

terms and conditions of the Guarantee, the Guarantor shall so inform the party which gave that Guarantor its instructions in relation to the Guarantee and shall suspend payment of the claim for such time as the Guarantor shall consider reasonable to permit the Principal and the Beneficiary to reach agreement on the granting of such extension and for the Principal to arrange for such an extension to be issued. The Guarantor shall incur no liability (for interest or otherwise) should any payment to the Beneficiary be delayed as a result of the above-mentioned procedure.

Even if the Principal were to agree to or request such an extension, it shall not be granted unless the Guarantor also consents thereto.

I. APPLICABLE LAW AND JURISDICTION

Article 27

Unless otherwise provided in the Guarantee, the applicable law shall be that of the Guarantor's place of business. If the Guarantor has more than one place of business, the applicable law shall be that applying to the branch which issued the Guarantee.

Article 28

Unless otherwise provided in the Guarantee, any dispute between the Parties relating to the Guarantee shall be settled exclusively by the competent court of the country of the Guarantor's place of business or, if the Guarantor has more than one place of business, by the competent court of the country of the branch which issued the Guarantee.

2. Stand-by letters of credit and guarantees: tentative considerations on the preparation of a uniform law: note by the Secretariat (A/CN.9/WG.III/WP.63) [Original: English]

I. GENERAL CONSIDERATIONS ON PREPARATION OF UNIFORM LAW

1. The Commission, at its twenty-first session, entrusted the Working Group on International Contract Practices not only with the review of the ICC draft Uniform Rules on Guarantees but also with the examination of the desirability and feasibility of any future work towards a uniform law.¹ The present note is designed to assist the Working Group in that examination.

2. At the outset, the Secretariat wishes to emphasize that the considerations and suggestions set forth in this note are of a very tentative nature, due to the early stage of the deliberations and in line with the purpose of the Working Group's examination. The results of that examination would assist the Secretariat in preparing the study, requested by the Commission for its twenty-second session, on possible features and issues that might be covered in a uniform law.² Above all, they would help the Commission at that session to decide whether a uniform law should be

prepared and, if so, what its scope and contents should be, including the question of whether, in addition to guarantees and stand-by letters of credit, traditional documentary letters of credit should also be covered.³

3. In view of this latter question of the possible scope of any uniform law, this note, while focussing on guarantees and stand-by letters of credit, takes into account some special issues of commercial letters of credit (e.g. relationship between issuing and confirming bank, deferred payment credit). The considerations on most of the more general issues (e.g. principle of independence, strict construction and compliance, fraud exception, applicable law) would apply to guarantees and stand-by letters of credit as well as commercial letters of credit, although solutions might differ in detail.

4. This fact may be regarded as an important reason for including commercial letters of credit in any future uniform law. Another reason could be that it would allow the establishment of a clear classification of independent guarantees, stand-by letters of credit and commercial letters of credit, in particular, by separating stand-by letters of credit from commercial letters of credit and recognizing their functional equivalence with independent guarantees.⁴

5. A possible objection to such inclusion could be based on the existence and worldwide acceptance of the Uniform Customs and Practice for Documentary Credits (UCP) and, more generally, on the volatile and ever-developing nature of letter of credit law and practice. It is submitted that any such concern would be valid also in respect of the "emerging law"⁵ of stand-by letters of credit and guarantees, although the extent will depend on the success of the future ICC Uniform Rules on Guarantees. Here and there the response would be the same and constitute a guiding principle in shaping the contents of any future uniform law: The uniform law would concentrate on those matters that cannot effectively be regulated by agreement of the parties, including any uniform rules, and its treatment of issues should be sufficiently general or abstract so as to allow and foster future development of rules and practice.

6. The latter consideration would be particularly relevant to the inclusion of any definitions, rules of interpretation or other issues hitherto not satisfactorily regulated by uniform rules. Some examples are mentioned in this note and may assist the Working Group in identifying further appropriate issues during its deliberations on the ICC draft Uniform Rules on Guarantees.

7. It is hoped that the following points and suggestions are of some use in the Working Group's examination of the desirability and feasibility of preparing a uniform law. If at this early stage a tentative conclusion may be ventured, it would be that an informed and final decision on the general question of feasibility seems to require extensive deliberations of the various issues by the Commission

¹Report of the United Nations Commission on International Trade Law on the work of its twenty-first session, *Official Records of the General Assembly, Supplement No. 17 (A/43/17)*, para. 22.

²*Ibid.*, para. 25.

³*Ibid.*, para. 26.

⁴See conclusions in A/CN.9/301, paras. 91-93.

⁵Thus Kozolchik, *The Emerging Law of Standby Letters of Credit and Bank Guarantees*, 24 *Ariz. L.R.* (1982) 319.

or the Working Group; even if it is decided that preparation of a uniform law is not feasible, the very deliberations would be of value in clarifying matters.

II. SOME ISSUES POSSIBLY TO BE DEALT WITH IN A UNIFORM LAW

8. As outlined in the conclusions of the report of the Secretary-General (A/CN.9/301, paras. 97-99), greater uniformity at the statutory level seems desirable in various respects. One of the general topics suggested as being appropriate for a uniform law, convention or model law, is to recognize party autonomy and the independent nature of the promise to pay.

A. Recognition of party autonomy for independent undertaking

9. A uniform law could and should expressly recognize the parties' freedom and give full effect to their agreement, including a reference to any uniform rules on guarantees or to UCP. The need for such recognition seems greater in respect of guarantees than letters of credit, at least the traditional documentary type where care should be taken in drafting any rule of recognition so as not to preempt any current or future application of UCP as trade usage or customary law.

10. The main purpose of such recognition would be to establish firmly the independent nature of the guarantee as a product of agreed commercial practice, on an equal footing with the letter of credit. Recognition of the agreement in a special uniform law would mean, for example, doing away with current provisions of law that do not give full effect to party autonomy. A prime example would be the recognition of an agreed expiry date as prevailing over any provision of law which, as found in some States, denies the expiry effect as long as the beneficiary retains the guarantee document or as long as a statutory limitation period runs. The uniform law could further help in this matter by imposing an enforceable obligation to return or release the guarantee document.

11. A uniform law may usefully establish the characteristic requirements of independent undertakings and address the question of binding language that constitutes a commitment to honour demands for payment upon compliance with the conditions specified in the guarantee or the credit. It could, for example, specify the formal requirements and the decisive point of time of the establishment of a credit or a guarantee. In this context, consideration might be given to addressing questions of wider application such as the meaning of "signature" or "authentication".

12. It would appear advantageous to go beyond a general provision of the independent promise to pay and to distinguish between various promisors and types of credit or guarantees. This would help, for example, to clarify the differences in terms of rights and obligations between, on the one side, an issuing and a confirming bank and, on the

other side, a guaranteeing and a counter-guaranteeing bank. To mention an example concerning types of credit, one could envisage a definition of the modern "deferred payment credit" and possibly address controversial questions such as whether a bank is entitled to pay before the deferred payment date and, more generally, what precisely is the legal effect of a payment under reserve.

13. Another matter that might appropriately be covered is the designation or determination of the beneficiary as the person entitled to payment. Here it would be necessary to distinguish clearly between commercial letters of credit and guarantees, including stand-by letters of credit, in view of the considerable differences concerning the possibility and purpose of transferring the entitlement to payment. In this context, a further contribution could be made towards clarity of sometimes confused concepts, namely transfer of the credit or the guarantee itself, negotiation of any draft or commercial paper under a credit or guarantee and, possibly, assignment of proceeds.

B. Strict construction and compliance

14. Closely related to the principle of independence of the undertaking are two principles characterized by strictness or rigidity. The first one calls for strict construction of the terms and conditions of the guarantee or the credit. If the principle were to be embodied in a uniform law, consideration may be given to adding some rules of interpretation for language used by the parties (e.g. distinguishing between printed and superimposed terms; construing ambiguous clauses against the drafting party) and, possibly, for uniform rules (e.g. regard to international character and need for uniform application).

15. The second principle is that of strict compliance, in particular, of documents with the requirements set forth in the credit. A clear description of the principle, for example, elaborating the professional diligence of a reasonable banker and his ability to distinguish between essential and non-essential defects, might be useful. It could help to reduce two risks that threaten to endanger the viability of credits and guarantees, namely abusive insistence on an overly strict standard by an unwilling debtor or account party and injection of undue leniency by equitable considerations often relating to the underlying transaction. An ancillary question could be whether a dual standard would be appropriate, one for the bank's decision to pay or to refuse payment and the other for its right to reimbursement. Yet other issues would be the appropriateness of contacts (consultations or notice) with the account party, the precise scope and effect of any rule of preclusion such as the one in article 16(e) UCP and, possibly, the allocation of the risk of any loss of documents.

C. Fraud and other objections to payment

16. The most important effect of the independent nature of a guarantee or a letter of credit is that it limits the availability of objections or defenses against payment to those specified in the guarantee or credit, thus cutting off

any other objections relating, in particular, to an underlying transaction. However, at least one exception to this rule of exclusion has been widely recognized as such, namely the fraud exception.

17. As suggested in the report of the Secretary-General (A/CN.9/301, para. 98), the vexing problem of fraudulent or abusive calls and of appropriate court measures would probably be the most important topic for a uniform law. Since the problem has been discussed in that report in some detail,⁶ it may suffice here to present a kind of tentative check-list of pertinent questions:

- What constitutes fraud, and should other abuses be included
- Fraud “unravels all” or are there limits (as regards certain parties or relationships)
- Requirements of knowledge by payor, or payee, and decisive point of time (e.g. presentation of documents or payment date)
- Measure of damages for wrongful honour (to be covered, if at all, only if also generally for wrongful dishonour)
- Available procedures or court measures and their requirements (e.g. interpleader with payment into court, temporary restraining order and injunction enjoining call or payment; probably not to be covered: arrest, seizure, garnishment or freeze of funds).

18. The need for certainty about the admissible objections to payment suggests considering whether the payor may refuse to pay, or be enjoined from paying, for reasons other than those covered by the fraud exception. Such reasons might relate to illegality or violation of public policy affecting the establishment of the guarantee or credit or, more remotely, the underlying transaction. For example, the guarantee might constitute an outlawed penalty or the credit or guarantee might conflict with a wagering law, an export restriction or foreign exchange

control regulation. If any such ground for objection would be recognized in the uniform law, ancillary issues concerning the precise effects might be included (e.g. whether a payment obligation, based on a price doubled for purposes of avoiding foreign exchange control, would be unenforceable as regards the full sum or only half the amount). Finally, consideration may be given to the admissibility of a set-off and, if so, in what relationships.

D. Applicable law and related issues

19. International guarantee or credit transactions involve parties from two or more States. Thus questions arise as to the applicable law, to be answered separately for each particular relationship. As regards the possible inclusion of answers in a uniform law, the need therefor is probably greater in respect of guarantee or credit undertakings than in respect of underlying transactions or customer-bank relationships.

20. If rules for guarantee or credit undertakings were being considered, one could envisage giving effect to the parties' choice and, failing their agreement, to use as the connecting factor, for example, the promisor's place of business. Thus, to mention only one of many detailed issues, the law applicable to the guarantee obligations of an issuing bank may differ from that applicable to the rights of that bank towards a counter-guaranteeing bank; here, as in the comparable documentary credit situation of confirming and issuing bank, one may consider such disparity as undesirable and might try to overcome it (e.g. by implying a corresponding choice of law clause).

21. It may be noted in conclusion that any answers of the above kind need not necessarily be incorporated into complete conflicts of law rules. Some of them may be appropriately given in determining the territorial scope of application of any future uniform law. Similar considerations would apply to the inclusion of any rules on the jurisdiction of courts (or arbitral tribunals), at least in respect of rights, obligations and procedural measures covered by the uniform law.

⁶A/CN.9/301, paras. 60, 84-90.