credit, the bank requested to act on such instructions may give preliminary notification to the Beneficiary for information only and without responsibility. This preliminary notification should state clearly that the notification is provided for information only and without the responsibility of the Advising Bank. In any event, the Advising Bank must inform the Issuing Bank of the action taken and request it to provide the necessary information.

The Issuing Bank must provide the necessary information without delay. The Credit will be advised, confirmed or amended, only when complete and clear instructions have been received and if the Advising Bank is then prepared to act on the instructions.

LIABILITIES AND RESPONSIBILITIES**ARTICLE 13****Standard for Examination of Documents**

A. Banks must examine all documents stipulated in the Credit with reasonable care, to ascertain whether or not they appear, on their face, to be in compliance with the terms and conditions of the Credit. Compliance of the stipulated documents on their face with the terms and conditions of the Credit, shall be determined by international standard banking practice as reflected in these Articles.

Documents which appear on their face to be inconsistent with one another will be considered as not appearing on their face to be in compliance with the terms and conditions of the Credit.

Documents not stipulated in the Credit will not be examined by banks. If they receive such documents, they shall return them to the presenter or pass them on without responsibility.

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B. The Issuing Bank, the Confirming Bank, if any, or a Nominated Bank acting on their behalf, shall each have a reasonable time, not to exceed seven banking days following the day of receipt of the documents, to examine the documents and determine whether to take up or refuse the documents and to inform the party from which it received the documents accordingly.

C. If a Credit contains conditions without stating the document(s) to be presented in compliance therewith, banks will deem such conditions as not stated and will disregard them.

ARTICLE 14**Discrepant Documents and Notice**

A. When the Issuing Bank authorizes another bank to pay, incur a deferred payment undertaking, accept Draft(s), or negotiate against documents which appear on their face to be in compliance with the terms and conditions of the Credit, the Issuing Bank and the Confirming Bank, if any, are bound:

- i. to reimburse the Nominated Bank which has paid, incurred a deferred payment undertaking, accepted Draft(s), or negotiated,
- ii. to take up the documents.

B. Upon receipt of the documents the Issuing Bank and /or Confirming Bank, if any, or a Nominated Bank acting on their behalf, must determine on the basis of the documents alone whether or not they appear on their face to be in compliance with the terms and conditions of the Credit. If the documents appear on their face not to be in compliance with the terms and conditions of the Credit, such banks may refuse to take up the documents.

C. If the Issuing Bank determines that the documents appear on their face not to be in compliance with the terms and conditions of the Credit, it may in its sole judgment approach the Applicant for a waiver of the discrepancy(ies). This does not, however, extend the period mentioned in sub Article 13 (b).

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D. i. If the Issuing Bank and/or Confirming Bank, if any, or a Nominated Bank acting on their behalf, decides to refuse the documents, it must give notice to that effect by telecommunication or, if that is not possible, by other expeditious means, without delay but no later than the close of the seventh banking day following the day of receipt of the documents. Such notice shall be given to the bank from which it received the documents, or to the Beneficiary, if it received the documents directly from him.

ii. Such notice must state all discrepancies in respect of which the bank refuses the documents and must also state whether it is holding the documents at the disposal of, or is returning them to, the presenter.

iii. The Issuing Bank and/or Confirming Bank, if any, shall then be entitled to claim from the remitting bank refund, with interest, of any reimbursement which has been made to that bank.

E. If the Issuing Bank and/or Confirming Bank, if any, fails to act in accordance with the provisions of this Article and/or fails to hold the documents at the disposal of, or return them to the presenter, the Issuing Bank and/or Confirming Bank, if any, shall be precluded from claiming that the documents are not in compliance with the terms and conditions of the Credit.

F. If the remitting bank draws the attention of the Issuing Bank and/or Confirming Bank, if any, to any discrepancy(ies) in the document(s) or advises such banks that it has paid, incurred a deferred payment undertaking, accepted Draft(s) or negotiated under reserve or against an indemnity in respect of such discrepancy(ies), the Issuing Bank and/or Confirming Bank, if any, shall not be thereby relieved from any of their obligations under any provision of this Article. Such reserve or indemnity concerns only the relations between the remitting bank and the party towards whom the reserve was made, or from whom, or on whose behalf, the indemnity was obtained.

ARTICLE 15**Disclaimer on Effectiveness of Documents**

Banks assume no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document(s), or for the general and/or particular conditions stipulated in the document(s) or superimposed thereon; nor do they assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods represented by any document(s), or for the good faith or acts and/or omissions, solvency, performance or standing of the consignors, the carriers, the forwarders, the consignees or the insurers of the goods, or any other person whomsoever.

ARTICLE 16**Disclaimer on the Transmission of Messages**

Banks assume no liability or responsibility for the consequences arising out of delay and/or loss in transit of any message(s), letter(s) or document(s), or for delay, mutilation or other error(s) arising in the transmission of any telecommunication. Banks assume no liability or responsibility for errors in translation and/or interpretation of technical terms, and reserve the right to transmit Credit terms without translating them.

ARTICLE 17**Force Majeure**

Banks assume no liability or responsibility for the consequences arising out of the interruption of their business by Acts of God, riots, civil commotions, insurrections, wars or any other causes beyond their control, or by any strikes or lockouts. Unless specifically authorized, banks will not, upon resumption of their business, pay, incur a deferred payment undertaking, accept Draft(s) or negotiate under Credits which expired during such interruption of their business.

ARTICLE 18**Disclaimer for Acts of an Instructed Party**

A. Banks utilizing the services of another bank or other banks for the purpose of giving effect to the instructions of the Applicant do so for the account and at the risk of such Applicant.

B. Banks assume no liability or responsibility should the instructions they transmit not be carried out, even if they have themselves taken the initiative in the choice of such other bank(s).

C. i. A party instructing another party to perform services is liable for any charges, including commissions, fees, costs or expenses incurred by the instructed party in connection with its instructions.

ii. Where a credit stipulates that such charges are for the account of a party other than the instructing party, and charges cannot be collected, the instructing party remains ultimately liable for the payment thereof.

D. The Applicant shall be bound by and liable to indemnify the banks against all obligations and responsibilities imposed by foreign laws and usages.

ARTICLE 19**Bank to Bank Reimbursement Arrangements**

A. If an Issuing Bank intends that the reimbursement to which a paying, accepting or negotiating bank is entitled, shall be obtained by such bank (the "Claiming Bank"), claiming on another party (the "Reimbursing Bank"), it shall provide such Reimbursing Bank in good time with the proper instructions or authorization to honor such reimbursement claims.

B. Issuing Banks shall not require a Claiming Bank to supply a certificate of compliance with the terms and conditions of the Credit to the Reimbursing Bank.

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C. An Issuing Bank shall not be relieved from any of its obligations to provide reimbursement if and when reimbursement is not received by the Claiming Bank from the Reimbursing Bank.

D. The Issuing Bank shall be responsible to the Claiming Bank for any loss of interest if reimbursement is not provided by the Reimbursing Bank on first demand, or as otherwise specified in the Credit, or mutually agreed, as the case may be.

E. The Reimbursing Bank's charges should be for the account of the Issuing Bank. However, in cases where the charges are for the account of another party, it is the responsibility of the Issuing Bank to so indicate in the original Credit and in the reimbursement authorization. In cases where the Reimbursing Bank's charges are for the account of another party they shall be collected from the Claiming Bank when the Credit is drawn under. In cases where the Credit is not drawn under, the Reimbursing Bank's charges remain the obligation of the Issuing Bank.

DOCUMENTS**ARTICLE 20****Ambiguity as to the Issuers of Documents**

A. Terms such as "first class", "well known", "qualified", "independent", "official", "competent", "local", and the like, shall not be used to describe the issuers of any document(s) to be presented under a Credit. If such terms are incorporated in the Credit, banks will accept the relative document(s) as presented, provided that it appears on its face to be in compliance with the other terms and conditions of the Credit and not to have been issued by the Beneficiary.

B. Unless otherwise stipulated in the Credit, banks will also accept as an original document(s), a document(s) produced or appearing to have been produced: i. by reprographic, automated or computerized systems; ii. as carbon copies; provided that it is marked as original and, where necessary, appears to be signed.

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A document may be signed by handwriting, by facsimile signature, by perforated signature, by stamp, by symbol, or by any other mechanical or electronic method of authentication.

C. i. Unless otherwise stipulated in the Credit, banks will accept as a copy(ies), a document(s) either labeled copy or not marked as an original a copy(ies) need not be signed.

ii. Credits that require multiple document(s) such as "duplicate", "two fold", "two copies" and the like, will be satisfied by the presentation of one original and the remaining number in copies except where the document itself indicates otherwise.

D. Unless otherwise stipulated in the Credit, a condition under a Credit calling for a document to be authenticated, validated, legalized, visaed, certified or indicating a similar requirement, will be satisfied by any signature, mark, stamp or label on such document that on its face appears to satisfy the above condition.

ARTICLE 21

Unspecified Issuers or Contents of Documents When documents other than transport documents, insurance documents and commercial invoices are called for, the Credit should stipulate by whom such documents are to be issued and their wording or data content. If the Credit does not so stipulate, banks will accept such documents as presented, provided that their data content is not inconsistent with any other stipulated document presented.

ARTICLE 22**Issuance Date of Documents Vs. Credit Date**

Unless otherwise stipulated in the Credit, banks will accept a document bearing a date of issuance prior to that of the Credit, subject to such document being presented within the time limits set out in the Credit and in these Articles.

ARTICLE 23**Marine/Ocean Bill of Lading**

A. If a Credit calls for a bill of lading covering a port to port shipment, banks will, unless otherwise stipulated in the Credit, accept a document, however named, which:

i. appears on its face to indicate the name of the carrier and to have been signed or otherwise authenticated by:

- the carrier or a named agent for or on behalf of the carrier, or
- the master or a named agent for or on behalf of the master.

Any signature or authentication of the carrier or the master must be identified as carrier or master, as the case may be. An agent signing or authenticating for the carrier or master must also indicate the name and the capacity of the party, i.e. carrier or master, on whose behalf that agent is acting, and

ii. indicates that the goods have been loaded on board, or shipped on a named vessel.

Loading on board or shipment on a named vessel may be indicated by pre printed wording on the bill of lading that the goods have been loaded on board a named vessel or shipped on a named vessel, in which case the date of issuance of the bill of lading will be deemed to be the date of loading on board and the date of shipment.

In all other cases loading on board a named vessel must be evidenced by a notation on the bill of lading which gives the date on which the goods have been loaded on board, in which case the date of the board notation will be deemed to be the date of shipment. If the bill of lading contains the indication "intended vessel", or similar qualification in relation to the vessel, loading on board a named vessel must be evidenced by an on board notation on the bill of lading which, in addition to the date on which the goods have been loaded on board, also includes the name

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of the vessel on which the goods have been loaded, even if they have been loaded on the vessel named as the "intended vessel".

If the bill of lading indicates a place of receipt or taking in charge different from the port of loading, the on board notation must also include the port of loading stipulated in the Credit and the name of the vessel on which the goods have been loaded, even if they have been loaded on the vessel named in the bill of lading. This provision also applies whenever loading on board the vessel is indicated by pre printed wording on the bill of lading, and

iii. indicates the port of loading and the port of discharge stipulated in the Credit, notwithstanding that it:

a. indicates a place of taking in charge different from the port of loading, and/or a place of final destination different from the port of discharge, and/or

b. contains the indication "intended" or similar qualification in relation to the port of loading and/or port of discharge, as long as the document also states the ports of loading and/or discharge stipulated in the Credit, and

iv. consists of a sole original bill of lading or, if issued in more than one original, the full set as so issued, and

v. appears to contain all of the terms and conditions of carriage, or some of such terms and conditions by reference to a source or document other than the bill of lading (short form/blank back bill of lading); banks will not examine the contents of such terms and conditions, and

vi. contains no indication that it is subject to a charter party and/or no indication that the carrying vessel is propelled by sail only, and

vii. in all other respects meets the stipulations of the Credit.

B. For the purpose of this Article, transshipment means unloading and reloading from one vessel to another vessel during the course of ocean carriage from the port of loading to the port of discharge stipulated in the Credit.

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C. Unless transshipment is prohibited by the terms of the Credit, banks will accept a bill of lading which indicates that the goods will be transshipped, provided that the entire ocean carriage is covered by one and the same bill of lading.

D. Even if the Credit prohibits transshipment, banks will accept a bill of lading which:

i. indicates that the transshipment will take place as long as the relevant cargo is shipped in Container(s), Trailer(s) and/or "LASH" barge(s) as evidenced by the bill of lading, provided that the entire ocean carriage is covered by one and the same bill of lading, and/or ii. incorporates clauses stating that the carrier reserves the right to transship.

ARTICLE 24**Non Negotiable Sea Waybill**

A. If a Credit calls for a non negotiable sea waybill covering a port to port shipment, banks will, unless otherwise stipulated in the Credit, accept a document, however named, which:

i. appears on its face to indicate the name of the carrier and to have been signed or otherwise authenticated by:

- the carrier or a named agent for or on behalf of the carrier, or
- the master or a named agent for or on behalf of the master,

Any signature or authentication of the carrier or master must be identified as carrier or master, as the case may be. An agent signing or authenticating for the carrier or master must also indicate the name and the capacity of the party, i.e. carrier or master, on whose behalf that agent is acting, and

ii. indicates that the goods have been loaded on board, or shipped on a named vessel.

Loading on board or shipment on a named vessel may be indicated by pre printed wording on the nonnegotiable sea waybill that the goods have been loaded on

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board a named vessel or shipped on a named vessel, in which case the date of issuance of the non negotiable sea waybill will be deemed to be the date of loading on board and the date of shipment.

In all other cases loading on board a named vessel must be evidenced by a notation on the non negotiable sea waybill which gives the date on which the goods have been loaded on board, in which case the date of the on board notation will be deemed to be the date of shipment.

If the non negotiable sea waybill contains the indication "intended vessel", or similar qualification in relation to the vessel, loading on board a named vessel must be evidenced by an on board notation on the non negotiable sea waybill which, in addition to the date on which the goods have been loaded on board, includes the name of the vessel on which the goods have been loaded, even if they have been loaded on the vessel named as the "intended vessel".

If the non negotiable sea waybill indicates a place of receipt or taking in charge different from the port of loading, the on board notation must also include the port of loading stipulated in the Credit and the name of the vessel on which the goods have been loaded, even if they have been loaded on a vessel named in the nonnegotiable sea waybill. This provision also applies whenever loading on board the vessel is indicated by pre printed wording on the non negotiable sea waybill, and

iii. indicates the port of loading and the port of discharge stipulated in the Credit, notwithstanding that it:

a. indicates a place of taking in charge different from the port of loading, and/or a place of final destination different from the port of discharge, and/or

b. contains the indication "intended" or similar qualification in relation to the port of loading and/or port of discharge, as long as the document also states the ports of loading and/or discharge stipulated in the Credit, and

iv. consists of a sole original non negotiable sea waybill, or if issued in more than one original, the full set as so issued, and

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v. appears to contain all of the terms and conditions of carriage, or some of such terms and conditions by reference to a source or document other than the nonnegotiable sea waybill (short form/blank back nonnegotiable sea waybill); banks will not examine the contents of such terms and conditions, and

vi. contains no indication that it is subject to a charter party and/or no indication that the carrying vessel is propelled by sail only, and

vii. in all other respects meets the stipulations of the Credit.

B. For the purpose of this Article, transshipment means unloading and reloading from one vessel to another vessel during the course of ocean carriage from the port of loading to the port of discharge stipulated in the Credit.

C. Unless transshipment is prohibited by the terms of the Credit, banks will accept a non negotiable sea waybill which indicates that the goods will be transshipped, provided that the entire ocean carriage is covered by one and the same non negotiable sea waybill.

D. Even if the Credit prohibits transshipment, banks will accept a non negotiable sea waybill which:

i. indicates that transshipment will take place as long as the relevant cargo is shipped in Container(s), Trailer(s) and/or "LASH" barge(s) as evidenced by the nonnegotiable sea waybill, provided that the entire ocean carriage is covered by one and the same non negotiable sea waybill, and/or ii. incorporates clauses stating that the carrier reserves the right to transship.

ARTICLE 25**Charter Party Bill of Lading**

A. If a Credit calls for or permits a charter party bill of lading, banks will, unless otherwise stipulated in the Credit, accept a document, however named, which:

i. contains any indication that it is subject to a charter party, and

ii. appears on its face to have been signed or otherwise authenticated by:

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- the master or a named agent for or on behalf of the master, or
- the owner or a named agent for or on behalf of the owner.

Any signature or authentication of the master or owner must be identified as master or owner as the case may be. An agent signing or authenticating for the master or owner must also indicate the name and the capacity of the party, i.e. master or owner, on whose behalf that agent is acting, and

iii. does or does not indicate the name of the carrier, and

iv. indicates that the goods have been loaded on board or shipped on a named vessel.

Loading on board or shipment on a named vessel may be indicated by pre printed wording on the bill of lading that the goods have been loaded on board a named vessel or shipped on a named vessel, in which case the date of issuance of the bill of lading will be deemed to be the date of loading on board and the date of shipment.

In all other cases loading on board a named vessel must be evidenced by a notation on the bill of lading which gives the date on which the goods have been loaded on board, in which case the date of the on board notation will be deemed to be the date of shipment, and

v. indicates the port of loading and the port of discharge stipulated in the Credit, and

vi. consists of a sole original bill of lading or, if issued in more than one original, the full set as so issued, and

vii. contains no indication that the carrying vessel is propelled by sail only, and

viii. in all other respects meets the stipulations of the Credit.

B. Even if the Credit requires the presentation of a charter party contract in connection with a charter party bill of lading, banks will not examine such charter party contract, but will pass it on without responsibility on their part.

Article 26**Multimodal Transport Document**

A. If a Credit calls for a transport document covering at least two different modes of transport (multimodal transport), banks will, unless otherwise stipulated in the Credit, accept a document, however named, which:

i. appears on its face to indicate the name of the carrier or multimodal transport operator and to have been signed or otherwise authenticated by:

- the carrier or multimodal transport operator or a named agent for or on behalf of the carrier or multimodal transport operator, or
- the master or a named agent for or on behalf of the master.

Any signature or authentication of the carrier, multimodal transport operator or master must be identified as carrier, multimodal transport operator or master, as the case may be. An agent signing or authenticating for the carrier, multimodal transport operator or master must also indicate the name and the capacity of the party, i.e. carrier, multimodal transport operator or master, on whose behalf that the agent is acting, and

ii. indicates that the goods have been dispatched, taken in charge or loaded on board. Dispatch, taking in charge or loading on board may be indicated by wording to that effect on the multimodal transport document and the date of issuance will be deemed to be the date of dispatch, taking in charge or loading on board and the date of shipment. However, if the document indicates, by stamp or otherwise, a date of dispatch, taking in charge or loading on board, such date will be deemed to be the date of shipment, and

iii. a. indicates the place of taking in charge stipulated in the Credit which may be different from the port, airport or place of loading, and the place of final destination stipulated in the Credit which may be different from the port, airport or place of discharge, and/or

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- b. contains the indication "intended" or similar qualification in relation to the vessel and/or port of loading and/or port of discharge, and
- iv. consists of a sole original multimodal transport document or, if issued in more than one original, the full set as so issued, and
- v. appears to contain all of the terms and conditions of carriage, or some of such terms and conditions by reference to a source or document other than the multimodal transport document (short form/blank back multimodal transport document); banks will not examine the contents of such terms and conditions, and
- vi. contains no indication that it is subject to a charter party and/or no indication that the carrying vessel is propelled by sail only, and
- vii. in all other respects meets the stipulations of the Credit.

B. Even if the Credit prohibits transshipment, banks will accept a multimodal transport document which indicates that transshipment will or may take place, provided that the entire carriage is covered by one and the same multimodal transport document.

ARTICLE 27**Air Transport Document**

A. If a Credit calls for an air transport document, banks will, unless otherwise stipulated in the Credit, accept a document, however named, which:

i. appears on its face to indicate the name of the carrier and to have been signed or otherwise authenticated by:

- the carrier, or
- a named agent for or on behalf of the carrier.

Any signature or authentication of the carrier must be identified as carrier. An agent signing or authenticating for the carrier must also indicate the name and the capacity of the party, i.e. carrier, on whose behalf that agent is acting, and

ii. indicates that the goods have been accepted for carriage, and

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iii. where the Credit calls for an actual date of dispatch, indicates a specific notation of such date, the date of dispatch so indicated on the air transport document will be deemed to be the date of shipment.

For the purpose of this Article, the information appearing in the box on the air transport document (marked "For Carrier Use Only" or similar expression) relative to the flight number and date will not be considered as a specific notation of such date of dispatch.

In all other cases, the date of issuance of the air transport document will be deemed to be the date of shipment, and

iv. indicates the airport of departure and the airport of destination stipulated in the Credit, and

v. appears to be the original for consignor/shipper even if the Credit stipulates a full set of originals, or similar expressions, and

vi. appears to contain all of the terms and conditions of carriage, or some of such terms and conditions, by reference to a source or document other than the air transport document; banks will not examine the contents of such terms and conditions, and

vii. in all other respects meets the stipulations of the Credit.

B. For the purpose of this Article, transshipment means unloading and reloading from one aircraft to another aircraft during the course of carriage from the airport of departure to the airport of destination stipulated in the Credit.

C. Even if the Credit prohibits transshipment, banks will accept an air transport document which indicates that transshipment will or may take place, provided that the entire carriage is covered by one and the same air transport document.

ARTICLE 28**Road, Rail or inland Waterway Import Documents**

A. If a Credit calls for a road, rail, or inland waterway transport document, banks will, unless otherwise stipulated in the Credit, accept a document of the type called for, however named, which:

i. appears on its face to indicate the name of the carrier and to have been signed or otherwise authenticated by the carrier or a named agent for or on behalf of the carrier and/or to bear a reception stamp or other indication of receipt by the carrier or a named agent for or on behalf of the carrier.

Any signature, authentication, reception stamp or other indication of receipt of the carrier, must be identified on its face as that of the carrier. An agent signing or authenticating for the carrier must also indicate the name and the capacity of the party, i.e. carrier, on whose behalf that agent is acting, and

ii. indicates that the goods have been received for shipment, dispatch or carriage or wording to this effect. The date of issuance will be deemed to be the date of shipment unless the transport document contains a reception stamp, in which case the date of the reception stamp will be deemed to be the date of shipment, and

iii. indicates the place of shipment and the place of destination stipulated in the Credit, and

iv. in all other respects meets the stipulations of the Credit.

B. In the absence of any indication on the transport document as to the numbers issued, banks will accept the transport document(s) presented as constituting a full set. Banks will accept as original(s) the transport document(s) whether marked as original(s) or not.

C. For the purpose of this Article, transshipment means unloading and reloading from one means of conveyance to another means of conveyance, in different modes of transport, during the course of carriage from the place of shipment to the place of destination stipulated in the Credit.

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D. Even if the Credit prohibits transshipment, banks will accept a road, rail, or inland waterway transport document which indicates that transshipment will or may take place, provided that the entire carriage is covered by one and the same transport document and within the same mode of transport.

ARTICLE 29**Courier and Post Receipts**

A. If a Credit calls for a post receipt or certificate of posting, banks will, unless otherwise stipulated in the Credit, accept a post receipt or certificate of posting which:

i. appears on its face to have been stamped or otherwise authenticated and dated in the place from which the Credit stipulates the goods are to be shipped or dispatched and such date will be deemed to be the date of shipment or dispatch, and

ii. in all other respects meets the stipulations of the Credit.

B. If a Credit calls for a document issued by a courier or expedited delivery service evidencing receipt of the goods for delivery, banks will, unless otherwise stipulated in the Credit, accept a document, however named, which:

i. appears on its face to indicate the name of the courier/ service, and to have been stamped, signed or otherwise authenticated by such named courier/service (unless the Credit specifically calls for a document issued by a named Courier/Service, banks will accept a document issued by any Courier/Service), and

ii. indicates a date of pick up or of receipt or wording to this effect, such date being deemed to be the date of shipment or dispatch, and

iii. in all other respects meets the stipulations of the Credit.

ARTICLE 30**Transport Documents issued by Freight Forwarders**

Unless otherwise authorized in the Credit, banks will only accept a transport document issued by a freight forwarder if it appears on its face to indicate:

- i. the name of the freight forwarder as a carrier or multimodal transport operator and to have been signed or otherwise authenticated by the freight forwarder as carrier or multimodal transport operator, or
- ii. the name of the carrier or multimodal transport operator and to have been signed or otherwise authenticated by the freight forwarder as a named agent for or on behalf of the carrier or multimodal transport operator.

ARTICLE 31**"On Deck", "Shipper's Load and Count", Name of Consignor**

Unless otherwise stipulated in the Credit, banks will accept a transport document which:

- i. does not indicate, in the case of carriage by sea or by more than one means of conveyance including carriage by sea, that the goods are or will be loaded on deck. Nevertheless, banks will accept a transport document which contains a provision that the goods may be carried on deck, provided that it does not specifically state that they are or will be loaded on deck, and/or
- ii. bears a clause on the face thereof such as "shipper's load and count" or "said by shipper to contain" or words of similar effect, and/or
- iii. indicates as the consignor of the goods a party other than the Beneficiary of the Credit.

ARTICLE 32

Clean Transport Documents A. A clean transport document is one which bears no clause or notation which expressly declares a defective condition of the goods and/or the packaging.

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B. Banks will not accept transport documents bearing such clauses or notations unless the Credit expressly stipulates the clauses or notations which may be accepted.

C. Banks will regard a requirement in a Credit for a transport document to bear the clause "clean on board" as complied with if such transport document meets the requirements of this Article and of Articles 23, 24, 25, 26, 27, 28 or 30.

ARTICLE 33**Freight Payable/Prepaid Transport Documents**

A. Unless otherwise stipulated in the Credit, or inconsistent with any of the documents presented under the Credit, banks will accept transport documents stating that freight or transportation charges (hereafter referred to as "freight") have still to be paid.

B. If a Credit stipulates that the transport document has to indicate that freight has been paid or prepaid, banks will accept a transport document on which words clearly indicating payment or prepayment of freight appear by stamp or otherwise, or on which payment or prepayment of freight is indicated by other means. If the Credit requires courier charges to be paid or prepaid banks will also accept a transport document issued by a courier or expedited delivery service evidencing that the courier charges are for the account of a party other than the consignee.

C. The words "freight prepayable" or "freight to be prepaid" or words of similar effect, if appearing on transport documents, will not be accepted as constituting evidence of the payment of freight.

D. Banks will accept transport documents bearing reference by stamp or otherwise to costs additional to the freight, such as costs of, or disbursements incurred in connection with, loading, unloading or similar operations, unless the conditions of the Credit specifically prohibit such reference.

ARTICLE 34**Insurance Documents**

A. Insurance documents must appear on their face to be issued and signed by insurance companies or underwriters or their agents.

B. If the insurance document indicates that it has been issued in more than one original, all the originals must be presented unless otherwise authorized in the Credit.

C. Cover notes issued by brokers will not be accepted, unless specifically authorized in the Credit.

D. Unless otherwise stipulated in the Credit, banks will accept an insurance certificate or a declaration under an open cover pre signed by insurance companies or underwriters or their agents.

If a Credit specifically calls for an insurance certificate or a declaration under an open cover, banks will accept, in lieu thereof, an insurance policy.

E. Unless otherwise stipulated in the Credit, or unless it appears from the insurance document that the cover is effective at the latest from the date of loading on board or dispatch or taking in charge of the goods, banks will not accept an insurance document which bears a date of issuance later than the date of loading on board or dispatch or taking in charge as indicated in such transport document.

F. i. Unless otherwise stipulated in the Credit, the insurance document must be expressed in the same currency as the Credit.

ii. Unless otherwise stipulated in the Credit, the minimum amount for which the insurance document must indicate the insurance cover to have been effected is the CIF (cost, insurance and freight (... "named port of destination")) or CIP (carriage and insurance paid to (... "named place of destination")) value of the goods, as the case may be, plus 10%, but only when the CIF or CIP value can be determined from the documents on their face. Otherwise, banks will accept as such minimum

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amount 110% of the amount for which payment, acceptance or negotiation is requested under the Credit, or 110% of the gross amount of the invoice, whichever is the greater.

ARTICLE 35**Type of Insurance Cover**

A. Credits should stipulate the type of insurance required and, if any, the additional risks which are to be covered. Imprecise terms such as "usual risks" or "customary risks" shall not be used; if they are used, banks will accept insurance documents as presented, without responsibility for any risks not being covered.

B. Failing specific stipulations in the Credit, banks will accept insurance documents as presented, without responsibility for any risks not being covered.

C. Unless otherwise stipulated in the Credit, banks will accept an insurance document which indicates that the cover is subject to a franchise or an excess (deductible).

ARTICLE 36**All Risks Insurance Cover**

Where a Credit stipulates "insurance against all risks", banks will accept an insurance document which contains any "all risks" notation or clause, whether or not bearing the heading "all risks", even if the insurance document indicates that certain risks are excluded, without responsibility for any risk(s) not being covered.

ARTICLE 37**Commercial Invoices**

A. Unless otherwise stipulated in the Credit, commercial invoices;

i. must appear on their face to be issued by the Beneficiary named in the Credit (except as provided in Article 48), and

u. must be made out in the name of the Applicant (except as provided in sub Article 48 (H)), and

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iii. need not be signed.

B. Unless otherwise stipulated in the Credit, banks may refuse commercial invoices issued for amounts in excess of the amount permitted by the Credit. Nevertheless, if a bank authorized to pay, incur a deferred payment undertaking, accept Draft(s), or negotiate under a Credit accepts such invoices, its decision will be binding upon all parties, provided that such bank has not paid, incurred a deferred payment undertaking, accepted Draft(s) or negotiated for an amount in excess of that permitted by the Credit.

C. The description of the goods in the commercial invoice must correspond with the description in the Credit. In all other documents, the goods may be described in general terms not inconsistent with the description of the goods in the Credit.

ARTICLE 38**Other Documents**

If a Credit calls for an attestation or certification of weight in the case of transport other than by sea, banks will accept a weight stamp or declaration of weight which appears to have been superimposed on the transport document by the carrier or his agent unless the Credit specifically stipulates that the attestation or certification of weight must be by means of a separate document.

MISCELLANEOUS PROVISIONS**ARTICLE 39**

Allowances in Credit Amount, Quantity and Unit Price.

A. The words "about", "approximately", "circa" or similar expressions used in connection with the amount of the Credit or the quantity or the unit price stated in the Credit are to be construed as allowing a difference not to exceed 10% more or 10% less than the amount or the quantity or the unit price to which they refer.

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B. Unless a Credit stipulates that the quantity of the goods specified must not be exceeded or reduced, a tolerance of 5% more or 5% less will be permissible, always provided that the amount of the drawings does not exceed the amount of the Credit. This tolerance does not apply when the Credit stipulates the quantity in terms of a stated number of packing units or individual items.

C. Unless a Credit which prohibits partial shipments stipulates otherwise, or unless sub Article (B) above is applicable, a tolerance of 5% less in the amount of the drawing will be permissible, provided that if the Credit stipulates the quantity of the goods, such quantity of goods is shipped in full, and if the Credit stipulates a unit price, such price is not reduced. This provision does not apply when expressions referred to in sub Article (A) above are used in the Credit.

ARTICLE 40**Partial Shipments/Drawings**

A. Partial drawings and/or shipments are allowed, unless the Credit stipulates otherwise.

B. Transport documents which appear on their face to indicate that shipment has been made on the same means of conveyance and for the same journey, provided they indicate the same destination, will not be regarded as covering partial shipments, even if the transport documents indicate different dates of shipment and/or different ports of loading, places of taking in charge, or dispatch.

C. Shipments made by post or by courier will not be regarded as partial shipments if the post receipts or certificates of posting or courier's receipts or dispatch notes appear to have been stamped, signed or otherwise authenticated in the place from which the Credit stipulates the goods are to be dispatched, and on the same date.

ARTICLE 41**Installment Shipments/Drawings**

If drawings and/or shipments by installments within given periods are stipulated in the Credit and any installment is not drawn and/or shipped within the period

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allowed for that installment, the Credit ceases to be available for that and any subsequent installments, unless otherwise stipulated in the Credit.

ARTICLE 42**Expiry Date and Place for Presentation of Documents**

A. All Credits must stipulate an expiry date and a place for presentation of documents for payment, acceptance, or with the exception of freely negotiable Credits, a place for presentation of documents for negotiation. An expiry date stipulated for payment, acceptance or negotiation will be construed to express an expiry date for presentation of documents.

B. Except as provided in sub Article 44(A), documents must be presented on or before such expiry date.

C. If an Issuing Bank states that the Credit is to be available "for one month", "for six months", or the like, but does not specify the date from which the time is to run, the date of issuance of the Credit by the Issuing Bank will be deemed to be the first day from which such time is to run. Banks should discourage indication of the expiry date of the Credit in this manner.

ARTICLE 43**Limitation on the Expiry Date**

A. In addition to stipulating an expiry date for presentation of documents, every Credit which calls for a transport document(s) should also stipulate a specified period of time after the date of shipment during which presentation must be made in compliance with the terms and conditions of the Credit. If no such period of time is stipulated, banks will not accept documents presented to them later than 21 days after the date of shipment. In any event, documents must be presented not later than the expiry date of the Credit.

B. In cases in which sub Article 40(B) applies, the date of shipment will be considered to be the latest shipment date on any of the transport documents presented.

ARTICLE 44**Extension of Expiry Date**

A. If the expiry date of the Credit and/or the last day of the period of time for presentation of documents stipulated by the Credit or applicable by virtue of Article 43 falls on a day on which the bank to which presentation has to be made is closed for reasons other than those referred to in Article 17, the stipulated expiry date and/or the last day of the period of time after the date of shipment for presentation of documents, as the case may be, shall be extended to the first following day on which such bank is open.

B. The latest date for shipment shall not be extended by reason of the extension of the expiry date and/or the period of time after the date of shipment for presentation of documents in accordance with sub Article (A) above. If no such latest date for shipment is stipulated in the Credit or amendments thereto, banks will not accept transport documents indicating a date of shipment later than the expiry date stipulated in the Credit or amendments thereto.

C. The bank to which presentation is made on such first following business day must provide a statement that the documents were presented within the time limits extended in accordance with sub Article 44(A) of the Uniform Customs and Practice for Documentary Credits, 1993 Revision, ICC Publication No. 500.

ARTICLE 45**Hours of Presentation**

Banks are under no obligation to accept presentation of documents outside their banking hours.

ARTICLE 46**General Expressions as to Dates for Shipment**

A. Unless otherwise stipulated in the Credit, the expression "shipment" used in stipulating an earliest and/or a latest date for shipment will be understood to include expressions such as, "loading on board", "dispatch", "accepted for

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carriage", "date of post receipt", "date of pick up", and the like, and the case of a Credit calling for a multimodal transport document the expression "taking in charge".

B. Expressions such as "prompt", "immediately", "as soon as possible", and the like should not be used. If they are used banks will disregard them.

C. If the expression "on or about" or similar expressions are used, banks will interpret them as a stipulation that the shipment is to be made during the period from five days before to five days after the specified date, both end days included.

ARTICLE 47**Date Terminology for Periods of Shipment**

A. The words "to", "until", "till", "from" and words of similar import applying to any date or period in the Credit referring to shipment will be understood to include the date mentioned.

B. The word "after" will be understood to exclude the date mentioned.

C. The terms "first half", "second half of a month shall be construed respectively as the 1st to the 15th, and the 16th to the last day of such month, all dates inclusive.

D. The terms "beginning", "middle", or "end" of a month shall be construed respectively as the 1st to the 10th, the 11th to the 20th, and the 21st to the last day of such month, all dates inclusive.

TRANSFERABLE CREDIT**ARTICLE 48****Transferable Credit**

A. A transferable Credit is a Credit under which the Beneficiary (First Beneficiary) may request the bank authorized to pay, incur a deferred payment undertaking, accept or negotiate (the "Transferring Bank"), or in the case of a freely negotiable Credit, the bank specifically authorized in the Credit as a Transferring Bank, to

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make the Credit available in whole or in part to one or more other Beneficiary(ies) (Second Beneficiary(ies)).

B. A Credit can be transferred only if it is expressly designated as "transferable" by the Issuing Bank. Terms such as "divisible", "fractionable", "assignable", and "transmissible" do not render the Credit transferable. If such terms are used they shall be disregarded.

C. The Transferring Bank shall be under no obligation to effect such transfer except to the extent and in the manner expressly consented to by such bank.

D. At the time of making a request for transfer and prior to transfer of the Credit, the First Beneficiary must irrevocably instruct the Transferring Bank whether or not he retains the right to refuse to allow the Transferring Bank to advise amendments to the Second Beneficiary(ies). If the Transferring Bank consents to the transfer under these conditions, it must, at the time of transfer, advise the Second Beneficiary(ies) of the First Beneficiary's instructions regarding amendments.

E. If a Credit is transferred to more than one Second Beneficiary(ies), refusal of an amendment by one or more Second Beneficiary(ies) does not invalidate the acceptance(s) by the other Second Beneficiary(ies) with respect to whom the Credit will be amended accordingly. With respect to the Second Beneficiary(ies) who rejected the amendment, the Credit will remain unammended.

F. Transferring Bank charges in respect of transfers including commissions, fees, costs or expenses are payable by the First Beneficiary, unless otherwise agreed. If the Transferring Bank agrees to transfer the Credit it shall be under no obligation to effect the transfer until such charges are paid.

G. Unless otherwise stated in the Credit, a transferable Credit can be transferred once only. Consequently, the Credit cannot be transferred at the request of the Second Beneficiary to any subsequent Third Beneficiary. For the purpose of this Article, a retransfer to the First Beneficiary does not constitute a prohibited transfer. Fractions of a transferable Credit (not exceeding in the aggregate the

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amount of the Credit) can be transferred separately, provided partial shipment/drawings are not prohibited, and the aggregate of such transfers will be considered as constituting only one transfer of the Credit.

H. The Credit can be transferred only on the terms and conditions specified in the original Credit, with the exception of:

- the amount of the Credit,
- any unit price stated therein,
- the expiry date,
- the last date for presentation of documents in accordance with Article 43
- the period for shipment, any or all of which may be reduced or curtailed.

The percentage for which insurance cover must be effected may be increased in such a way as to provide the amount of cover stipulated in the original Credit, or these Articles.

In addition, the name of the First Beneficiary can be substituted for that of the Applicant, but if the name of the Applicant is specifically required by the original Credit to appear in any document(s) other than the invoice, such requirement must be fulfilled.

I. The First Beneficiary has the right to substitute his own invoice(s) (and Draft(s)) for those of the Second Beneficiary(ies), for amounts not in excess of the original amount stipulated in the Credit and for the original unit prices if stipulated in the Credit, and upon such substitution of invoice(s) (and Draft(s)) the First Beneficiary can draw under the Credit for the difference, if any, between his invoice(s) and the Second Beneficiaries(ies') invoice(s).

When a Credit has been transferred and the First Beneficiary is to supply his own invoice(s) (and Draft(s)) in exchange for the Second Beneficiary's(ies') invoices(s) (and Draft(s)) but fails to do so on first demand, the Transferring Bank has the right to deliver to the Issuing Bank the documents received under the transferred

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Credit, including the Second Beneficiary's(ies') invoice(s) (and Draft(s)) without further responsibility to the First Beneficiary.

J. The First Beneficiary may request that payment or negotiation be effected to the Second Beneficiary(ies) at the place to which the Credit has been transferred up to and including the expiry date of the Credit, unless the original Credit expressly states that it may not be made available for payment or negotiation at a place other than that stipulated in the Credit. This is without prejudice to the First Beneficiary's right to substitute subsequently his own invoice(s) (and Draft(s)) for those of the Second Beneficiary(ies) and to claim any difference due to him.

ASSIGNMENT OF PROCEEDS**ARTICLE 49****Assignment of Proceeds**

The fact that a Credit is not stated to be transferable shall not affect the Beneficiary's right to assign any proceeds to which he may be, or may become, entitled under such Credit, in accordance with the provisions of the applicable law. This Article relates only to the assignment of proceeds and not to the assignment of the right to perform under the Credit itself.

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Appendix B: U.C.C. - Article 5 - Letters of Credit

(Original Version)¹

§ 5-101. Short Title.

§ 5-102. Scope.

§ 5-103. Definitions.

§ 5-104. Formal Requirements; Signing.

§ 5-105. Consideration.

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§ 5-107. Advice of Credit; Confirmation; Error in Statement of Terms.

§ 5-108. "Notation Credit"; Exhaustion of Credit.

§ 5-109. Issuer's Obligation to Its Customer.

§ 5-110. Availability of Credit in Portions; Presenter's Reservation of Lien or Claim.

§ 5-111. Warranties on Transfer and Presentment.

§ 5-112. Time Allowed for Honor or Rejection; Withholding Honor or Rejection by Consent; "Presenter".

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§ 5-115. Remedy for Improper Dishonor or Anticipatory Repudiation.

§ 5-116. Transfer and Assignment.

§ 5-117. Insolvency of Bank Holding Funds for Documentary Credit.

§ 5-101. Short Title.

This Article shall be known and may be cited as Uniform Commercial Code-Letters of Credit.

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§ 5-102. Scope.**(1) This Article applies**

(a) to a credit issued by a bank if the credit requires a documentary draft or a documentary demand for payment; and

(b) to a credit issued by a person other than a bank if the credit requires that the draft or demand for payment be accompanied by a document of title; and

(c) to a credit issued by a bank or other person if the credit is not within subparagraphs (a) or (b) but conspicuously states that it is a letter of credit or is conspicuously so entitled.

(2) Unless the engagement meets the requirements of subsection (1), this Article does not apply to engagements to make advances or to honor drafts or demands for payment, to authorities to pay or purchase, to guarantees or to general agreements.

(3) This Article deals with some but not all of the rules and concepts of letters of credit as such rules or concepts have developed prior to this act or may hereafter develop. The fact that this Article states a rule does not by itself require, imply or negate application of the same or a converse rule to a situation not provided for or to a person not specified by this Article.

§ 5-103. Definitions.**(1) In this Article unless the context otherwise requires**

(a) "Credit" or "letter of credit" means an engagement by a bank or other person made at the request of a customer and of a kind within the scope of this Article (Section 5-102) that the issuer will honor drafts or other demands for payment upon compliance with the conditions specified in the credit. A credit may be either revocable or irrevocable. The engagement may be either an agreement to honor or a statement that the bank or other person is authorized to honor.

(b) A "documentary draft" or a "documentary demand for payment" is one honor of which is conditioned upon the presentation of a document or documents. "Document" means any paper including document of title, security, invoice, certificate, notice of default and the like.

(c) An "issuer" is a bank or other person issuing a credit.

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(d) A "beneficiary" of a credit is a person who is entitled under its terms to draw or demand payment.

(e) An "advising bank" is a bank which gives notification of the issuance of a credit by another bank.

(f) A "confirming bank" is a bank which engages either that it will itself honor a credit already issued by another bank or that such a credit will be honored by the issuer or a third bank.

(g) A "customer" is a buyer or other person who causes an issuer to issue a credit. The term also includes a bank which procures issuance or confirmation on behalf of that bank's customer.

(2) Other definitions applying to this Article and the sections in which they appear are:

"Notation Credit". Section 5-108.

"Presenter". Section 5-112(3).

(3) Definitions in other Articles applying to this Article and the sections in which they appear are:

"Accept" or "Acceptance". Section 3-409.

"Contract for sale". Section 2-106.

"Draft". Section 3-104.

"Holder in due course". Section 3-302.

"Midnight deadline". Section 4-104.

"Security". Section 8-102.

(4) In addition, Article 1 contains general definitions and principles of construction and interpretation

applicable throughout this Article.

§ 5-104. Formal Requirements; Signing.

(1) Except as otherwise required in subsection (1)(c) of Section 5-102 on scope, no particular form of phrasing is required for a credit. A credit must be in writing and signed by the issuer and a confirmation must be in writing and signed by the confirming bank. A modification of the terms of a credit or confirmation must be signed by the issuer or confirming bank.

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(2) A telegram may be a sufficient signed writing if it identifies its sender by an authorized authentication. The authentication may be in code and the authorized naming of the issuer in an advice of credit is a sufficient signing.

§ 5-105. Consideration.

No consideration is necessary to establish a credit or to enlarge or otherwise modify its terms.

§ 5-106. Time and Effect of Establishment of Credit.

(1) Unless otherwise agreed a credit is established

(a) as regards the customer as soon as a letter of credit is sent to him or the letter of credit or an authorized written advice of its issuance is sent to the beneficiary; and

(b) as regards the beneficiary when he receives a letter of credit or an authorized written advice of its issuance.

(2) Unless otherwise agreed once an irrevocable credit is established as regards the customer it can be modified or revoked only with the consent of the customer and once it is established as regards the beneficiary it can be modified or revoked only with his consent.

(3) Unless otherwise agreed after a revocable credit is established it may be modified or revoked by the issuer without notice to or consent from the customer or beneficiary.

(4) Notwithstanding any modification or revocation of a revocable credit any person authorized to honor or negotiate under the terms of the original credit is entitled to reimbursement for or honor of any draft or demand for payment duly honored or negotiated before receipt of notice of the modification or revocation and the issuer in turn is entitled to reimbursement from its customer.

§ 5-107. Advice of Credit; Confirmation; Error in Statement of Terms.

(1) Unless otherwise specified an advising bank by advising a credit issued by another bank does not assume any obligation to honor drafts drawn or demands for payment made under the credit but it does assume obligation for the accuracy of its own statement.

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(2) A confirming bank by confirming a credit becomes directly obligated on the credit to the extent of its confirmation as though it were its issuer and acquires the rights of an issuer.

(3) Even though an advising bank incorrectly advises the terms of a credit it has been authorized to advise the credit is established as against the issuer to the extent of its original terms.

(4) Unless otherwise specified the customer bears as against the issuer all risks of transmission and reasonable translation or interpretation of any message relating to a credit.

§ 5-108. "Notation Credit"; Exhaustion of Credit.

(1) A credit which specifies that any person purchasing or paying drafts drawn or demands for payment made under it must note the amount of the draft or demand on the letter or advice of credit is a "notation credit".

(2) Under a notation credit

(a) a person paying the beneficiary or purchasing a draft or demand for payment from him acquires a right to honor only if the appropriate notation is made and by transferring or forwarding for honor the documents under the credit such a person warrants to the issuer that the notation has been made; and

(b) unless the credit or a signed statement that an appropriate notation has been made accompanies the draft or demand for payment the issuer may delay honor until evidence of notation has been procured which is satisfactory to it but its obligation and that of its customer continue for a reasonable time not exceeding thirty days to obtain such evidence.

(3) If the credit is not a notation credit

(a) the issuer may honor complying drafts or demands for payment presented to it in the order in which they are presented and is discharged pro tanto by honor of any such draft or demand;

(b) as between competing good faith purchasers of complying drafts or demands the person first purchasing has priority over a subsequent purchaser even though the later purchased draft or demand has been first honored.

§ 5-109. Issuer's Obligation to Its Customer.

(1) An issuer's obligation to its customer includes good faith and observance of any general banking usage but unless otherwise agreed does not include liability or responsibility

(a) for performance of the underlying contract for sale or other transaction between the customer and the beneficiary; or

(b) for any act or omission of any person other than itself or its own branch or for loss or destruction of a draft, demand or document in transit or in the possession of others; or

(c) based on knowledge or lack of knowledge of any usage of any particular trade.

(2) An issuer must examine documents with care so as to ascertain that on their face they appear to comply with the terms of the credit but unless otherwise agreed assumes no liability or responsibility for the genuineness, falsification or effect of any document which appears on such examination to be regular on its face.

(3) A non-bank issuer is not bound by any banking usage of which it has no knowledge.

§ 5-110. Availability of Credit in Portions; Presenter's Reservation of Lien or Claim.

(1) Unless otherwise specified a credit may be used in portions in the discretion of the beneficiary.

(2) Unless otherwise specified a person by presenting a documentary draft or demand for payment under a credit relinquishes upon its honor all claims to the documents and a person by transferring such draft or demand or causing such presentment authorizes such relinquishment. An explicit reservation of claim makes the draft or demand non-complying.

§ 5-111. Warranties on Transfer and Presentment.

(1) Unless otherwise agreed the beneficiary by transferring or presenting a documentary draft or demand for payment warrants to all interested parties that the necessary conditions of the credit have been complied with. This is in addition to any warranties arising under Articles 3, 4, 7 and 8.

(2) Unless otherwise agreed a negotiating, advising, confirming, collecting or issuing bank presenting or transferring a draft or demand for payment under a credit warrants only the matters warranted by a collecting bank under Article 4 and any such bank transferring a document warrants only the matters warranted by an intermediary under Articles 7 and 8.

§ 5-112. Time Allowed for Honor or Rejection; Withholding Honor or Rejection by Consent; "Presenter".

(1) A bank to which a documentary draft or demand for payment is presented under a credit may without dishonor of the draft, demand or credit

(a) defer honor until the close of the third banking day following receipt of the documents; and

(b) further defer honor if the presenter has expressly or impliedly consented thereto.

Failure to honor within the time here specified constitutes dishonor of the draft or demand and of the credit [except as otherwise provided in subsection (4) of Section 5-114 on conditional payment].

Note: The bracketed language in the last sentence of subsection (1) should be included only if the optional provisions of Section 5-114(4) and (5) are included.

(2) Upon dishonor the bank may unless otherwise instructed fulfill its duty to return the draft or demand and the documents by holding them at the disposal of the presenter and sending him an advice to that effect.

(3) "Presenter" means any person presenting a draft or demand for payment for honor under a credit even though that person is a confirming bank or other correspondent which is acting under an issuer's authorization.

§ 5-113. Indemnities.

(1) A bank seeking to obtain (whether for itself or another) honor, negotiation or reimbursement under a credit may give an indemnity to induce such honor, negotiation or reimbursement.

(2) An indemnity agreement inducing honor, negotiation or reimbursement

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(a) unless otherwise explicitly agreed applies to defects in the documents but not in the goods; and

(b) unless a longer time is explicitly agreed expires at the end of ten business days following receipt of the documents by the ultimate customer unless notice of objection is sent before such expiration date. The ultimate customer may send notice of objection to the person from whom he received the documents and any bank receiving such notice is under a duty to send notice to its transferor before its midnight deadline.

§ 5-114. Issuer's Duty and Privilege to Honor; Right to Reimbursement.

(1) An issuer must honor a draft or demand for payment which complies with the terms of the relevant credit regardless of whether the goods or documents conform to the underlying contract for sale or other contract between the customer and the beneficiary. The issuer is not excused from honor of such a draft or demand by reason of an additional general term that all documents must be satisfactory to the issuer, but an issuer may require that specified documents must be satisfactory to it.

(2) Unless otherwise agreed when documents appear on their face to comply with the terms of a credit but a required document does not in fact conform to the warranties made on negotiation or transfer of a document of title (Section 7-507) or of a certificated security (Section 8-306) or is forged or fraudulent or there is fraud in the transaction:

(a) the issuer must honor the draft or demand for payment if honor is demanded by a negotiating bank or other holder of the draft or demand which has taken the draft or demand under the credit and under circumstances which would make it a holder in due course. (Section 3-302) and in an appropriate case would make it a person to whom a document of title has been duly negotiated (Section 7-502) or a bona fide purchaser of a certificated security (Section 8-302); and

(b) in all other cases as against its customer, an issuer acting in good faith may honor the draft or demand for payment despite notification from the customer of fraud, forgery or other defect not apparent on the face of the documents but a court of appropriate jurisdiction may enjoin such honor.

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(3) Unless otherwise agreed an issuer which has duly honored a draft or demand for payment is entitled to immediate reimbursement of any payment made under the credit and to be put in effectively available funds not later than the day before maturity of any acceptance made under the credit.

[(4) When a credit provides for payment by the issuer on receipt of notice that the required documents are in the possession of a correspondent or other agent of the issuer

(a) any payment made on receipt of such notice is conditional; and

(b) the issuer may reject documents which do not comply with the credit if it does so within three banking days following its receipt of the documents; and

(c) in the event of such rejection, the issuer is entitled by charge back or otherwise to return of the payment made.]

[(5) In the case covered by subsection (4) failure to reject documents within the time specified in sub-paragraph (b) constitutes acceptance of the documents and makes the payment final in favor of the beneficiary.]

Note: Subsections (4) and (5) are bracketed as optional. If they are included the bracketed

language in the last sentence of Section 5-112(1) should also be included.

[As amended in 1977.]

§ 5-115. Remedy for Improper Dishonor or Anticipatory Repudiation.

(1) When an issuer wrongfully dishonors a draft or demand for payment presented under a credit the person entitled to honor has with respect to any documents the rights of a person in the position of a seller (Section 2-707) and may recover from the issuer the face amount of the draft or demand together with incidental damages under Section 2-710 on seller's incidental damages and interest but less any amount realized by resale or other use or disposition of the subject matter of the transaction.

In the event no resale or other utilization is made the documents, goods or other subject matter involved in the transaction must be turned over to the issuer on payment of judgment.

(2) When an issuer wrongfully cancels or otherwise repudiates a credit before presentment of a draft or demand for payment drawn under it the beneficiary has the rights of a seller after anticipatory repudiation by the buyer under Section 2-610 if he learns of the repudiation in time reasonably to avoid procurement of the required documents. Otherwise the beneficiary has an immediate right of action for wrongful dishonor.

§ 5-116. Transfer and Assignment.

(1) The right to draw under a credit can be transferred or assigned only when the credit is expressly designated as transferable or assignable.

(2) Even though the credit specifically states that it is nontransferable or nonassignable the beneficiary may before performance of the conditions of the credit assign his right to proceeds. Such an assignment is an assignment of an account under Article 9 on Second Transactions and is governed by that Article except that

(a) the assignment is ineffective until the letter of credit or advice of credit is delivered to the assignee which delivery constitutes perfection of the security interest under Article 9; and

(b) the issuer may honor drafts or demands for payment drawn under the credit until it receives a notification of the assignment signed by the beneficiary which reasonably identifies the credit involved in the assignment and contains a request to pay the assignee; and

(c) after what reasonably appears to be such a notification has been received the issuer may without dishonor refuse to accept or pay even to a person otherwise entitled to honor until the letter of credit or advice of credit is exhibited to the issuer.

(3) Except where the beneficiary has effectively assigned his right to draw or his right to proceeds, nothing in this section limits his right to transfer or negotiate drafts or demands drawn under the credit.

[As amended in 1972.]

§ 5-117. Insolvency of Bank Holding Funds for Documentary Credit.

(1) Where an issuer or an advising or confirming bank or a bank which has for a customer procured issuance of a credit by another bank becomes insolvent before final payment under the credit and the credit is one to which this Article is made applicable by paragraphs (a) or (b) of Section 5-102(1) on scope, the receipt or allocation of funds or collateral to secure or meet obligations under the credit shall have the following results:

(a) to the extent of any funds or collateral turned over after or before the insolvency as indemnity against or specifically for the purpose of payment of drafts or demands for payment drawn under the designated credit, the drafts or demands are entitled to payment in preference over depositors or other general creditors of the issuer or bank; and

(b) on expiration of the credit or surrender of the beneficiary's rights under it unused any person who has given such funds or collateral is similarly entitled to return thereof; and

(c) a charge to a general or current account with a bank if specifically consented to for the purpose of indemnity against or payment of drafts or demands for payment drawn under the designated credit falls under the same rules as if the funds had been drawn out in cash and then turned over with specific instructions.

(2) After honor or reimbursement under this section the customer or other person for whose account the insolvent bank has acted is entitled to receive the documents involved.

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Appendix C: U.C.C. - Article 5 - Letters of Credit (Revised 1995)¹

§ 5-101. Short Title.

§ 5-102. Definitions.

§ 5-103. Scope.

§ 5-104. Formal Requirements.

§ 5-105. Consideration.

§ 5-106. Issuance, Amendment, Cancellation, and Duration.

§ 5-107. Confirmer, Nominated Person, and Adviser.

§ 5-108. Issuer's Rights and Obligations

§ 5-109. Fraud and Forgery.

§ 5-110. Warranties.

§ 5-111. Remedies.

§ 5-112. Transfer of Letter of Credit.

§ 5-113. Transfer by Operation of Law.

§ 5-114. Assignment of Proceeds.

§ 5-115. Statute of Limitations.

§ 5-116. Choice of Law and Forum.

§ 5-117. Subrogation of Issuer, Applicant, and Nominated Person.

§ 5-101. Short Title.

This Article shall be known and may be cited as Uniform Commercial Code-Letters of Credit.

§ 5-102. Definitions.

(a) In this article:

(1) "Adviser" means a person who, at the request of the issuer, a confirmer, or another adviser, notifies or requests another adviser to notify the beneficiary that a letter of credit has been issued, confirmed, or amended.

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(2) "Applicant" means a person at whose request or for whose account a letter of credit is issued. The term includes a person who requests an issuer to issue a letter of credit on behalf of another if the person making the request undertakes an obligation to reimburse the issuer.

(3) "Beneficiary" means a person who under the terms of a letter of credit is entitled to have its complying presentation honored. The term includes a person to whom drawing rights have been transferred under a transferable letter of credit .

(4) "Confirmer" means a nominated person who undertakes, at the request or with the consent of the issuer, to honor a presentation under a letter of credit issued by another.

(5) "Dishonor" of a letter of credit means failure timely to honor or to take an interim action, such as acceptance of a draft, that may be required by the letter of credit.

(6) "Document" means a draft or other demand, document of title, investment security, certificate, invoice, or other record, statement, or representation of fact, law, right, or opinion (i) which is presented in a written or other medium permitted by the letter of credit or, unless prohibited by the letter of credit, by the standard practice referred to in Section 5-108(e) and (ii) which is capable of being examined for compliance with the terms and conditions of the letter of credit. A document may not be oral.

(7) "Good faith" means honesty in fact in the conduct or transaction concerned.

(8) "Honor" of a letter of credit means performance of the issuer's undertaking in the letter of credit to pay or deliver an item of value. Unless the letter of credit otherwise provides, "honor" occurs

(i) upon payment,

(ii) if the letter of credit provides for acceptance, upon acceptance of a draft and, at maturity, its payment, or

(iii) if the letter of credit provides for incurring a deferred obligation, upon incurring the obligation and, at maturity, its performance.

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(9) "Issuer" means a bank or other person that issues a letter of credit, but does not include an individual who makes an engagement for personal, family, or household purposes.

(10) "Letter of credit" means a definite undertaking that satisfies the requirements of Section 5-104 by an issuer to a beneficiary at the request or for the account of an applicant or, in the case of a financial institution, to itself or for its own account, to honor a documentary presentation by payment or delivery of an item of value .

(11) "Nominated person" means a person whom the issuer (i) designates or authorizes to pay, accept, negotiate, or otherwise give value under a letter of credit and (ii) undertakes by agreement or custom and practice to reimburse.

(12) "Presentation" means delivery of a document to an issuer or nominated person for honor or giving of value under a letter of credit .

(13) "Presenter" means a person making a presentation as or on behalf of a beneficiary or nominated person.

(14) "Record" means information that is inscribed on a tangible medium, or that is stored in an electronic or other medium and is retrievable in perceivable form.

(15) "Successor of a beneficiary" means a person who succeeds to substantially all of the rights of a beneficiary by operation of law, including a corporation with or into which the beneficiary has been merged or consolidated, an administrator, executor, personal representative, trustee in bankruptcy, debtor in possession, liquidator, and receiver.

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(b) Definitions in other Articles applying to this article and the sections in which they appear are:

"Accept" or "Acceptance" Section 3-409

"Value" Sections 3-303, 4-211

(c) Article 1 contains certain additional general definitions and principles of construction and interpretation applicable throughout this article.

§ 5-103. Scope.

(a) This article applies to letters of credit and to certain rights and obligations arising out of transactions involving letters of credit.

(b) The statement of a rule in this article does not by itself require, imply, or negate application of the same or a different rule to a situation not provided for, or to a person not specified, in this article.

(c) With the exception of this subsection, subsections (a) and (d), Sections 5-102(a) (9) and (10), 5-106(d), and 5-114(d), and except to the extent prohibited in Sections 1-102(3) and 5-117(d), the effect of this article may be varied by agreement or by a provision stated or incorporated by reference in an undertaking. A term in an agreement or undertaking generally excusing liability or generally limiting remedies for failure to perform obligations is not sufficient to vary obligations prescribed by this article.

(d) Rights and obligations of an issuer to a beneficiary or a nominated person under a letter of credit are independent of the existence, performance, or nonperformance of a contract or arrangement out of which the letter of credit arises or which underlies it, including contracts or arrangements between the issuer and the applicant and between the applicant and the beneficiary.

§ 5-104. Formal Requirements.

A letter of credit, confirmation, advice, transfer, amendment, or cancellation may be issued in any form that is a record and is authenticated (i) by a signature or (ii) in accordance with the agreement of the parties or the standard practice referred to in Section 5-108(e).

§ 5-105. Consideration.

Consideration is not required to issue, amend, transfer, or cancel a letter of credit, advice, or confirmation.

§ 5-106. Issuance, Amendment, Cancellation, and Duration.

(a) A letter of credit is issued and becomes enforceable according to its terms against the issuer when the issuer sends or otherwise transmits it to the person requested to advise or to the beneficiary. A letter of credit is revocable only if it so provides.

(b) After a letter of credit is issued, rights and obligations of a beneficiary, applicant, confirmer, and issuer are not affected by an amendment or cancellation to which that person has not consented except to the extent the letter of credit provides that it is revocable or that the issuer may amend or cancel the letter of credit without that consent.

(c) If there is no stated expiration date or other provision that determines its duration, a letter of credit expires one year after its stated date of issuance or, if none is stated, after the date on which it is issued.

(d) A letter of credit that states that it is perpetual expires five years after its stated date of issuance, or if none is stated, after the date on which it is issued.

§ 5-107. Confirmer, Nominated Person, and Adviser.

(a) A confirmer is directly obligated on a letter of credit and has the rights and obligations of an issuer to the extent of its confirmation. The confirmer also has

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rights against and obligations to the issuer as if the issuer were an applicant and the confirmer had issued the letter of credit at the request and for the account of the issuer.

(b) A nominated person who is not a confirmer is not obligated to honor or otherwise give value for a presentation .

(c) A person requested to advise may decline to act as an adviser. An adviser that is not a confirmer is not obligated to honor or give value for a presentation. An adviser undertakes to the issuer and to the beneficiary accurately to advise the terms of the letter of credit, confirmation, amendment, or advice received by that person and undertakes to the beneficiary to check the apparent authenticity of the request to advise. Even if the advice is inaccurate, the letter of credit, confirmation, or amendment is enforceable as issued.

(d) A person who notifies a transferee beneficiary of the terms of a letter of credit, confirmation, amendment, or advice has the rights and obligations of an adviser under subsection (c). The terms in the notice to the transferee beneficiary may differ from the terms in any notice to the transferor beneficiary to the extent permitted by the letter of credit, confirmation, amendment, or advice received by the person who so notifies.

§ 5-108. Issuer's Rights and Obligations

(a) Except as otherwise provided in Section 5-109, an issuer shall honor a presentation that, as determined by the standard practice referred to in subsection (e), appears on its face strictly to comply with the terms and conditions of the letter of credit. Except as otherwise provided in Section 5-113 and unless otherwise agreed with the applicant, an issuer shall dishonor a presentation that does not appear so to comply.

(b) An issuer has a reasonable time after presentation , but not beyond the end of the seventh business day of the issuer after the day of its receipt of documents:

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(1) to honor,

(2) if the letter of credit provides for honor to be completed more than seven business days after presentation, to accept a draft or incur a deferred obligation, or

(3) to give notice to the presenter of discrepancies in the presentation.

(c) Except as otherwise provided in subsection (d), an issuer is precluded from asserting as a basis for dishonor any discrepancy if timely notice is not given, or any discrepancy not stated in the notice if timely notice is given.

(d) Failure to give the notice specified in subsection (b) or to mention fraud, forgery, or expiration in the notice does not preclude the issuer from asserting as a basis for dishonor fraud or forgery as described in Section 5-109(a) or expiration of the letter of credit before presentation.

(e) An issuer shall observe standard practice of financial institutions that regularly issue letters of credit. Determination of the issuer's observance of the standard practice is a matter of interpretation for the court. The court shall offer the parties a reasonable opportunity to present evidence of the standard practice.

(f) An issuer is not responsible for:

(1) the performance or nonperformance of the underlying contract, arrangement, or transaction,

(2) an act or omission of others, or

(3) observance or knowledge of the usage of a particular trade other than the standard practice referred to in subsection (e).

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(g) If an undertaking constituting a letter of credit under Section 5-102(a) (10) contains nondocumentary conditions, an issuer shall disregard the nondocumentary conditions and treat them as if they were not stated.

(h) An issuer that has dishonored a presentation shall return the documents or hold them at the disposal of, and send advice to that effect to, the presenter.

(i) An issuer that has honored a presentation as permitted or required by this article:

(1) is entitled to be reimbursed by the applicant in immediately available funds not later than the date of its payment of funds;

(2) takes the documents free of claims of the beneficiary or presenter;

(3) is precluded from asserting a right of recourse on a draft under Sections 3-414 and 3-415;

(4) except as otherwise provided in Sections 5-110 and 5-117, is precluded from restitution of money paid or other value given by mistake to the extent the mistake concerns discrepancies in the documents or tender which are apparent on the face of the presentation; and

(5) is discharged to the extent of its performance under the letter of credit unless the issuer honored a presentation in which a required signature of a beneficiary was forged.

§ 5-109. Fraud and Forgery.

(a) If a presentation is made that appears on its face strictly to comply with the terms and conditions of the letter of credit, but a required document is forged or

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materially fraudulent, or honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant :

(1) the issuer shall honor the presentation, if honor is demanded by (i) a nominated person who has given value in good faith and without notice of forgery or material fraud, (ii) a confirmer who has honored its confirmation in good faith, (iii) a holder in due course of a draft drawn under the letter of credit which was taken after acceptance by the issuer or nominated person, or (iv) an assignee of the issuer's or nominated person's deferred obligation that was taken for value and without notice of forgery or material fraud after the obligation was incurred by the issuer or nominated person; and

(2) the issuer, acting in good faith, may honor or dishonor the presentation in any other case.

(b) If an applicant claims that a required document is forged or materially fraudulent or that honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant, a court of competent jurisdiction may temporarily or permanently enjoin the issuer from honoring a presentation or grant similar relief against the issuer or other persons only if the court finds that:

(1) the relief is not prohibited under the law applicable to an accepted draft or deferred obligation incurred by the issuer;

(2) a beneficiary, issuer, or nominated person who may be adversely affected is adequately protected against loss that it may suffer because the relief is granted;

(3) all of the conditions to entitle a person to the relief under the law of this State have been met; and

(4) on the basis of the information submitted to the court, the applicant is more likely than not to succeed under its claim of forgery or material fraud and the person demanding honor does not qualify for protection under subsection (a)(1).

§ 5-110. Warranties.

(a) If its presentation is honored, the beneficiary warrants:

(1) to the issuer, any other person to whom presentation is made, and the applicant that there is no fraud or forgery of the kind described in Section 5-109(a); and

(2) to the applicant that the drawing does not violate any agreement between the applicant and beneficiary or any other agreement intended by them to be augmented by the letter of credit.

(b) The warranties in subsection (a) are in addition to warranties arising under Article 3, 4, 7, and 8 because of the presentation or transfer of documents covered by any of those articles.

§ 5-111. Remedies.

(a) If an issuer wrongfully dishonors or repudiates its obligation to pay money under a letter of credit before presentation, the beneficiary, successor, or nominated person presenting on its own behalf may recover from the issuer the amount that is the subject of the dishonor or repudiation. If the issuer's obligation under the letter of credit is not for the payment of money, the claimant may obtain specific performance or, at the claimant's election, recover an amount equal to the value of performance from the issuer. In either case, the claimant may also recover incidental but not consequential damages. The claimant is not obligated to take action to avoid damages that might be due from the issuer under this subsection. If, although not obligated to do so, the claimant avoids damages, the claimant's recovery from the issuer must be reduced by the amount of damages avoided. The issuer has the burden of proving the amount of damages avoided. In the case of repudiation the claimant need not present any document.

(b) If an issuer wrongfully dishonors a draft or demand presented under a letter of credit or honors a draft or demand in breach of its obligation to the applicant, the applicant may recover damages resulting from the breach, including incidental but not consequential damages, less any amount saved as a result of the breach.

(c) If an adviser or nominated person other than a confirmer breaches an obligation under this article or an issuer breaches an obligation not covered in subsection (a) or (b), a person to whom the obligation is owed may recover damages resulting from the breach, including incidental but not consequential damages, less any amount saved as a result of the breach. To the extent of the confirmation, a confirmer has the liability of an issuer specified in this subsection and subsections (a) and (b).

(d) An issuer, nominated person, or adviser who is found liable under subsection (a), (b), or (c) shall pay interest on the amount owed thereunder from the date of wrongful dishonor or other appropriate date.

(e) Reasonable attorney's fees and other expenses of litigation must be awarded to the prevailing party in an action in which a remedy is sought under this article.

(f) Damages that would otherwise be payable by a party for breach of an obligation under this article may be liquidated by agreement or undertaking, but only in an amount or by a formula that is reasonable in light of the harm anticipated.

§ 5-112. Transfer of Letter of Credit.

(a) Except as otherwise provided in Section 5-113, unless a letter of credit provides that it is transferable, the right of a beneficiary to draw or otherwise demand performance under a letter of credit may not be transferred.

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(b) Even if a letter of credit provides that it is transferable, the issuer may refuse to recognize or carry out a transfer if:

(1) the transfer would violate applicable law; or

(2) the transferor or transferee has failed to comply with any requirement stated in the letter of credit or any other requirement relating to transfer imposed by the issuer which is within the standard practice referred to in Section 5-108(e) or is otherwise reasonable under the circumstances.

§ 5-113. Transfer by Operation of Law.

(a) A successor of a beneficiary may consent to amendments, sign and present documents, and receive payment or other items of value in the name of the beneficiary without disclosing its status as a successor.

(b) A successor of a beneficiary may consent to amendments, sign and present documents, and receive payment or other items of value in its own name as the disclosed successor of the beneficiary. Except as otherwise provided in subsection (e), an issuer shall recognize a disclosed successor of a beneficiary as beneficiary in full substitution for its predecessor upon compliance with the requirements for recognition by the issuer of a transfer of drawing rights by operation of law under the standard practice referred to in Section 5-108(e) or, in the absence of such a practice, compliance with other reasonable procedures sufficient to protect the issuer.

(c) An issuer is not obliged to determine whether a purported successor is a successor of a beneficiary or whether the signature of a purported successor is genuine or authorized.

(d) Honor of a purported successor's apparently complying presentation under subsection (a) or (b) has the consequences specified in Section 5-108(i) even if the purported successor is not the successor of a beneficiary. Documents signed in the

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name of the beneficiary or of a disclosed successor by a person who is neither the beneficiary nor the successor of the beneficiary are forged documents for the purposes of Section 5-109.

(e) An issuer whose rights of reimbursement are not covered by subsection (d) or substantially similar law and any confirmer or nominated person may decline to recognize a presentation under subsection (b).

(f) A beneficiary whose name is changed after the issuance of a letter of credit has the same rights and obligations as a successor of a beneficiary under this section.

§ 5-114. Assignment of Proceeds.

(a) In this section, "proceeds of a letter of credit" means the cash, check, accepted draft, or other item of value paid or delivered upon honor or giving of value by the issuer or any nominated person under the letter of credit. The term does not include a beneficiary's drawing rights or documents presented by the beneficiary.

(b) A beneficiary may assign its right to part or all of the proceeds of a letter of credit. The beneficiary may do so before presentation as a present assignment of its right to receive proceeds contingent upon its compliance with the terms and conditions of the letter of credit.

(c) An issuer or nominated person need not recognize an assignment of proceeds of a letter of credit until it consents to the assignment.

(d) An issuer or nominated person has no obligation to give or withhold its consent to an assignment of proceeds of a letter of credit, but consent may not be unreasonably withheld if the assignee possesses and exhibits the letter of credit and presentation of the letter of credit is a condition to honor.

(e) Rights of a transferee beneficiary or nominated person are independent of the beneficiary's assignment of the proceeds of a letter of credit and are superior to the assignee's right to the proceeds.

(f) Neither the rights recognized by this section between an assignee and an issuer, transferee beneficiary, or nominated person nor the issuer's or nominated person's payment of proceeds to an assignee or a third person affect the rights between the assignee and any person other than the issuer, transferee beneficiary, or nominated person. The mode of creating and perfecting a security interest in or granting an assignment of a beneficiary's rights to proceeds is governed by Article 9 or other law. Against persons other than the issuer, transferee beneficiary, or nominated person, the rights and obligations arising upon the creation of a security interest or other assignment of a beneficiary's right to proceeds and its perfection are governed by Article 9 or other law.

§ 5-115. Statute of Limitations.

An action to enforce a right or obligation arising under this article must be commenced within one year after the expiration date of the relevant letter of credit or one year after the [claim for relief] [cause of action] accrues, whichever occurs later. A [claim for relief] [cause of action] accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach.

§ 5-116. Choice of Law and Forum.

(a) The liability of an issuer, nominated person, or adviser for action or omission is governed by the law of the jurisdiction chosen by an agreement in the form of a record signed or otherwise authenticated by the affected parties in the manner provided in Section 5-104 or by a provision in the person's letter of credit, confirmation, or other undertaking. The jurisdiction whose law is chosen need not bear any relation to the transaction.

(b) Unless subsection (a) applies, the liability of an issuer, nominated person, or adviser for action or omission is governed by the law of the jurisdiction in which the person is located. The person is considered to be located at the address

indicated in the person's undertaking. If more than one address is indicated, the person is considered to be located at the address from which the person's undertaking was issued. For the purpose of jurisdiction, choice of law, and recognition of interbranch letters of credit, but not enforcement of a judgment, all branches of a bank are considered separate juridical entities and a bank is considered to be located at the place where its relevant branch is considered to be located under this subsection.

(c) Except as otherwise provided in this subsection, the liability of an issuer, nominated person, or adviser is governed by any rules of custom or practice, such as the Uniform Customs and Practice for Documentary Credits, to which the letter of credit, confirmation, or other undertaking is expressly made subject. If (i) this article would govern the liability of an issuer, nominated person, or adviser under subsection (a) or (b), (ii) the relevant undertaking incorporates rules of custom or practice, and (iii) there is conflict between this article and those rules as applied to that undertaking, those rules govern except to the extent of any conflict with the nonvariable provisions specified in Section 5-103(c).

(d) If there is conflict between this article and Article 3, 4, 4A, or 9, this article governs.

(e) The forum for settling disputes arising out of an undertaking within this article may be chosen in the manner and with the binding effect that governing law may be chosen in accordance with subsection (a).

§ 5-117. Subrogation of Issuer, Applicant, and Nominated Person.

(a) An issuer that honors a beneficiary's presentation is subrogated to the rights of the beneficiary to the same extent as if the issuer were a secondary obligor of the underlying obligation owed to the beneficiary and of the applicant to the same extent as if the issuer were the secondary obligor of the underlying obligation owed to the applicant.

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(b) An applicant that reimburses an issuer is subrogated to the rights of the issuer against any beneficiary, presenter, or nominated person to the same extent as if the applicant were the secondary obligor of the obligations owed to the issuer and has the rights of subrogation of the issuer to the rights of the beneficiary stated in subsection (a).

(c) A nominated person who pays or gives value against a draft or demand presented under a letter of credit is subrogated to the rights of:

(1) the issuer against the applicant to the same extent as if the nominated person were a secondary obligor of the obligation owed to the issuer by the applicant;

(2) the beneficiary to the same extent as if the nominated person were a secondary obligor of the underlying obligation owed to the beneficiary; and

(3) the applicant to same extent as if the nominated person were a secondary obligor of the underlying obligation owed to the applicant.

(d) Notwithstanding any agreement or term to the contrary, the rights of subrogation stated in subsections (a) and (b) do not arise until the issuer honors the letter of credit or otherwise pays and the rights in subsection (c) do not arise until the nominated person pays or otherwise gives value. Until then, the issuer, nominated person, and the applicant do not derive under this section present or prospective rights forming the basis of a claim, defense, or excuse.

Appendix: D

Appendix D: Uniform Commercial Code Revised Article 5 (1995) Compared With the Original Version—Letters of Credit

Introduction

The original intention behind Article 5 was to provide a framework within which business practice could be allowed to evolve in a number of different directions. In doing this it defined the letter of credit and some other key terms, set rules for establishing a letter of credit, provided *some very basic rules* which prescribed the obligations of the parties to a letter of credit, described the obligations of confirmers and advisors, and established some basic remedies for breach of these obligations.¹

Under the (1995) revision the essential objectives and format of Article 5 remain the same, however, the revised Article leaves more room for the evolution of new business practices so allowing it to respond to modern commercial needs and technology.² It achieves this mainly by considerably simplifying the rules that apply to letters of credit. However, it has been argued that the reason why the revised UCC continues to provide non-comprehensive rules, is to enable the parties to a letter of credit to incorporate into the letter of credit other rules e.g. the UCP.³

¹ The original Article 5 (pre-1995) made clear that it dealt with “some but not all of the rules and concepts” of letter of credit law. See in this regard UCC – 5-102(3) (pre-1995), and UCC – 5-102,(pre-1995) cmt. See web site <http://www.nccusl.org/summary/ucc5.html>.

² UCC – 5-103(C)(1995). cmt, UCC – 5-103 (2). UCC – 5-10(3) (pre-1995 version). See generally, Barnes, J.G., and Byrne, J.E., ‘Revision of UCC Article 5’ 50 *The Business Lawyer* (August) (1995) 1449 at 1451.

³ UCC – 5-116(c). See UCC – 5-101, cmt. Article 5 does not exclusively govern all aspects of letters of credit and other laws do apply to letters of credit in certain situations. For example, in addition to the UCP and the international convention, the following bodies of law also apply on some occasions to letters of credit:

- (1) the federal bankruptcy law which applies to letters of credit with respect to applicants and beneficiaries that are in bankruptcy;
- (2) regulations of the Federal Reserve Board and the Comptroller of the Currency lay out requirements for banks that issue letters of credit. They also describe how letters of credit are to be treated for calculating asset risk and for the purpose of loan limitations;
- (3) an array of anti-boycott and other similar laws that may affect the issuance and performance of letters of credit.

Therefore, although the commentators on Section 5-101 state that all of these laws are beyond the scope of Article 5, in certain circumstances they will override Article 5. In addition, other Articles of the

They may do this by expressly making the letter of credit subject to those rules. However, it should be noted that at the same time as simplifying the law, the new revision has introduced some new concepts and modifications. The following are the most apparent modifications and new concepts which have been introduced into the revised UCC Article 5, in relation to the sections that this research has consulted:

1. Formal Requirements

Under the revised Article 5 of the UCC, it is no longer a requirement that a letter of credit has to be expressly labeled as such.⁴ This contrasts significantly with its predecessor which described in detail the form of document which had to be stated as a letter of credit⁵. As a sign of flexibility, a letter of credit may now be issued in any form that is a “record” provided that the record is authenticated⁶. Authentication could be achieved either through a signature⁷, via any other method of authentication which the parties agree to, or through any form which is permitted according to the “standard practice”.⁸

In simple terms, the way to interpret this language is to say that a written document is no longer absolutely necessary to establish the existence of a valid letter of credit or of any other associated obligation. Under the new legal regime, all that is required is an authenticated “record”, in fact a properly preserved computer record will suffice.⁹ This new definition of a letter of credit means that

UCC may apply to letters of credit. For instance, if the transaction involves the use of an instrument, such as a draft, that is a negotiable instrument under Article 3 and is collected and presented for payment through the banking system where the rules of Article 4 apply. Article 4 can also apply to the collection of documentary drafts [UCC – 4-501 to 4-504]. The terms of the letter of credit may require presentation of a document of title, such as a bill of lading, or a warehouse receipt to which Article 7 applies and one or more parties may have a security interest in property involved in the transaction, which is governed by Article 9. Finally, the issuer may pay the beneficiary using a cheque that is a negotiable instrument under Article 3 or a funds transfer. This would be subject to Article 4A. However, it should be mentioned here that if there is a tension (conflict) between Article 5 and Article 3, 4, 4A, or 9, Article 5 has overriding authority.[UCC –5-116(d). Pre-revision Article 5 was silent on the relationship it had to those other articles. See UCC –5-102 (pre-1995 version).

⁴ UCC – 5-102(a) (10) & cmt. 6. (1995).

⁵ UCC – 5-102(1) (c). (Pre-1995 version).

⁶ UCC – 5-104.

⁷ UCC – 5-102(c) and S 1-201(39).

⁸ UCC – 5-104.

⁹ See web site <http://www.nccusl.org/summary/ucc5.html>.

the electronic transmission methods can now be utilised to issue a credit or present documents for honour.¹⁰ Under the original Article 5, a “document” that was called for in a “documentary draft” or a “documentary demand for payment” had to be a “paper”.¹¹ This modification makes Article 5 fit for the age of electronic communications.

2. Revocable and Irrevocable Credits

With regard to the irrevocability of a credit, the revised Article 5 takes the same line as the UCP¹². Thus the UCP and the UCC provide that a letter of credit is deemed irrevocable in the absence of any indication in the credit as to whether it is revocable or irrevocable¹³. By comparison, under the original Section although it was recognised that a letter of credit could be either revocable or irrevocable, it was not specified how to treat a letter of credit that failed to describe its status. Consequently, it deliberately left the question for courts to resolve.

3. Time of Enforceability

According to the revised Article 5-106(a), a letter of credit becomes enforceable from the time it is “issued”. In turn, the time of issuance is defined as the moment when the issuer “sends” the letter of credit or “otherwise transmits it”, to the person who is the beneficiary or the person requested to advise the letter of credit¹⁴. This differs from the original UCC in that previously the right of the beneficiary did not become established until either the beneficiary received the letter of credit, or was in possession of an authorised piece of written advice that the letter of credit had been issued.¹⁵

4. Strict Compliance

With regard to the issuing bank’s obligations, the revised Article 5 has introduced the standard of strict compliance. This standard means that it is the duty of the

¹⁰ Schroeder, M R., “The 1995 Revisions to UCC Article 5, Letters of Credit”, 29, No 4, Spring (1997), *Uniform Commercial Code Law Journal* 331 at 333.

¹¹ UCC – 5-103(b) (pre-1995 version).

¹² Article 6(c) of the UCP.

¹³ UCC – 5-106(a) (1995).

¹⁴ *Ibid.*

¹⁵ UCC – 5-106(1)(b) (pre-1995 version).

issuer to determine whether a presentation “appears on its face strictly to comply” with the terms of the letter of credit¹⁶. Thus in contrast to its predecessor, the revised version clearly adopts the “strict compliance” standard over the so-called “substantial compliance standard”¹⁷ which was examined in Chapter Five. However, the phrase “strictly to comply” used in this section, is to be construed in line with the “standard practice of financial institutions that regularly issue letters of credit”.¹⁸ Accordingly, commentators on this Article have suggested that “strict compliance” does not mean “slavish conformity to the terms of the credit”.¹⁹ It is also worth noting that under the revised UCC, the doctrine of strict compliance is softened by the requirement on the issuer to give timely notice to the presenter of “discrepancies in the presentation”.²⁰ With the exception of cases of fraud or forgery, failure to do so will result in the issuer being precluded from using such discrepancies as a basis for rejection.²¹

5. Warranties

Under a letter of credit the presenter owes the issuer and the applicant a warranty duty of fraud and forgery. According to the revised Article, this cannot be effective until the issuer honours the presentation. This new approach makes it impossible for the issuer to justify a failure to honour a presentation just because there is a breach of this warranty. Moreover, the warranty to the applicant now extends to cover the underlying contract as well. “It is a warranty that the beneficiary has performed all the acts expressly and implicitly necessary under the underlying agreement to entitle the beneficiary to honour”.²² That is to say, this warranty gives the applicant rights against the beneficiary where he fails to meet those terms

¹⁶ UCC – 5-108(a). See generally, Barnes, J.G., and Byrne, J.E, *supra* note 2 at 1453-5.

¹⁷ Schroeder maintains that the revisers point to *Banco Espanol de Creditor v. State Street Bank & Trust Co.*, 385 F2d 230 (1 st Cir. 1967), and *Flagship Cruises Ltd. v. New England Merchants Nat'l Bank*, 569 F2d 699 (1 st Cir. 1978), as cases that “arguably” applied a substantial compliance standard. UCC – 5-108, cmt.1. See the same author, *supra* note 10, fn 136 p. 356.

¹⁸ UCC – 5-108(a), – UCC – 5-108(e). For more on UCC – 5-108(e), see Byrne, J.E., ‘Revised UCC Section 5-108(e): A Constitutional Nudge to Courts’ 29 *Uniform Commercial Code Law Journal* (1997) 419, 419-427.

¹⁹ UCC – 5-108, cmt. 1.

²⁰ UCC – 5-108(b)(3).

²¹ UCC – 5-108, cmt. 3. Similarly, see Articles 14(d) and 14(e) of the UCP.

²² UCC – 5-110, cmt.2.

in the underlying contract that specify the conditions under which the beneficiary can draw on the letter of credit.²³ Warranties also may arise as the result of the application of Articles 3, 4, 7, and 8 to the transaction. However, the new Article 5 limits the warranties arising under those other articles to ones which relate to “the presentation or transfer of documents covered by any of those articles”.²⁴

6. Reasonable Time for Examination

The revised UCC has introduced a section that deals with the time within which the issuing bank is to either honour or dishonour the credit. This should occur in “a reasonable time after presentation, but not beyond the end of the seventh business day” after receipt of documents.²⁵ Again this section has been drafted in line with the UCP, Article (13)(b) under which a period of seven-days is required for the issuer to act.

7. Expiry Date

The revised UCC has introduced a new approach regarding expiration of the credit. As a result, if the credit does not state its expiration date, it is considered to expire one year after the date of issue stated in the letter²⁶. Moreover, if the letter of credit fails to state the date when it was issued, it expires one year after the date on which it was issued in practice. If a letter of credit states that it is perpetual, it will expire five years after the date states as its date of issue. The original UCC was silent on those issues.²⁷

8. Bifurcated Standard

The revised UCC does not adopt the so-called “bifurcated standard” which was discussed in Chapter Six. However, the issuer and the applicant may create such a relationship by agreement.²⁸

²³ Ibid. See for more on the point, Schroeder, *supra* note 10. at 369.

²⁴ UCC – 5-110(b). UCC – 5-111 (pre-1995 version).

²⁵ UCC – 5-108(b) & cmt.2.

²⁶ UCC – 5-106 (c).

²⁷ UCC – 5-106 (d).

²⁸ UCC – 1-08, cmt.1.

9. The Standard of Practice Provision

The standard of practice provision in the new Article is undoubtedly the most significant part of these revisions. In the revised version there is an explicit recognition of standards of practice.²⁹ This entails that standards such as the Uniform Customs and Practices for Documentary Credits can govern many of the particulars of letters of credit. The primary reason for such simplifications is the specific inclusion of standards of practice in the revised Article 5. It provides that “An issuer shall observe standard practice of financial institutions that regularly issue letters of credit. Determination of the issuer’s observance of that standard practice is a matter of interpretation for the court”.³⁰ This means that the standards will apply unless the contract states otherwise. This differs from the original Article which only assumed that standards of practice would be adopted as a matter of contract between the parties to a letter of credit. Hence the standards were ineffective where the contract was silent.

Standards of practice for letters of credit are very well documented. First and foremost are the Uniform Customs and Practices for Documentary Credits (UCP), I.C.C. Publication No. 500, which have been set out by the International Chamber of Commerce. The UCP is updated on a decadal basis, and is much relied upon in international trade as a common language of letter of credit transactions. Thus the adoption of common standards of practice can be said once again to suggest a clear recognition by the drafters of the UCC, of the UCP as the source for many of the formal requirements and details of letters of credit. This permits business practices to govern the evolution of letters of credit within the aforementioned basic framework that Article 5 intends to provide.³¹

This new stance also removes an issuer’s obligations to its customer including “observance of any general banking usage”,³² and consequently relieves an issuer

²⁹ See web site <http://www.nccusl.org/summary/ucc5.html>.

³⁰ UCC – 5-108(e).

³¹ Schroeder, *supra* note 10 at 346.

³² UCC – 5-108(e). UCC – 5-109(1) (pre-1995 version).

of responsibility for “observance or knowledge of the usage of a particular trade other than the standard practice referred to in [revised Article 5].”³³

10. Fraud and Forgery

Another improvement is that with the revised version, the opportunity has been taken to clarify certain ambiguities surrounding the concept of fraud. One of these changes concerns fraud and forgery in presentation for payment. Basically, a letter of credit requires the presentation of a document, commonly a draft, for payment. According to the original Article, if the draft was fraudulent in some aspect or forged, the issuer’s reaction varied according to the circumstances. Nor was the issuer required to police the process by which payment was obtained³⁴. However, in those situations in which the issuer had the discretion to honour the draft, the customer could petition the appropriate court to enjoin honouring the draft.

The original Article 5 adopted the terminology of fraud in the transaction, and provided no guidelines with respect to which a court could determine the level of fraud that triggered the issuance of an injunction. This is why in the Revised Article the terminology of fraud in the transaction has been eliminated.³⁵ A fraud that justifies an injunction must be a “material” fraud.³⁶ Further, standards have now been established that the court must apply in determining whether to enjoin the issuer from honouring the draft. Included in these are factors of prohibition of injunction by other law, adverse effect upon the beneficiary, and availability of a remedy for fraud or forgery against the responsible individual or institution.³⁷

11. Remedies

Damages for a dishonoured or repudiated letter of credit are limited to the amount of the document plus incidental damages.³⁸ Consequential damages are not

³³ UCC – 5-108(f)(3). See generally on the standard practice, Moses, M.L., ‘The Uniform Commercial Code Meets the Seventh Amendment: The Demise of Jury Trials Under Article 5’ *72 Indiana Law Review* (1997) 681 at 690-709.

³⁴ Schroeder, *supra* note 10 at 370; see web site <http://www.nccusl.org/summary/ucc5.html>.

³⁵ See generally on fraud, Greenleaf, C.J., ‘The Holder-In-Due-Course Exception to the Fraud Exception to Compelled Honour Under Revised Article 5’ *Banking Law Journal* (1998) January 29-36.

³⁶ UCC – 5-109(a).

³⁷ UCC – 5-109, cmt. 1. See web site <http://www.nccusl.org/summary/ucc5.html>.

³⁸ UCC – 5-111(a). generally, Barnes, J.G., and Byrne, J.E., *supra* note 2 at 1459.

permitted for two reasons. First, it is believed that the beneficiary and the applicant are in the best position to avoid such damages; second, it is feared that the imposition of consequential damages would raise the cost of letters of credit to the extent that they would be viewed as uneconomical. Thus “[h]aving excluded consequential damages, punitive damages ‘a fortiori’ are excluded”³⁹ and overall the remedies against an issuer for wrongful repudiation or dishonour of a letter of credit will become more consistent for letter of credit transactions.

In short, the current situation is that an issuer is bound to honour a proper documentary presentation. Accordingly, repudiation occurs when the issuer communicates that a presentation will not be honoured and a dishonour occurs when the issuer does not pay when the appropriate document is presented. Finally, like any other legal obligation, the issuer is liable for all wrongful repudiation or dishonour.

In the original Article 5, the injured party could obtain the amount of the dishonoured document plus incidental damages less the amount realized on the underlying transaction.⁴⁰ This meant that if goods or documents of value produced as a result of the transaction were not sold to cover the losses, the issuer was entitled to them upon payment of judgment.

The position now is that the beneficiary or appropriate nominee is entitled to “the amount that is the subject of the dishonor or repudiation”.⁴¹ If the obligation is not for payment of money, the injured party may have specific performance in lieu of damages, at the option of the injured person. Significantly, incidental damages are allowed but not consequential damages nor is there an obligation to cover losses. If there is cover, the savings must be deducted from the recovered damages.

³⁹ Schroeder, *supra* note 10 at 389. See also UCC S 5-111, cmt.4. The official comment on this Section, however, states that Article 5 “does not bar recovery or consequential or even punitive damages for breach of statutory or common law duties arising outside of [Article 5].”

⁴⁰ UCC – 5-115 (1) (pre-1995 version).

⁴¹ UCC – 5-111(a).

As for the applicant, he has a remedy for damages “resulting from breach”, again including incidental but not consequential damages. A breach by a confirmer or advisor gives rise to actual damages plus incidentals.⁴²

Interest is due for any damages from the date of breach or dishonour and the prevailing party has a right to attorney's fees.⁴³ There is also a specific authority for prior agreement to liquidate damages. It can be concluded that these provisions vastly improve and clarify the remedies available under Article 5.

12. Subrogation

One area which was not specifically addressed in the original version was the possibility of the subrogation of one party to another party to a letter of credit, upon payment of the other party's obligations. Subrogation rights are available by contract under the original Article.⁴⁴ However, in the absence of provision within the contract, the courts have not agreed upon their availability. This has given rise to some confusion in the law.

The new rules provide specific rules to cover such eventualities. For example, if the issuer pays the beneficiary, the issuer is subrogated to the rights of the beneficiary and the applicant to the same extent as if the issuer were a secondary obligor of the underlying obligation.⁴⁵ However, subrogation rights do not arise until there has been an actual payment to the party whose rights are subrogated.⁴⁶ Subrogation puts the person with the subrogation right in the shoes of the person who benefited from the payment that triggered the subrogation right. Subrogation rights balance equities between parties in complex transactions like letters of credit. As a result, the revised Article 5 has cleared up the judicial doubt as to whether automatic rights of subrogation exist.⁴⁷

⁴² UCC – 5-111(b).

⁴³ UCC – 5-111(e).

⁴⁴ See web site <http://www.nccusl.org/summary/ucc5.html>. Pre-revision Article 5 did not address the subrogation rights of parties to letters of credit. See Schroeder, *supra* note 10, fn 185 at p. 365.

⁴⁵ UCC – 5-117(a).

⁴⁶ See Schroeder, *supra* note 10 pp. 365-68.

⁴⁷ See web site <http://www.nccusl.org/summary/ucc5.html>.

13. Variation of Article 5 Rules by Agreement of the Parties

Article 5 continues to provide rules that can be waived or modified by agreement between the parties. Since almost the entirety of Article 5 in its revised or original form is variable by agreement, the specific provisions of the UCP may also become part of the agreement between the parties, or its provisions may be waived by agreement. Thus in between the expanded reliance upon existing standards of business practice as a default rule and the ordinary ability of the parties to vary the default rules, the revised Article 5 grants commercial people the maximum flexibility to tailor their relationships under letters of credit. As a result, there is considerable freedom to vary by agreement the framework of rights and duties established in Article 5. In addition the courts are encouraged to be sensitive to the commercial expectations created by custom and usage that “are not inconsistent with the essential definitions and substantive mandates of the statute”.⁴⁸

13.1. Limitations to Variation of Article 5 Rules by Agreement of the Parties

Although under the revised Article 5, the parties to a letter of credit may, by agreement, vary most of the terms in the agreement and thereby alter the obligations that would otherwise be imposed by Article 5⁴⁹, there are seven exceptions to this rule. These exceptions serve to foster certainty.

1. An overriding clause which attempts to disclaim liability or limit remedies, is not effective. Thus issuers cannot limit their liability to only those circumstances where there has been an act of bad faith or gross negligence.
2. It is not possible to disclaim liability for breach of “the obligations of good faith, diligence, reasonableness and care”.
3. The legal scope of Article 5 cannot be altered, nor can a definition of letters of credit be given to a contract which is outside Article 5.

⁴⁸ UCC – 5-101, cmt. See generally, Stern, S., ‘Varying Article 5 of the UCC by Agreement’ 114 *Banking Law Journal* (1997) 516.

⁴⁹ This may be done either “by agreement” or by a provision stated or incorporated by reference in an undertaking” (UCC – 5-108).

4. The independence principle may not be varied. This means that any concurrent rights and obligations under any underlying contract cannot undermine the rights and obligations of the issuer under a letter of credit.
5. The restrictions imposed by Article 5 on who can be an issuer of a letter of credit, cannot be altered. Thus ordinary consumers cannot issue letters of credit.
6. Letter of credit cannot be made in perpetuity and any attempt to do so will be null and void.
7. Subrogation rights can be claimed by an issuer, applicant or a nominated person, however, those rights cannot be used to avoid honouring, reimbursing or paying an essential term of the letter of credit.⁵⁰

14. Enjoining an Issuer from Honouring a Presentation Under a Letter of Credit

Under the former Article 5, there was much debate as to whether the court could be justified in enjoining an issuer from honouring a letter of credit because of fraud.⁵¹ These rules have been modified by the revised version in two major respects.

14.1. The Issuer's Ability to Dishonour for Fraud

According to the new Article, three specifically defined conditions must be met before the issuer can dishonour a contract where, on the face of it, presentation appears to meet the terms and the conditions of the letter of credit.

- (i) The required document must be forged, or presentation involves material fraud.⁵² In addition the material fraud, even if it involves a breach of the underlying contract, must do so in a way that means the beneficiary is acting fraudulently against the issuer or applicant.⁵³

⁵⁰ Schroeder, *supra* note 10 at pp. 344-5.

⁵¹ UCC 5-114 (pre – 1995 version).

⁵² UCC 5-109(a).

⁵³ UCC 5-109, cmt. 1.

- (ii) Where a person has given value in good faith because of the letter of credit, then a contract cannot be dishonoured against him because of fraud. The Article lists the type of parties that it is referring to here.⁵⁴
- (iii) Provided the other two exceptions are met, then provided he acts in good faith, the issuer has the discretion to dishonour or honour the presentation, regardless of the viewpoint of the applicant.⁵⁵ It is worth noting though that the applicant will only have an action against the issuer if he can prove bad faith.⁵⁶ Therefore, where the issue is in doubt, it is safer for the issuer to accept presentation than it is to dishonour the contract. This is because the issuer will be liable if he cannot prove conditions (i) and (ii). Consequently, in practice it is likely that it will be for the applicant to obtain an injunction to force the issuer to dishonour the contract.⁵⁷

14.2. The Applicant's Rights to an Injunction Against Honour

For such an application, a special set of conditions must be satisfied, and these conditions apply to temporary restraining orders, preliminary injunctions and permanent injunctions. The conditions will also apply if the applicant attempts to use alternative legal means to arrive at the same conclusion because the "[e]xpanded use of any of these devices could threaten the independence principle just as much as an injunction against honor".⁵⁸

For the conditions to be met, there must be a claim by an *applicant* of forgery or material fraud⁵⁹ and in doing this condition (i) of the preceding section must be met. Thereafter, provided that the court is a competent one, four further conditions must be met⁶⁰

⁵⁴ UCC 5-109(a)(1).

⁵⁵ UCC 5-109(a)(2).

⁵⁶ UCC 5-102(a)(7).

⁵⁷ Schroeder, *supra* note 10 at p. 370.

⁵⁸ UCC 5-109, cmt.5.

⁵⁹ UCC 5-109(b).

⁶⁰ Summarised by Schroeder, *supra* note 10 at 374.

First, “the relief is not prohibited under the law applicable to an accepted draft or deferred obligation incurred by the issuer;”⁶¹
 second, “a beneficiary, issuer, or nominated person who may be adversely affected is adequately protected against loss that it may suffer because the relief is granted;”⁶²
 third, “all of the conditions to entitle a person to the relief under the law of this State have been met; and”⁶³
 fourth, “on the basis of the information submitted to the court, the applicant is more likely than not to succeed under its claim of forgery or material fraud and the person demanding honour does not qualify for protection under subsection (a)(1).”⁶⁴

With letters of credit the term honour means “performance of the issuer’s undertaking in the letter of credit to pay or deliver an item of value.”⁶⁵ Thus “[u]nless the letter of credit otherwise provides”, there is honour: “upon payment ...; if the letter of credit provides for acceptance, upon acceptance of a draft and, at maturity, its payment; or if the letter of credit provides for incurring a deferred obligation, upon incurring the obligation and, at maturity, its performance.”⁶⁶ Obviously, this definition has implications for proceedings for an injunction by the applicant against the issuer. A particular example is where a letter of credit is honoured by a time draft. The question here is whether an injunction can be made out preventing the issuer from paying the draft when it matures, even when the issuer has already accepted the draft. It would appear that here the present case law applies⁶⁷, but also that the revised Article 5 outlines two ways in which such an injunction can be prevented. Thus either the letter of credit should specify that honour occurs when the draft is accepted, or declare that injunctions cannot be brought post acceptance.⁶⁸ It should also be noted, that the section that provides for the applicant’s right to enjoin the issuer from honouring a letter of credit can be varied.⁶⁹

⁶¹ UCC 5-109(b)(1).

⁶² UCC 5-109(b)(2).

⁶³ UCC 5-109(b)(3).

⁶⁴ UCC 5-109(b)(4).

⁶⁵ UCC 5-102(a)(8).

⁶⁶ *Ibid.* There are many similarities in approach to the former version of Article 5.

⁶⁷ UCC 4-303(1).

⁶⁸ UCC 5-109, cmt.4.

⁶⁹ UCC 5-103(c).

15. Insolvency of Bank Holding Funds for Documentary Credit

It is to be noted here that section 5-117 (dealing with "Insolvency of Bank Holding Funds for Documentary Credit") was omitted in the Revised Article 5 of 1995. The author has consulted the American Law Institute (ALI) about the reason why the insolvency section has disappeared in the revised Article. The answer was that "The April 6, 1995, Proposed Final Draft, however, has a "Table of Disposition of Sections in Former Article 5." The table indicates that old section 5-117 was omitted in Revised Article 5 because it was "covered by other law." The table does not offer any other information. It is likely that in the 40 years since old section 5-117 was drafted, some federal banking or bankruptcy laws were issued covering the topic". Similarly, Dolan states that the (1995) version "has no analogue to Section 5-117, leaving to other law, including, one would assume, the common law, the questions that Section 5-117 addresses".⁷⁰

Summary

In many respects Article 5 is now much clearer, simpler and less detailed because of the explicit reliance it places upon standards of practice. It is not possible to list entirely in a short summary all of the problems under the original Article 5 that are solved in the revised version. As a result, we can now be confident that letters of credit are not only an important part of the credit granting and payment system, but they will remain at the forefront of commercial law well into the 21st Century. Thus because these changes give letters of credit the clarity and flexibility necessary for their successful operation, there is a case for saying that all states should act to adopt these important revisions as soon as possible.⁷¹

⁷⁰ Dolan, J., *The Law of Letters of Credit. Commercial and Standby Credits*. Revised edition. (Warren, Gorham and Lamont, 1996) p. (12-12).

⁷¹ See comment on why states should adopt revised UCC Article 5, Letters of Credit (1995) at web site: <http://www.nccusl.org/whystate/ucc5why.html>.

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