

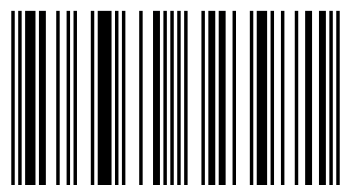
The focus of this book is upon the UCP, which consists of a set of principles that standardise banking procedures for payments by way of documentary credits (DC). These principles do not apply automatically, but are in play once traders choose to pay by letter of credit and to incorporate the UCP as part of their contract terms. The Uniform Customs and Practice for Documentary Credits (UCP) is a set of rules governing credits drafted by the International Chamber of Commerce (ICC). The objective of UCP is to create a set rule that would establish uniformity in practice and to facilitate the flow of international trade and alleviate problems encountered when individual countries try and promote their own national rules on letter of credit practice. Although there have been dramatic changes in the operations of international trade since UCP was first adopted, it continues to be used by banks around the world because it has moved with and reflects those changes. The amendments made to UCP in its various revisions have addressed problems arising from the existing version of UCP and the interests and developments, which are seen as being relevant in the future.



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Ucp 600 : An Improvement on Ucp 500?

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Chapter One

Introduction

The UCP: Background to Reform

The Uniform Customs and Practice for Documentary Credits (UCP) is a set of rules governing credits drafted by the International Chamber of Commerce (ICC). While the “UCP” have no legislative force, they are in effect the world standard for the almost universal operation of letters of credit. Indeed, so pervasive is their incorporation into letters of credit that the ICC, whose Banking Commission generates the UCP, has, in the latest version of the instrument, called the UCP a set of “rules”. The objective of UCP is to create a set rule that would establish uniformity in practice followed by parties in handling letter of credit. The UCP represents the work of a private international organization, ICC, which insists on self regulations and remains the most successful set of private rules for international trade ever developed.

The focus of this article is upon the UCP, which consists of a set of principles that standardise banking procedures for payments by way of documentary credits (DC). These principles do not apply automatically, but are in play once traders choose to pay by letter of credit and to incorporate the UCP as part of their contract terms. The UCP was first issued by the ICC in 1933. It has been regularly revised since then in order to ensure that it reflects current banking and trade practice. The objective of the ICC in creating uniform rules for documentary credits

was to facilitate the flow of international trade and alleviate problems encountered when individual countries try and promote their own national rules on letter of credit practice.¹

This first version of the UCP was promulgated by the 7th Congress of the ICC, convened in Vienna.² It viewed documentary credit transactions as involving the two commercial parties - the buyer (applicant) and the seller (beneficiary) and two banks, the issuing bank and the correspondent bank, and it recognised the distinction between revocable and irrevocable credits as well as the confirmation of a letter of credit. However, there was no attempt to classify letters of credit according to the method of payment and no provision dealing with negotiation. At the same time, the 1933 version affirmed the autonomy of the credit and recognised that, in letter of credit transactions, parties deal with documents and not in goods. The Code underwent a thorough revision in 1951 and its second version,³ endorsed by ICC, was adopted by the banks of many countries in Asia and Europe and by the banks of the US. The banks of the UK and of the Commonwealth of Nations, however, resolve to adhere to their own practice.

A fresh revision of the Code took place in 1962.⁴ The result was a unification and harmonisation of the practice of letters of credit all over the world. In terms of basic structure, though, the 1962 revision did not depart to a substantial extent from the earlier versions. There was still no clear clarification of letters of credit according to the method of payment. However, the basic rules governing documentary credits were elevated into general principles, grouped together in the first part of the Code. Included in it were two provisions respecting the autonomy of credit. The

¹ Paul Downes, "UCP 600: not so strict compliance" (2007) 4 JIBFL 196; <http://www.simsl.com/UCP6000807.html>

² Published as ICC Brochure No 82.

³ Brochure No. 151 prior to it, the 1929 Congress of the ICC, held in Amsterdam, recommended a set of regulations, which, however, were adopted only in Belgium and France.

⁴ ICC Brochure No. 222.

1962 revision further defined the meaning of a “clean” transport document and, generally, improved the draftsmanship of individual Articles of the Code.

The next revision took place in 1974.⁵ It introduced four improvements. First, it replaced most of the “option” which stated that banks may act in a certain matter with imperative provisions requiring banks to do, or refrain from doing, certain acts. Secondly, many of the provisions were redrafted with the object of attaining clarity.⁶ Thirdly, combined transport documents were dealt with in Art 23 and, finally, Art 47 provided that an assignment of the proceeds of the credits was to be governed by the applicable local law.

The UCP were next revised in 1983.⁷ Five innovations were effected. First, the principle under which the parties to documentary transactions deal in documents and not in goods was removed from the provisions dealing with the examination of the documents⁸ and constituted a separate Article numbered as Art 4. By placing this provision in the first part of the UCP 400, the draftsmen reinforced the autonomy principle, spelt out in Art 3.⁹ Secondly, the 1983 revision made provision for “deferred payment credits”¹⁰ and “standby credits,”¹¹ the two types of letter of credits which had not been expressly brought within the ambit of the code till then.

⁵ Published as ICC Brochure 290. The Banking Commission was, on this occasion, assisted by the United Nations Commission on International Trade Law (UNCITRAL) and by the ad hoc Committee comprising members of some of the East European and other socialist bloc countries not represented on the ICC.

⁶ For instance, Art 3 (a) processor of UCP 500, Art 9) clarified that, where the credit was available by negotiation, the issuer's undertaking was “without recourse.”

⁷ ICC Brochure No. 400.

⁸ Art 8 (a) in the 1974 Revision

⁹ Structurally, the “General Provisions” of the previous versions were constituted Part I of UCP 400 and renumbered accordingly.

¹⁰ The credit does not call for drawing of the bills of exchange. Any doubt about their being within the ambit of the Code was removed by UCP 400, Art 10.

¹¹ By Art 2, recasting the definition of letters of credit. The position was unclear before then, although the Code used to be incorporated in letters of credit issued by American bank.

The third innovation of the UCP 400 resulted from the developments in communications. Instead of “telegrams” and “telexes”, the new revision referred to “teletransmissions”, which encompasses SWIFT messages. Fourthly, the new revision classified documentary credits according to the nature of the issuing bank’s payment undertaking which could assume one of the four following forms:¹² (i) payment of cash against the tender of documents (ii) deferred payment, (iii) an undertaking to accept a draft (a bill of exchange) for the amount of the credit and (iv) negotiation of bills drawn on a third party, which was deemed to be without recourse.

Finally, UCP 400 came up with yet a further revision of the provision respecting documents of transport. Omitting an express reference to combined transport documents, it divided transport documents into marine bill of lading (Art 26), postal receipts (Art 30) and “other transport documents” (encompassing combined transport documents). The 1983 revision was more precise than the earlier versions. Furthermore, the opinions of the ICC Banking Commission during 1984-1986 were more numerous than those delivered in the earlier years.¹³

Another version had been the UCP500, promulgated by the ICC in 1993 and effective from January 1, 1994.¹⁴ The 1993 revision UCP 500 was principally an update of UCP 400.¹⁵ There have of course, been a number of innovations and clarifications. Thus, Art 2 defines a “bank”; Art 9 (replacing UCP 400, Art 10) discourages the use of letter of credit available by negotiation;¹⁶ and Art 10 defines “negotiation”¹⁷ and introduces the concept of “nomination

¹² UCP 400, Art 10.

¹³ ICC Brochure 434.

¹⁴ P. Ellinger, “The UCP-500: Considering a New Revision” (2004) L.M.C.L.Q. 30 at pp.31-32.

¹⁵ P. Ellinger, “The uniform Customs and Practice for Documentary Credit- the 1993 Revision” (1994) LMCLQ 377.

¹⁶ But it does not proscribe their use.

bank”.¹⁸ In addition, the provisions respecting documents tendered under letters of credit have been thoroughly revised in Arts 23–29. This constitutes an improvement and update version of the 1983 revision.

The latest (and sixth) version of the UCP - the UCP600¹⁹ was formally adopted by the Banking Commission of the ICC on October 25, 2006²⁰. As of 1 July 2007, however, the new revision came into force.²¹²² The revision was brought about following criticism of the now old UCP 500, which was perceived as outdated, over-complicated and open to ambiguity and error. The old rules were widely criticised by the shipping industry, in particular, Article 23 which set out the requirements for bills of lading.

Although there have been dramatic changes in the operations of international trade since UCP was first adopted, it continues to be used by banks around the world because it has moved with and reflects those changes. The amendments made to UCP in its various revisions have addressed problems arising from the existing version of UCP and the interests and developments, which are seen as being relevant in the future. While the latest revision is no exception to this general statement, it should be appreciated, however, that its drafters have had to confront fewer pioneering issues than did the drafters of its predecessor. Indeed, it is fair to say that the latest revision, while incorporating significant redrafting, achieves an overhaul of UCP 500 without changing its provisions substantively and should therefore be seen as the latest step in the

¹⁷ UCP 500, Art 10 (b) (ii).

¹⁸ UCP 500, Art 10 (b) (i).

¹⁹ ICC Uniform Customs and Practice for Documentary Practice, 2007 Revision, ICC Publication No.600, ISBN 92-842-1257-X, www.iccbooks.com, henceforth “UCP600”.

²⁰ The first version of the UCP was adopted by the ICC in 1933.

²¹ UCP 600, Art.1.

²² ICC Publication No.600

evolution of UCP rather than a document which makes revolutionary changes to UCP. Despite this popularity, UCP600 is neither a perfect nor an up to date Code.

Why a Revision?

UCP 500 offered many improvements but still fell short of the expected reduction in disputes arising from inconsistent interpretation and application particularly of certain terms like 'negotiation' and 'reasonable time'. When the revision project was first announced by the ICC, the relevant working committees made it clear that the revision was to achieve three objectives. Therefore, the introduction to the UCP 600 identifies three main reasons for the revision²³:

- I. To address development in the banking, transport and insurances industries.²⁴
- II. Need to look at the language and style used in the UCP, to remove wording that could lead to inconsistent application and interpretation.²⁵
- III. The third objective was to attempt to stem a rate of rejection which was regarded as being too high.²⁶ There was concern over the prevalence of rejection of the documents presented in order to claim under a credit. When the revision began, global surveys showed that approximately 70% of documents presented were being rejected on first

²³ UCP 600, p.11.

²⁴ Ibid at p.11

²⁵ Such as the 'original document' requirement that created conflicting judicial interpretation under the UCP 500. See *Glencore International AG v Bank of China* [1996] 1 Lloyd's Rep 135 and *Kredietbank Antwerp v Midland Bank Plc.* Times, 31 October 1997 (QBD). "Unilateral and incorrect interpretations" of certain Articles of the UCP500 (the immediate successor to the UCP600) had been the cause of four Position Papers, published by the ICC on September 1, 2004, to emphasise the need to correctly interpret and apply a number of Articles in the UCP 500. See Gutteridge & Megrah, *Law of Bankers' Commercial Credits* (8th edn, 2001) and, for the full text of the Position Papers, see Jack, Malek and Quest, *Documentary Credits* (3rd edn, 2001)11. These Position Papers will not be applicable in the context of the UCP600. It remains to be seen, of course, whether the UCP600 will stand the test of time without generating their own set of Position Papers.

²⁶ The ICC Uniform Customs and Practice for Documentary Credits UCP 600, Introduction, 11.

presentation because of discrepancies. This was considered by the Commission to constitute a serious threat to maintaining and increasing the use of documentary credits as means of payment in international trade.

The underlying problem appeared to be that the UCP 500 procedure was too open to differentiating interpretations and errors. The ICC's Banking Commission's intention was, therefore, to bring the UCP procedure up-to-date and to improve the consistency of its application and interpretation by means of adding clarity to the UCP rules so, hopefully, reducing the frequency of banks' documentary rejections. When comparing the new rules with their predecessor (UCP 500), a large number of drafting changes are obvious, including a restructuring of the presentation of the sections, but on closer examination it becomes clear that many of these revisions have been made to provide clarification of an existing rule rather than to introduce a radical change.

Chapter Two

The New UCP 600: Changes from UCP 500

Doctrine of Strict Compliance

a. Standards for the Examination of Documents

In arranging for the carriage of goods overseas, sellers need the reassurance that the standards applied by banks in scrutinising documents will not vary from country to country. A measure of predictability is needed because, if the documents are rejected, this is likely to cause delay and expense in selling the goods elsewhere. Yet the traditional rule in English law and elsewhere is harsh: there must be strict compliance between the documents tendered by the beneficiary and the stipulations in the letter of credit.²⁷ This rule was not spelt out in the UCP, although Art.13 (a) of the UCP500 offered some guidance in relation to the banks' scrutiny of documents. It provided that banks must examine all documents stipulated in the credit with "reasonable care" and also stated that compliance with the terms of the credit must be determined in accordance with "international standard banking practice (ISBP) as reflected in these Articles". The concluding words "as reflected in these Articles" were not thought to confine banks solely to the standards embedded within the UCP itself; reference to the UCP could be supplemented by considering the standard practice rules established by financial institutions in particular regions.²⁸ Article 14(d) of the new UCP600 appears to confirm this view by making reference to "international standard banking practice", but omitting the final words.

²⁷ *Equitable Trust Co of New York v. Dawson Partners Ltd* (1927) 26 Ll. L. Rep. 49, HL.

²⁸ J. F. Dolan, "Letters of Credit: A Comparison of UCP 500 and the New U.S. Article 5" [1999] J.B.L. 521 at pp.523-525; C. del Busto, *Documentary Credits, UCP500 & 400 Compared* (ICC Publishing, 1993), pp.39-40.

Substantial changes to the standard for examination of documents, the refusal of discrepant documents and the form of refusal and waiver have also been made (Articles 14 and 16). This should bring much greater certainty and precision to the document checking procedure. The concepts of “reasonable time” and “without delay” often proved to be highly subjective. These have been removed completely and replaced by a time period of five banking days, following the day of presentation, for a bank to deal with the document-handling process. Article 16 now includes the option for the Issuing Bank to advise the presenter, when refusing documents. For example, UCP 500 only gave the examining bank the option of *holding them at the disposal of the presenter or returning them*. However, in practice many banks seek a waiver of discrepancies from the applicant and if they obtain one, the bank may want to release the documents without consulting the beneficiary. New Art.16 “*Discrepant Documents, Waiver and Notice*” (previously Art.14) now provides these four options for a bank:

- i. hold the documents pending further instructions from the presenter
- ii. hold the documents until the bank receives a waiver and agrees to accept it or receives further instructions from the presenter prior to agreeing to accept a waiver
- iii. return the documents
- iv. act in accordance with instructions previously given by the presenter.

This reflects a sensible commercial compromise, which should lead to a much more streamlined and less complex document-handling procedure for both beneficiaries and banks alike. The changes to Articles 14 and 16 should, therefore, provide for a significant improvement in one of the key areas of conflict and delay in the documentary credit process.²⁹

²⁹ John Turnbull, “UCP 600- A new era for documentary credits” (2007), 1(4) Bankers’ Law at p30.

b. Reasonable Care

The sparseness of the UCP600 is also evidenced by the removal of vague phrases. For example, banks are no longer required to inspect documents with “reasonable care”³⁰ in determining whether they comply with the letter of credit.³¹ Although some ICC members advocated that banks should not be required to inspect documents at all, this met with resistance and the result is that the UCP600 still requires them to do so. As an examination is necessary, it can be argued that, implicitly, it must not be negligent. Consequently, this revision cannot be presented as a significant one and it is unlikely by itself to affect the percentage of documents which are rejected. In tune with the doctrine of the autonomy of the credit, Art.14 (a) of the UCP600 provides that banks (nominated banks, confirming banks and issuing banks) must make their checks on the basis of the documents alone.³² Article 13(a) of the UCP500 had required banks to examine documents to ascertain whether “on their face” they appeared to comply with the terms and conditions of the credit. Obviously, documents must be regular and of the type current in the trade in question.³³ However, the precise meaning of the phrase “on their face” was controversial. It appeared in a number of different Articles in the UCP500 and its meaning varied according to the context in which it was found. In relation to examination of documents, it should refer to the fact that the banks' examination is confined to the documents alone.³⁴

³⁰ Require by UCP500, Art.13 (a).

³¹ Banks have never been expected to act as detectives: the onus has always been upon the customer to show lack of reasonable care in failing, for example, to detect a forgery: *Gian Singh & Co Ltd v Banque de l' Indochine* [1974] 1 W.L.R. 1234 at 1239 *per* Lord Diplock.

³² As mentioned previously, both “presentation” and “complying presentation” are defined in Art 2.

³³ A. G. Guest, *Benjamin's Sale of Goods* (Sweet and Maxwell, 2006), para.23-206.

³⁴ C. del Busto(n 28)p.39.

Nevertheless, in the past some banks have assumed that they must simply pay regard to the front page of the document.³⁵

The general thrust of the revision was to reduce uncertainty by removing vague or ambiguous phrases. It had been suggested that the phrase was redundant and should be removed entirely from the new draft. However, the eventual consensus was that it should be retained in relation to examination of documents in Art.14, but that it should be removed from all other provisions in the UCP600. Its retention is a reminder that the banks' scrutiny of documents may be superficial; banks are not expected to know the customs of a particular trade and nor are they obliged to verify any of the information contained in the documents supplied.³⁶ In practice, banks may well be more proactive³⁷; however, the UCP does not impose such an obligation upon them. It is not anticipated, however, that this omission will lead to any substantive difference in the way this duty will be construed by the banks in the exercise of their duty to examine the documents. Given that the duty always was and remains to ascertain whether the documents appear to conform, it must follow that the banks are under a duty to exercise reasonable care rather than any stricter duty of examination.

³⁵ C. Debattista, "Legislative Techniques in International Trade: Madness or Method" [2002] J.B.L. 626, pp.634-635.

³⁶ But it has been argued that this is an undesirable consequence because the scrutiny of documents by the banks can act as a significant check on fraud: P. Holst, "A Shipping Association's View" (2006) 12(4) *DC Insight* 9. Nevertheless, Art.34 of the UCP 600, like its predecessor, protects banks by providing a general disclaimer of responsibility for fraud or inaccuracy in any document.

³⁷ Banks may well attempt to verify information or to encourage an applicant to waive a breach if it is of no real significance: R. Sappideen, "International Commercial Letters of Credit: Balancing the Rights of Buyers and Sellers in Insolvency" [2006] J.B.L. 133 at pp.141-142; R. J. Mann, "The role of letters of credit in payment transactions" (1999-2000) 98 *Michigan Law Review* 2494.

c. The Preclusion Rules

The rule of absolute documentary conformity can lead to harsh results. It is almost impossible to achieve complete standardisation in an area where each letter of credit will normally be adjusted to reflect the parties' concerns and the trade in question. However, the potential for unfair treatment of beneficiaries is reduced considerably by preclusion rules, which require the issuing bank to act speedily in giving notice of documentary defects. Article 14(e) of the old UCP500 spelt out that a bank's failure to do so would mean that it was precluded from claiming that the documents were non-conforming. As a consequence, time limits for scrutinising documents are immensely significant. Drafters of the UCP600 struggled to find a simple rule governing time limits which would cover all possibilities. At one extreme, a letter of credit might call for hundreds of pages of documentation, some of which might require translation; but, at other times the documentation required might be minimal. Article 14(d) of the UCP500 had provided that each bank involved (the nominated bank, confirming bank and issuing bank) had a "reasonable time" within which to inspect, not exceeding seven banking days. The thrust of the new revision was to eradicate vague phrases such as "reasonable". Yet there was a fear that, if "reasonable time" was replaced by a set period of days, banks would assume that every time a beneficiary of a credit presented documents, they were entitled to take those set period of days to process them, thereby causing unnecessary delays in making payments to beneficiaries.

Another danger was that the buyer would expect the bank to take this period of time before his or her account was debited to reflect the payment made. It was therefore suggested that banks should be protected by providing a "safe harbour" period, which would consist of a minimum set

period of days, which would always be seen as a reasonable time for inspection of documents, together with a maximum period of time which would be available depending on the circumstances of the individual case. In the end, however, it was decided that, in the interests of certainty, there should be one set period and the new Art.14 (b) of the UCP600 therefore provides that each bank has five banking days as a maximum period,³⁸ after the day of presentation, within which to consider the documents. The five-day period represents a compromise: some traders argued that the period of examination should be even shorter (such as three days) because of the costs which can accrue during this period of time, such as storage charges.³⁹ However, there are bankers who say that the word “maximum” suggests that an expeditious approach (or at least the absence of wilful delay) is still required. It is also worth noting that the timescale is from presentation to completion of examination, not to date of *payment*. Therefore, prudent sellers will still specify any payment timescales within the contract of sale.⁴⁰

Like the UCP500, the drafters have separated the duty to examine documents from the duty to give notice. The duty to examine is contained within Art.14, but the duty to give notice is to be found (along with the preclusion rules) in Art.16. A subtle link between these two Articles is to be found in Art.16 (b) which provides that, if a bank contacts the applicant to explore whether he or she is prepared to waive the discrepancy, this does not have the effect of extending the five-

³⁸ Steven Jeffery, “The New UCP 600” (2007) Vol. 23, Iss. 1, Banking & Finance Law Review p. 189-210.

³⁹ P. Holst, (n 36).

⁴⁰ Robert Parson, “UCP 600 A New Lease of Life for Documentary Credits? Part 1” (2007) 9-1 Finance and Credit Law 1, 3

day time period specified in Art.14 (b).⁴¹ The slightly tortuous position is that, if a bank fails to comply with the maximum time period for examination of documents, it will not have served a proper notice which satisfies Art.16.⁴² This brings Art.16 (f) into play, which provides that it is precluded from claiming that the documents do not comply with the letter of credit. This is also true where, for example, a bank failed to properly notify the beneficiary of the defects. Nevertheless, by forcing banks to act speedily and to serve one single notice specifying each and every discrepancy (together with a statement indicating whether it is returning the documents or seeking further instructions), the combined effect of Arts 14(b) and 16 may reduce the number of documents rejected on first presentation. It should also mean that, if a beneficiary presents his or her documents well before the credit's expiry, he or she will have more time to rectify a discrepancy and to present conforming documents.

However, while omission of the phrase “reasonable time” may have resolved some differences of interpretation, the new so-called “safe haven” of “a maximum of five banking days” may give rise to a new set of problems. Thus, for example, what if a bank decides on the second day that the documents are compliant? Can the seller insist on payment on that second day or must he wait until the fifth day for payment? Article 14(b) gives each bank five banking days to decide whether to pay, Article 15 says that it must pay (“honour”) or give notice of refusal immediately it comes to that decision.⁴³ Moreover, Article 16(d) states that the notice of its refusal to pay

⁴¹ R. Bergami, ‘UCP 600 rules - changing letter of credit business for international traders?’ (2009) Vol.1, No.2, Int. J. Economic and Business Research, pp191- 203.

⁴² Art.16 (d) of the UCP600 provides that the notice must be served within five days of presentation of documents. For a critique of this split in duties, see Dolan, above fn.17, pp.530-531.

⁴³ Commodities Finance Impact of UCP 600- A guide to the new rules.

must be given “by telecommunication or, if that is not possible, by other expeditious means no later than (emphasis added) the close of the fifth banking day following the day of presentation.”

The consequence would be that a bank proven by the beneficiary to have waited for the fifth day would be in breach of its duty to pay the beneficiary and would be liable towards the beneficiary, for example, for interest on the sum due.

The same issue may cause problems for the buyer. If the bank were to pay on the second day, and if the goods are lost or damaged on the fourth day in a sale contract concluded on a “delivered” basis, is it open to the buyer to complain that the bank had paid the sum under the credit before it was obliged to and that the bank should indemnify the buyer for the costs of recovering the price from the seller in a foreign jurisdiction? Alternatively, the bank giving notice of refusal on the second day may thereby give an opportunity for the seller to re-present documents before the expiry of the credit, whereas had the bank waited the full five days, the credit would have expired. Think the buyer cannot complain: it is probable that Article 14(b) does not require the bank to wait five days: it simply gives it five days to examine the documents if it needs five days. The consequence would be that a bank is entitled, as far as the buyer is concerned, to pay on the second day if it rightly decides then that the documents comply or to reject on the second day.⁴⁴

d. Description: The Commercial Invoice and Other Documents

The key document is the commercial invoice. According to the old Art.37(c) of the UCP500, the description of the goods in the invoice must correspond with the credit, whereas the goods might

⁴⁴ Commodities Finance Impact of UCP 600- A guide to the new rules.

be described in more general terms in all other documents provided the description did not conflict with the credit. In the UCP600, Art.18 sets out the essential ingredients of the commercial invoice; Art.18(c) specifies that not only the description but also services and performance must comply with the credit. In relation to other documents, one must refer to Art.14, which sets the standard expectation of banks in their examination of documents. Article 14(e) in the UCP600 provides that the description of the goods, services or performance, if stated, can be described in general terms provided that they do not conflict with the terms of the credit. Although there is no major change in approach, the new provisions are wider in scope in covering descriptions of services and performance in addition to the goods themselves. Furthermore, the decision to separate the treatment of the commercial invoice from other less important documents is yet another example of the drafters' desire for a clear and simple structure.

e. Identification and Linkage

Certain data must be included in each individual document tendered to link it to the cargo in question.⁴⁵ This requirement can easily be defended because a document is of little value if the goods to which it refers cannot be readily identified and it would create a fertile ground for fraud. The UCP 500 had been somewhat light of touch on linkage, dealing with inconsistency regarding the description of the goods in Article 37(c) and with inconsistency in general in Article 13(a). More controversially, in relation to documents other than transport documents, insurance documents and the commercial invoice, there was a further requirement in Art.21 of the UCP500

⁴⁵ *Banque de L' Indochine et De Suez SA v J.H. Rayner (Mincing Lane) Ltd* [1983] Q.B. 711.

that the data contained in them must not be inconsistent with any other document stipulated by the credit.⁴⁶ This is an area which demanded a fresh reappraisal because a large percentage of the cases where documents have been rejected on the grounds of discrepancy are the result of inconsistent data between documents. Much of this data may not have been specified in the letter of credit itself or required by the UCP. The Drafting Group of the UCP 600 considered including a rule which stated that the data contained in each particular document should only be considered in the light of the stipulations in the credit and the UCP; this would put the burden upon the applicant to state precisely what information was required in any given document. The advantage of this proposal was that, provided the goods were sufficiently identified in the credit, there would be no danger of uncertainty. Unfortunately, this proposal was rejected by the national committees.⁴⁷ Instead, under the UCP 600, the new Art.14 (d) provides that:

“Data in a document, when read in context with the credit, the document itself and international standard banking practice, need not be identical to, but must not conflict with, data in that document, and any other stipulated document or the credit.”

There was discussion over whether the closing words (“any other stipulated document”) should be included; the effect of their presence is to require linkage between all documents which have been specified in the credit. Checking for conflicts between a numbers of documents is intensely time-consuming for banks and increases the risk that documents will be rejected as discrepant and there appears to be little to be gained from the exercise.⁴⁸ This result is seen in some quarters

⁴⁶ C. del Busto, (n 28) p.61. An ICC Opinion suggested that linkage between documents and the credit was essential: ICC Opinion R251, published in *ICC Banking Commission Collected Opinions 1995-2001* (ICC, 2002), p.57.

⁴⁷ G. Collyer, “A Look at the UCP Revision” (2006) 12(4) *DC Insight* 1.

⁴⁸ W. Cameron, “Balancing the Pluses and Minuses of the Revision” (2006) 12(4) *DC Insight* 10; J. Smith, “A Major Opportunity Missed” (2006)(4) 12 *DC Insight* 6 at p.7.

as a contentious one.⁴⁹

But was there something more that was driving the revision? There is a real fear that an overly technical approach to the test for compliance in the presentation of documents under a letter of credit will undermine the commercial efficacy of these instruments.⁵⁰ Of course, the converse proposition is also true and since Viscount Sumner's warning in the case of *Equitable Trust Co v Dawson*⁵¹ that: 'There is no room for documents which are almost the same, or which will do just as well. Business could not proceed securely on any other lines ...' practitioners have regarded a strict approach to discrepancy issues as underlying the integrity of the credit.⁵²

However, it must be said that there are two views about the new Article (Art.14 (d)). The first is that the new wording simply explains but does not extend the purpose and effect of the old Article 13, and may (because of the wording "not identical" and reference to international standard practice) lead to less rejections.⁵³ The second is that there must have been a purpose to such a detailed change in the wording and that the effect must be that the banks are now entitled and obliged to be far more rigorous in scrutinising the data in each document tendered.⁵⁴ When the Article says, for example, that the banks must compare data in each document with data "in the credit", does this mean that data in a document conflicting with a non-documentary requirement in the credit would make the document discrepant? Logically, yes. But this is wholly inconsistent with Article 14(h) requiring the banks to disregard non-documentary requirements.

⁴⁹ It gave rise to some debate at the ICC UK Annual Trade Finance Seminar, "Understanding the UCP600", held on December 6, 2007 in London.

⁵⁰ Paul Downes, (n 1).

⁵¹ (1926) 27 Lloyd's Rep 49 at p52

⁵² Steven Jeffery, (n 38) 189-210.

⁵³ Commodities Finance Impact of UCP 600- A guide to the new rules.

⁵⁴ *ibid*

Thus, for example, would a reference to the age of the vessel as 17 years used in one of the documents tendered render a presentation discrepant if the credit contained a non-documentary requirement that the vessel be under 15 years of age?

This is one of the least happy alterations to the old version of the Rules and it is hoped that the Commission and courts called upon to construe the new Article 14(d) will interpret it as an explanation rather than an extension of the old Article 13(a), in keeping with the aim stated in the introduction to the UCP 600 to reduce unnecessary rejections of documentary tenders.

f. “Original” Documents

There is now more clarity over “original” documents presented (Art.17). Under the UCP 500, there was controversy surrounding Article 20(b), which governed what could be accepted by banks as 'original' documents. That Article allowed banks to accept as original documents that had been produced by automated or computerised systems, provided they were marked as original and (if necessary) signed. This led to conflicting interpretation. The first case to deal with this Article was *Glencore International AG v Bank of China*.⁵⁵ In that case, it was held that in order to be considered original, a document produced by the means listed must be both marked as original and signed. Signature alone was not sufficient to establish the originality of a document.

The following year however, the case of *Kredietbank Antwerp v Midland Bank Plc*⁵⁶ arose. That case took a different interpretation of Article 20(b), which was that it was intended to add to the

⁵⁵ [1996] 1 Lloyd's Rep 135.

⁵⁶ Times, 31 Oct 1997 (QBD).

pool of documents that could be accepted as original. Therefore, the section was read as only applying to copies produced by the means listed and not to originals. It was held that documents that appeared on their face to be original, should still be accepted as original regardless of the means by which they were produced.⁵⁷

A third case *Crédit Industriel et Commercial v China Merchants*⁵⁸ attempted to reconcile these two judgments. It was held that documents which are not obviously original must be marked in accordance with Article 20(b) if they were, or appear to have been, produced by one of the methods listed in that Article. But documents which are obviously original, or which would have been accepted as original prior to the UCP must be accepted, even if they are produced by one of the Article 20(b) methods and not marked "original".⁵⁹ The UCP 600 has dealt with this conflict in Article 17. This Article sets out that "a bank shall treat as original any document bearing an apparently original signature, mark, stamp, or label of the issuer of the document, unless the document itself indicates that it is not original." The Article goes on to state that a bank will also accept as original a document that: "appears to be written, typed, perforated or stamped by the document issuer's hand; or appears to be on the document issuer's original stationery; or states that it is original, unless the statement appears does not apply to the document presented." By setting out exactly what can be accepted as original by a bank, the UCP creates greater certainty for both banks and users of credits. This will speed up the honouring process and ensure that credits are still regarded as an efficient means of financial settlement.

⁵⁷ John Turnbull, (n 29)30.

⁵⁸ [2002] EWHC 973

⁵⁹ Ganotaki "Documentary Credits: Another Original Story" (2003) *LMCLQ* 151, 155.

The UCP 600, is therefore, more satisfactory for users than the UCP500: it incorporates the Policy Statement and presents the principles within a more rational scheme. The parts of the old Art.20 of the UCP500 which related to “original” documents can be found in the new Art.17. This includes related matters, such as the position where the credit calls for documents “in duplicate”; here, it is ordinarily sufficient if at least one original is submitted. However, other issues, which are independent of the definition of an original document (such as the use of facsimile signatures and stamps), have been hived off. They are dealt with in the new Art.3, which is concerned with general matters of interpretation.

However, the object of the re-wording of the new provision was to settle the doubts respecting the meaning of “original”, produced by a number of cases decided under UCP 500. It is hoped that this object has been achieved. Two further clauses are added for the sake of clarity. Under Art 17 (d), if a credit requires presentation of copies of documents, presentation of either originals or copies is permitted. Under sub-cl 17(e), a requirement for the presentation of multiple documents is satisfied by the presentation of at least one original and the remaining number in copies.⁶⁰

g. Introduction of “Definitions” (Art.2) and Interpretation” (Art.3) Provisions

Articles 2 and 3 of UCP 600 create new definition and interpretation sections. These are designed to make the UCP 600 more accessible and easier to read. Instead of referring to specific definitions in the substantive provisions as was the case under the UCP 500, the new UCP provides in Articles 2 and 3 a list of definitions and interpretative aids. Some of the terms which

⁶⁰ UCP 500, Art 20 (d).

were formerly simply assumed to have an indisputable definition, are now given explicit definitions to remove all elements of doubt. For example Article 2 contains definitions of 'advising bank', 'applicant', 'banking day' etc. Setting out these definitions prevents repetition of the meaning of the terms used throughout the subsequent articles. This is a positive step towards making the UCP a more understandable and easier to read document. However, this has not gone all the way to answer all the problems related to the definition of terms used in UCP.

The goal of the UCP 600 was to reduce redundancy.⁶¹ It remains doubtful however, whether these summaries, in particular Article 3, are advantageous. Article 3 contains, without any numbering or division, in twelve paragraphs of completely differing content. Beginning with the concept of irrevocability of letters of credit, continuing to creation of originals, time related concepts like "on or about", "to", "until", "fill", "from" and "between", and "beginning", "middle" and "end" of a month.

h. Modifications of the Doctrine

Like Art.39 of the UCP500, Art.30 of the UCP600 modifies the doctrine of strict compliance. Subject to certain conditions, there is a tolerance of 5 per cent more or 5 per cent less if there is some discrepancy as to quantity. If the words "about" or "approximately" are used in relation to the amount of the credit or the quantity or the unit price stated in the credit, a tolerance not to exceed 10 per cent more or 10 per cent less is permitted. However, there is a new provision, contained in Art.14 (j), which will also affect the doctrine of strict compliance. In general, there is no need for the addresses of the beneficiary and applicant to correspond with either the credit

⁶¹ ICC-Publication No 600 ED, Introduction, p15.

or other documents, provided the addresses are within the same country as the addresses stated in the credit. Their contact details are irrelevant.⁶² In many respects, this is a welcome modification because addresses are invariably in local languages and it is therefore easy for foreign beneficiaries to make a minor mistake. On the other hand, it would be unfortunate if this new provision had the effect of encouraging banks to take a lax attitude towards the question of identification of the parties. This would make money laundering considerably easier and the banks would risk falling foul of money laundering legislation.⁶³

However, the changes made in the UCP 600 are relatively minor and the ISBP and old case law will still be relevant in applying the doctrine of strict compliance. It may well be that, despite the change relating to addresses and the preclusion rules relating to examination of documents, the adoption of the UCP600 will not lead to a dramatic reduction in the percentage of documents which are rejected as discrepant.⁶⁴

⁶² As an exception, where the address and contact details of the applicant appear in a transport subject to the UCP600, these details must be mentioned in the credit: UCP600, Art.14(j).

⁶³ Regulation 1781/2006 of November 15, 2006, which applies to trade finance and which requires banks to provide accurate and meaningful information concerning the payer which must accompany transfers of funds.

⁶⁴ For a contrary view, P. Taneja, "A Document Restoring the Credibility of Letter of Credits" (2006) 12(4) *DC Insight* 3.

Chapter Three

Possible Problems Arising From the Changes Made By UCP 600

While UCP 600 represents a major drafting overhaul of UCP 500, it is worth noting that certain contentious problem areas associated with UCP 500 still remain in the latest revision. Some of these problem areas as outlined below are, Banco Santander and the UCP 600, Typographical Errors, Non-Documentary conditions, Data Content Essential and Revocable Credits. Here we shall be looking at them one after the other to explain how each of these create problem.

A. Banco Santander and the UCP 600

i. Banco Santander

A deferred letter of credit is one which provides for maturity, i.e the due date for payment, to be at a stipulated date some time after the documents have been presented and the conditions of the letter of credit have been complied with rather than at the time of presentation of the documents.⁶⁵ A bank discounting a deferred payment credit takes the risk of fraud emerging between discount and maturity. This is because unless expressly stated in the credit, a nominated bank is not authorised to negotiate the credit and does so on its own account, as principle, at its own risk. There is little doubt that discounting of future payment obligation stands at the heart of the deferred payment credit, as it indeed does in credits available by the acceptance of drafts. It evolved as a creature of the mercantile and banking community to serve the interests of both the

⁶⁵ H.C. Gutteridge and M. Megrah, *The Law of Bankers' Commercial Credits*, (7th Ed, Europa Publications Ltd, London 1984) p 14 and Henry Harfield, *Bank Credits and Acceptances* (5th Ed John Wiley & Sons, Inc, New York 1974), p 48.

buyer and the seller. This much is, of course, undisputed. But there appeared to have been difficulties regarding the effect of a fraud by the beneficiary uncovered after the discounting of the amount of a deferred payment credit, but before the date on which payment was due.⁶⁶

However, prior to the introduction of Art.12 (b) by the UC P 600, the issuing bank could assert a fraud by the beneficiary as a defence to a claim for reimbursement by the nominated bank where the latter has discounted its obligation under a deferred payment undertaking without the knowledge of the fraud. This is because the nominated bank under a deferred payment credit, by definition, has the issuing bank's authority to incur a deferred payment undertaking and to pay at maturity but, without a further explicit authorisation as conferred under Art.12(b) of the UCP 600, it does not have a requisite mandate to pay before maturity.⁶⁷ The well-known decision of the English Court of Appeal in *Banco Santander SA v Bayfern Ltd*⁶⁸ confirmed this point and it is submitted that the decision accords with legal logic.⁶⁹ The soundness of its reasoning is attested by the fact that in other countries, too, judgments had been rendered on the same basis, such as the Singaporean decision of *Credit Agricole Indosuez v Banque Nationale de Paris*⁷⁰ and the South African decision of *Vereins-und Westbank AG v Veren Investments*.⁷¹

⁶⁶ One such question arose in *Czarnikow-Rionda Sugar Trading Inc v Standard Bank London Ltd* [1999] 2 Lloyd's Rep. 187. But the judge's "provisional view" was that the credits in question were negotiation credit and proceeded to conclude accordingly.

⁶⁷ Adodo Ebenezer Adodo, "the Legal Effect of Nomination under the New UCP 600" (2008) 23 (4) J.I.B.L.R. 231.

⁶⁸ *Banco Santander SA v Bayfern Ltd* [2000] 1 All E.R. (Comm) 776 CA.

⁶⁹ Commentaries making similarly positive appraisals include, e.g. Daniel Aharoni & Adam Johnson "Fraud and Discounted Deferred Payment Documentary Credits: The Banco Santander" (2000) 15 J.I.B.L.R. 22, 25; Eyal Berger, "Putting Florida Buyers on par with International Buyers: A Cost-Benefit Analysis of Revising Florida Statute" 675.109(1)(A)(4)" (2004) 16 Fla. J. Int'l L. 529.

⁷⁰ *Credit Agricole Indosuez v Banque Nationale de Paris* [2001] 2 S.L.R. 1.

⁷¹ *Vereins-und Westbank AG v Veren Investments* 2000 (4) S.A. 238; Eyal Berger, (n 69), A. Moher, "Discounting of Deferred Payment Credits—Comparative Aspects" (1983) 10 Banking & Fin. L. Rev. 379, 388.

In *Banco Santander SA v Bayfern Ltd* case,⁷³ Santander on receipt of complying documents, and at the beneficiary's request, discounted its deferred payment undertaking. Some days after discount, fraud was alleged and on the maturity date, Paribas refused to reimburse Santander. There were a number of issues considered, not least the fact that Santander had taken an "assignment of the proceeds" from the beneficiary, which rather weakened their position. The Court of Appeal found for the issuing bank, holding that, on the facts, Banco Santander was a mere assignee of the fraudulent seller's right to payment, and stood in no better position than that of the assignor.⁷⁴ Moreover, the issuing bank had not authorised the early, discounted payment by Banco Santander.⁷⁵ The decision caused much consternation among banks, which had developed a market in early discounting of payments under deferred credits.⁷⁶ Since the effect of *Banco Santander* was to place the risk of fraud on the discounting bank, the case "all but killed that business overnight".⁷⁷ As one commentator has noted⁷⁸ :

"The decision discouraged banks from discounting payments before the date of maturity.

This injured small operations exporting goods because, as beneficiaries under letters of credit, many relied upon receiving payment in advance (at a discount) in order to

⁷² As noted by Adodo Ebenezer Adodo, (n 67) ; *Czarnikow-Rionda Sugar Trading Inc v Standard Bank London Ltd* [1999] 1 All E.R. (Comm) 890, [1999] 2 Lloyd's Rep. 187; 360 days in *Vereins-und Westbank AG v Veren Investments* 2000 (4) S.A. 238; 180 days from the date of presentation of the specified documents in *Credit Agricole Indosuez v Banque Nationale de Paris* [2001] 2 S.L.R. 1; 180 days from the date of bills of lading in *Banco Santander SA v Bayfern Ltd* [2000] 1 All E.R. (Comm) 776 CA

⁷³ *Banco Santander SA v Bayfern Ltd* [2000] 1 All E.R. (Comm) 776, CA.

⁷⁴ *ibid* at 778.

⁷⁵ *ibid*.

⁷⁶ Robert Parson, (n 40)3 and P Taneja, "UCP 600: A Document Restoring the Credibility of Letters of Credit", available at <http://iccbooks.com/Home/CredibilityofLCs.aspx> [Accessed June 26, 2008].

⁷⁷ Parson, "(n 40)3.

⁷⁸ J. Ulph, "The UCP 600: Documentary Credits in the 21st Century" [2007] J.B.L. 355.

alleviate cash flow problems.”⁷⁹

However, in the Court's view, it was simply not possible to treat the assignee under a deferred payment letter of credit as though he were a holder in due course.⁸⁰ In one's view, that was the correct stance to take, since the two instruments are entirely distinct. It may be open to debate as to why one instrument, with only a slightly different structure from the other, should attract particular protections while the other does not. However, based on the decision in *Banco Santander*, the assignee would bear the risk of fraud.⁸¹

In order to appease the banking community, the drafters of the recently revised UCP (2007 revision, UCP 600) sought to reverse the effect produced by *Banco Santander*. In the new version of the UCP, Arts 7 and 12(b) have been designed to carry out that task. In Art.7, the “issuing bank's undertaking to reimburse a nominated bank”, include under a deferred credit, has been further entrenched. Pursuant to Art.12 (b), if an issuing bank authorises a nominated bank to incur a deferred payment undertaking, it also automatically authorises that bank to prepay. Therefore the new provisions appear to transfer the risk of fraud to the issuing bank, by ensuring that it pre-authorises the nominated bank to pay early.⁸²

However, we may well inquire whether the revised articles of the UCP will properly reverse the effect of *Banco Santander* in all future situations involving deferred payment credits. Those who consider that the revised articles do comprehensively deal with *Banco Santander* rely on the new Art.7, or the new Art.12 (b), or both, to support their position. Nonetheless, it may well be the

⁷⁹ *ibid* at 373.

⁸⁰ *Banco Santander* [2000] 1 All E.R. (Comm) 776 at 782-783 [emphasis added].

⁸¹ Deborah Horowitz, “*Banco Santander* and the UCP 600” [2008] *Journal of Business Law* 508

⁸² As discussed further below, parties to the credit should still be able to amend or reverse the effect of these articles by inserting appropriate contractual terms.

case that the new UCP provisions do not take into account the problem of assignment: if the seller assigns the right to payment to the confirming bank, that bank is still a mere assignee, taking “subject to equities”. Below, it will be argued that the drafters of the new UCP have appropriately reversed *Banco Santander* to some degree, but have not fixed the “assignment” problem.

Nonetheless, we must step back and assess the outcome produced by *Banco Santander*, and the extent to which the new UCP 600 provisions redress any concerns raised by that case. As stated earlier, the decision in *Banco Santander* is sound. Since the beneficiary assigned its right to payment to the confirming bank, it is correct that the assignee took “subject to equities” and the fraud defence barred payment. Moreover, the claim for payment was merely as an assignee, which is inconsistent with a discharge entitling reimbursement of the confirming bank's payment undertaking under the credit. The *Banco Santander* judgment focused on the assignment point, the remaining discussion on authorisation was of a secondary nature. However, the new UCP provisions only address the authorisation issue: they have not and arguably could not deal with the assignment point.

Turning to the assignment point in more detail, it is worth remembering that there were *two* separate issues in *Banco Santander*: one was the effect of the assignment of Bayfern's rights to Santander, and the other was whether Santander had been authorised to provide early, discounted payment under the credit. Article 12 only deals with authorisation. Evidently, it would be open to the confirming bank to argue that the combined effect of Arts 7 and 12 is that the issuing bank must reimburse a nominated bank, even if it pays early, and that by authorising prepayment, the

issuing bank accepts the risk of fraud.⁸³ The confirming bank would then contend that the issuing bank must also accept the risk in the case of assignment: Arts 7 and 12 provide “broad brush” cover for any prepayment or purchase situation. However, as explained by the Court of Appeal in *Banco Santander*, assignment and prepayment are mutually exclusive possibilities. A confirming bank can either take an assignment of the proceeds under Art.39 of the UCP, and present for payment as assignee; or it can discharge its undertaking to the beneficiary (at a discount or in full) and present for reimbursement in its own right. Articles 7 and 12 arguably only cover the latter situation. Indeed, Professor Goode has explained, in relation to Art.49 of the UCP 500 (now Art.39 of the UCP 600) that:

“A beneficiary who assigns the proceeds is merely transferring the right to ask for payment as and when earned by his own performance. Hence, to claim under the credit the assignee must present the beneficiary's documents *as agent of the beneficiary*, or get the beneficiary to present them. The assignee of the proceeds cannot tender documents in his own right.”⁸⁴

Therefore, in *Banco Santander*, where there was a clear assignment of Bayfern's right to proceeds to Santander, Santander could only have been presenting the documents to Paribas *as agent for Bayfern*, and not in its own right. On that note, Professor Goode specifically remarks that:

“Assignments of proceeds are typically in favour of the advising or confirming bank

⁸³ Deborah Horowitz, (n 81)

⁸⁴ Roy Goode, *Commercial Law*, (3rd edn London: Butterworths, 2004)p.1010.

itself where it has made an advance of funds payable under a deferred payment credit.”⁸⁵

Santander took “subject to equities”, and so too would any future assignee confirming bank, notwithstanding the provisions of the new UCP.⁸⁶ Again, by authorising the early payment under Art.12, the issuing bank might then be said also to take the risk even in cases of assignment. It could potentially be barred, also by virtue of the principles of equity, from setting up the defence against the assignee.⁸⁷ However, that is by no means clear from the UCP provisions, and one would have thought that if the drafters truly wanted to reverse all aspects of *Banco Santander*, they would have made provision for the assignment issue as well. Moreover, it is certainly not sufficient simply to assume, as some commentators have done already, that Arts 7 and 12 have also protected an assignee negotiating bank. Indeed, the very fact that the UCP 600 does not mention assignments, while at least one other key set of rules does so, may indicate that the omission of the assignment point was intentional. As is well known, para.5-109 of the US Uniform Commercial Code (UCC) deals with fraud and forgery in relation to letter of credit transactions. In that paragraph, there is express protection for assignees. Specifically, para.5-109(a)(1)(iv) provides that if fraud or forgery occurs, the issuer still must pay if honour is demanded by:

“... 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.”

⁸⁵ *ibid* at 1010.

⁸⁶ Deborah Horowitz, (n 81).

⁸⁷ *ibid*

Therefore, had the drafters wished to reverse *Banco Santander* in full, they could have inserted a provision into the UCP 600 along the above lines. More significantly, perhaps it is also inappropriate to refer to assignment in the UCP precisely because the negotiating bank should take the risk when it is an assignee. An assignee should not be elevated to the status of a holder in due course. Moreover, there are other reasons for not shifting the risk to the issuing bank, and these points have been raised more generally by critics, rather than being confined to the assignment issue.⁸⁸ For example, during the drafting process, commentators stated:

“Some Commission members do not want these provisions included in the UCP 600 because they feel this unfairly pushes a greater fraud risk on to the issuing bank, and therefore the applicant. Others feel they should be included because it should not be the confirming bank that bears this risk.”⁸⁹

In the nearly two decades following the recognition of the deferred payment credit in the UCP until 1999 when the *Banco Santander* case was decided, there was nothing in practice to suggest that this was not the common understanding of the international business world. The banking community was therefore unsurprisingly devastated by the denial of recovery to the nominated bank in the case. However, at any rate, the conclusion by the *Banco Santander* courts that the nominated bank did not have the authority of the issuing bank to entertain the beneficiary's request for a discounted payment of the credit was pure fiction. As earlier indicated and as was attested by the various expert witnesses, it was quite expedient for bankers to regard a

⁸⁸ *ibid.*

⁸⁹ G. Richardson, “UCP 600 Where It's Got To and What's Happening Next”, available at [http://dentonwildesapte.com/assets/1/18150-Bank notes.pdf](http://dentonwildesapte.com/assets/1/18150-Bank%20notes.pdf) [Accessed June 26, 2008].

nomination as entailing the so-called authority.⁹⁰

ii. The New UCP Provisions and Deferred Payments

As mentioned briefly above, the *Banco Santander* decision “sent shockwaves through the banking community”.⁹¹ One commentator notes:

“I know some bankers in the Middle East who resorted to increased issuance of deferred payment letter of credits, but when it came to adding confirmations insisted on acceptance credits, presumably believing, in the light of *Banco Santander*, that they were protected in cases of fraud.”⁹²

Turning first to Art.7, the key aspects are in para.(c), which sets out the issuing bank's reimbursement obligation. It begins by providing that an issuing bank “undertakes to reimburse a nominated bank that has honoured or negotiated a complying presentation and forwarded the documents to the issuing bank”. Evidently, there are some definitional issues that must first be addressed. First, the nominated bank must have made a “complying presentation”.⁹³ It is strongly arguable that if a beneficiary has produced documents that are forged, null or contain fraudulent misrepresentations, it cannot have provided a “complying presentation”.⁹⁴ On the same basis, any nominated bank that passes on those documents cannot have made a “complying presentation” to the issuing bank. Therefore, provided that the confirming bank had notice of the

⁹⁰ Adodo Ebenezer Adodo, (n 67). 231.

⁹¹ J. Ulph, (n 78) 373.

⁹² P.Taneja, “UCP 600”, p.2, available at <http://iccbooks.com/Home/CredibilityofLCs.aspx> [Accessed June 26, 2008].

⁹³ Deborah Horowitz, (n 81)

⁹⁴ P. Ellinger, “Documentary Credits and Finance by Mercantile Houses” in A.G. Guest *et al.*, *Benjamin's Sale of Goods*, (7th edn, Sweet & Maxwell, London 2006), p.1999; Roy Goode, (n 84), p.996; and Richard Hooley, “Fraud and Letters of Credit: Is there a Nullity Exception?” [2002] C.L.J. 279, 280.

fraud when presenting the documents (or, arguably, at any time up until reimbursement is due), this may constitute a ground for which the issuing bank could refuse payment. However, for the reasons set out below, such a right to refuse payment would probably be subject to Art.12(b). As has also been mentioned, “negotiation” would probably cover early payment under a deferred credit, because of the words:

“... By advancing or agreeing to advance funds to the beneficiary on or before the banking day on which reimbursement is due to the nominated bank.”⁹⁵

Nonetheless, some commentators have appropriately observed that the use of “prepay” in Art.12 (b) may cause confusion: “prepay” is not defined anywhere, and may be interpreted to mean something different from the “advancing or agreeing to advance funds” expression in Art.2.⁹⁶

However, we must turn to the remainder of Art.7(c). It goes on to provide that reimbursement:

“... under a credit available by acceptance or deferred payment is due at maturity, whether or not the nominated bank prepaid or purchased before maturity.”

Again, this would appear to protect the discounting bank, since the reimbursement obligation has been given explicit force. In the same vein, that provision could be seen to strengthen the abstraction of the credit, although it is true that, in this context, the situation is only as between the banks. The last sentence of Art.7(c) states: “an issuing bank's undertaking to reimburse a nominated bank is independent of the issuing bank's undertaking to the beneficiary.” Here, the

⁹⁵ UCP 600 Art.2.

⁹⁶ Kim Christensen, “Mixed Reactions to UCP 600 Draft” (2006) 49 L.C. Views 28, 32: “A sub-article has been included to solve the famous ‘Banco Santander’ case. It states that if a credit is available by deferred payment the nominated bank is authorized to ‘prepay or purchase’. Once again it is not for me to say whether this will work or not but it is risky to introduce new words like ‘prepay’: looking at the definition which says ‘advance funds’ one may ask what is the difference and perhaps a judge will evaluate that there is a difference because two different words have been used.” Also, James Byrne, “UCP 600 Final Text Released to ICC National Committees” (2006) 10(8) *Documentary Credit World* 18.

abstraction of the banks' independent, autonomous payment undertakings is reinforced. The aim of this provision may be to overcome the assignment issue: it suggests that, come what may, the issuing bank must reimburse the confirming bank, regardless of the issuing bank's obligations to the beneficiary. On that basis, even if the confirming bank were an assignee, it would still have a separate right to payment from the issuing bank. However, as discussed above, a confirming bank can only claim payment under one or the other: it either has a right to payment as assignee of the proceeds of the credit, or because it has discharged its own undertaking and seeks reimbursement.⁹⁷ Realistically speaking, the last sentence of Art.7(c) only properly addresses the reimbursement issue, but cannot cater for the assignment point. The recapitulated theme is that an assignee still takes “subject to equities”.

Article 12(b) better addresses the problem in *Banco Santander*. As the Court of Appeal stated, if the confirming bank wants reassurance of payment, it must obtain authorisation from the issuing bank to discount early. Now, that authorisation is automatic, and an issuing bank would expressly have to contract out of the effect of Art.12 (b) if it wished to avoid authorising early payment of a deferred payment undertaking. Article 12(b) states:

“By nominating a bank to accept a draft or incur a deferred payment undertaking, an issuing bank authorizes that nominated bank to prepay or purchase a draft accepted or a deferred payment undertaking incurred by that nominated bank.”

At first glance, that provision seems to tackle the *Banco Santander* problem with full force. Pursuant to the UCP 600, a confirming bank will always be authorised to pay early under a

⁹⁷ Deborah Horowitz, (n 83)

deferred payment letter of credit, and should be assured of reimbursement by the issuing bank. Again, it will be unsurprising if the “prepay or purchase” point is litigated. If a confirming bank prepays, it should be entitled to “reimbursement”. However, if it purchases the deferred payment undertaking, that involves purchasing the beneficiary's or its own right to payment. On the reasoning adopted by the Court of Appeal, if no “prepayment” is involved, then there is no entitlement to be “reimbursed”. More specifically, the purchase of a right to be paid begins to look rather like an assignment.⁹⁸

And it is the assignment point that has not been addressed by the new UCP provisions. Interestingly, if we survey reactions to the UCP 600, most writers appear to consider that the new UCP has dealt with all of the problems presented by *Banco Santander*. Generally, they do so either on the basis of Art.7 (undertaking to reimburse), or on the basis of Art.12 (express authorisation), and sometimes both. In the Art.7 group, Pradeep Taneja states:

“There has been an attempt to resolve the *Banco Santander* problem by establishing a definite undertaking of issuing and confirming banks to reimburse on maturity whether or not the nominated bank prepaid or purchased its own acceptance or deferred payment undertaking.”⁹⁹

It is submitted that Art.7 alone cannot solve any of the “problems” brought about by *Banco Santander*. Most importantly, if the confirming bank knowingly presents non-complying documents to the issuing bank (such that it has not provided a “complying presentation”), then it should not be entitled to payment. Only Art.12 will carry across the risk from the confirming

⁹⁸ Deborah Horowitz,(n 83).

⁹⁹ P. Taneja, “UCP 600”, p.2, available at <http://iccbooks.com/Home/CredibilityofLCs.aspx> [Accessed June 26, 2008].

bank to the issuing bank, but that provision, in turn, needs Art.7 to confirm that payment is required.¹⁰⁰ Nonetheless, other practitioners have also referred only to Art.7:

“Article 7(c) UCP 600 states, in effect, that if fraud happens during this period, then the issuing bank is liable to reimburse the confirming bank.”¹⁰¹ Actually, Art.7(c) does *not* say that, “in effect” or at all.

Professor Ellinger has recently discussed both Art.7(c) and Art.12. He refers to the last sentence of Art.7(c) (the independence of the issuing bank's obligation to the confirming bank) and then states:

“Notably, the liability to the ‘nominated bank’ arises when a complying presentation is tendered by such bank to the issuer. The emphasis thus is on the complying presentation tendered by the nominated bank. A fraud or forgery, affecting the authenticity of the documents tendered, should accordingly not be an issue between the issuing bank and the nominated bank.”¹⁰²

Professor Ellinger added the following footnote to the last sentence quoted above: “Militating against the ruling in *Banco Santander*”¹⁰³, which indicates that he appears to regard Art.7(c) as a cure for the result in *Banco Santander*. In relation to Art.12(b), he describes the Article, and then adds, in a footnote: “This provision, too, seeks to side-step the ruling in *Banco Santander*.”¹⁰⁴. Similarly, Professor Goode has recently commented that Art.12(b) “is designed to reverse the

¹⁰⁰ Robert Parson, (n 40)

¹⁰¹ G. Wynne and F. Nash, “UCP 600 Coming Soon to a Letter of Credit Near You”, available at <http://www.dentonwildeapte.com/assets/B/BankNotes2006.pdf> [Accessed March 29, 2007].

¹⁰² P. Ellinger, “The Uniform Customs and Practice for Documentary Credits (UCP): Their Development and the Current Revisions” [2007] L.M.C.L.Q. 152, 163.

¹⁰³ *ibid*

¹⁰⁴ *ibid*

effect of that decision”.¹⁰⁵ Notably, both authors have, admittedly, qualified their statements: Ellinger says that the provision “seeks to” side-step the ruling; Goode states that it is “designed to” reverse *Banco Santander*. Evidently, both comments leave open the possibility that the provisions will not, in fact, work. Slightly less reticently, the latest edition of *Paget's Law of Banking* observes:

“Under the draft UCP 600, it appears that the outcome in the *Banco Santander* case will in the future be reversed, since the mandate of a nominated bank is expressly stated to extend to discounting a deferred payment obligation” (referring to Art.12(b), as well as Art.7(c)).¹⁰⁶

In addition, Janet Ulph notes that Art.12 “is intended to respond to the furore created by the *Banco Santander* case”,¹⁰⁷ and in banking circles, Standard Chartered Bank (a well-known confirming bank and discounter) has reported that Art.12(b) “represents a major change in the scope of the UCP”.¹⁰⁸ Notably, the new provisions do not “overturn” the position regarding assignment; and there is no new exposure for the beneficiary only for the issuing bank, which is then passed on, typically, to the applicant.

However, the purpose of the above surveyed comments is to indicate the potential trouble caused by the new UCP provisions. Notably, future courts may base the apparent “reversal” of *Banco Santander* on Art.7, or on Art.12, or both. Problematically, they may simply assume that the new provisions deal with the assignment issue, when they do not expressly do so at all.

¹⁰⁵ Roy Goode *et al.*, *Transnational Commercial Law: Text, Cases and Materials* (OUP, Oxford, 2007)p.360.

¹⁰⁶ Mark Hapgood, *Paget's Law of Banking*, (13th edn, Butterworths, London 2006), para.35.12.

¹⁰⁷ J. Ulph, (n 78).

¹⁰⁸ Gary Collyer, “UCP 600 an Analysis of Articles 7-13” (2007) 3 *Standard Chartered Newsletter* 3.

B. Typographical Errors

Typographical errors in a letter of credit (which are common) can give rise to difficulties where the documents presented accurately state the address (note this is by far the most common way in which this difficulty arises). A banker checking documents in an obscure jurisdiction may not know whether a town spelt slightly differently is a typographical error or is a reference to a completely different place.

As Lord Justice Evans observed in the *Kredietbank* case:¹⁰⁹

'... The distinction between "trivial" discrepancies and those which require the bank to reject the documents tendered (subject to further express instructions from the customer) is not always easy to draw.'

Be that as it may, the ICC have sought to codify one aspect of the problem by providing in the new Art 14(j), which addresses that the beneficiary and the applicant need not be identical so long as they refer to the same country. The exception being with transport documents subject to new Arts 19-25, in which case the contact details for the applicant as the consignee or notify party must correspond to the credit.

As with any change to an admittedly problematic draft, there is the risk that the new wording causes more problems than it solves. Whilst the general clarity may be welcomed, there is still no easy answer to the problem of whether a banker checking documents in London should regard a

¹⁰⁹ *Kredietbank Antwerp v Midland Bank Plc*,

reference to, for example, 'Turku-Pori, Finland' as equivalent to 'Turku, Finland(The answer is in fact that they are two completely different places.)'.¹¹⁰

C. Non-Documentary Conditions

One of the “great successes” of UCP 500 was Art. 13(c), which allows banks to disregard non-documentary conditions even if they would usually expect to see the necessary information in a stipulated document. The new UCP 600 provides that all non documentary conditions are to be disregarded. On a similar theme, UCP 600 has renounced ICC position papers 1-4, which *inter alia*, dealt with the problems of non-documentary conditions,¹¹¹ providing that in general they would be ignored save where the non-documentary condition 'can be clearly linked to a document stipulated in that documentary credit'. The principle that non documentary conditions are to be disregarded is now found in Article 14 (h) and there is no obligation on banks to look for a document which could satisfy that condition. Thus a condition that goods are of Chinese origin in a credit calling for a certificate of origin will be interpreted as a data content requirement for the certificate.¹¹²

Sub-article 14h in UCP 600 (and sub-article 13c in UCP 500) encourages good practice, but whether it can justify overriding a specifically stated condition in a credit which cannot be verified by a stipulated document in all circumstances is a matter of at least a little doubt. There may be circumstances where the answer may well be to invite the parties to the credit who wish a condition to stand without stipulating a supporting document to verify the condition, to amend

¹¹⁰ P. Downes, (n 1)p.5-6.

¹¹¹ ICC Position Papers No.3.

¹¹² *ibid*

the credit as necessary or in the last resort to exclude sub-article 14h. It is an area where the common sense of the practitioner based on experience, the knowledge of the trade, the customer and other factors, i.e. the nature of goods, their value and their destination, may help to make a sound judgment and generally that is what an experienced practitioner does.

Furthermore, the upshot is that the abandoning of the position papers and the provisions of new Art 14(h) requiring banks to disregard all non-documentary conditions may give rise to an increase in consistency arguments. In practice, it may be difficult to give no regard whatsoever to all non-documentary conditions where they have a very close connection to a required document. It is not difficult to imagine hard cases coming before the courts (particularly if there is a suggestion of fraud) and judges straining to qualify the absolute prohibition contained in new Art 14(h).¹¹³ As Turnbull says, problem can still arise where it is not clear whether a documentary condition relates to a listed document contained in the credit. That if a credit requires a certificate of origin to be presented and also stipulates as a condition that the goods originate in France then a potential problem may arise.¹¹⁴ The cancellation of the Position Paper is nevertheless justified as the ICC cannot hold the practitioner's hand in every circumstance of every presentation.

D. Data Content Essential.

The drafting group in introducing this change to the banking community have been at pains to emphasise that where a letter of credit merely calls for a document without saying what it must provide: the document presented will be acceptable whatever its contents. Thus where a contract for the supply of frozen chickens is supported by a letter of credit calling for an inspection

¹¹³P. Downes, (n 1)p.5.

¹¹⁴ *ibid*

certificate without more: the condition will be satisfied if an inspection certificate is presented even if it does not 'pass' the chickens: for example stating that they are unfit for human consumption. But how far can this example be taken? If the inspection certificate observed that the chickens were no longer 'frozen' would this suffice? Or if it observed that the chickens had nearly thawed? The new draft seeks to reduce discrepancies by taking such consistency issues out of play: but in so doing many have observed that common sense might be taking a back seat.¹¹⁵

E. A Revocable Credit cannot be Subject to UCP 600.

Another important amendment is the removal of revocable credits. Under the UCP 500, Article 6 distinguished between revocable and irrevocable credits and Article 8 further provided for the revocation of a credit. There was a preference for irrevocable credits in UCP 500, as it there was a presumption that a credit would be irrevocable if it did not expressly set out whether it was revocable or not. The UCP 600 by contrast does not expressly deal with revocable credits. This firm move away from revocable credits is demonstrated in Articles 2, 3 and 10. Article 2 defines a credit as "any arrangement, howsoever named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honour a complying presentation." Article 3 adds to this that a credit is irrevocable even if there is no indication to that effect. Further, Article 10(a) makes it apparent that without the consent of the beneficiary, a credit cannot be revoked. This default position, that credits are irrevocable, favours the interests of the seller/beneficiary who has the benefit of a binding obligation from the bank that payment will be made on presentation of conforming documents.

¹¹⁵ *ibid.*

In practice, revocable credits are rare. However, there are situations where the parties agree that upon the satisfaction of a given contingency, a letter of credit may be revoked. In such circumstances, issuers should express the letter of credit to be subject to UCP 500. A reference to UCP 600 will create an internal inconsistency in the credit which would not easily be resolved.¹¹⁶

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¹¹⁶ *ibid*

Chapter Four

Areas Which Should Have Been Improved But Not Changed

In this section we shall be looking at some of the areas which are not changed by the UCP 600 and may be seen as its weakness. That is there are some issues that are not dealt with by the UCP 600, however, which continue to cause controversy and confusion in the law of documentary credits. For example, some of these are: Exceptions to the Principle of Autonomy, Conflict of Laws, Money Laundry and finally, Acceptance Credit and Deferred Payment Credit. But one may argue that some of these issues have points to justify its omission under the new UCP.

A. Exceptions to the Principle of Autonomy

In any sales transaction, there is a risk that the goods supplied will be defective in some respect. If the defect is serious, or the wrong goods are delivered or no goods are supplied at all, it is easy for the buyer to jump to the conclusion that the seller is dishonest. A general principle, which was spelt out in Art.3 (a) of the UCP500 and which has been carried through into Art.4 of the UCP600, is that the banks are concerned with documents and not with the performance of the underlying contract. Thus, if there is a breach of that contract, the applicant cannot ordinarily stop his or her bank from fulfilling its primary obligation to honour the credit where the documents presented appear to comply with its requirements. Any dispute over the nature and quality of the cargo is a matter for the seller and buyer which can be settled by litigation or arbitration.¹¹⁷

¹¹⁷ *R. D. Harbottle (Mercantile) Ltd v Nat West Bank* [1978] Q.B. 146.

Nevertheless, the principle that the letter of credit is independent of any underlying contract is subject to a well-established exception of fraud. The scope of this exception is hedged round with restrictions by English courts: it only applies if a third party has not acquired rights¹¹⁸ and where it can convincingly be shown that the beneficiary has been knowingly dishonest.¹¹⁹ The exception is narrowly confined to situations where the beneficiary fraudulently present documents that contain material misrepresentations of fact, which he or she knows are untrue and the fraud comes to the notice of the bank. Fraud by independent third parties is irrelevant.¹²⁰ The exception has been construed narrowly because the purpose of irrevocable documentary credits has always been to provide the seller with much needed reassurance that he or she would be paid before he or she transferred control of the goods.¹²¹

Although the fraud exception to the autonomy of the credit is well established worldwide,¹²² there is no express reference to it in the UCP500.¹²³ Equally, the UCP600 leaves questions of fraud to the relevant municipal law. This could be seen as a weakness,¹²⁴ but it must be borne in mind that the precise scope of the fraud exception remains controversial. For example, not all

¹¹⁸ For example, a holder in due course of an accepted bill of exchange can enforce it regardless of disputes relating to the underlying transaction. For a discussion querying whether, from a policy perspective, third parties should have priority, see Sappideen, R. Sappideen, (n 37) at pp. 141-142

¹¹⁹ The burden of proving fraud is a heavy one where the applicant seeks an injunction to prevent the bank paying: *Discount Records Ltd v Barclays Bank Ltd* [1975] 1 W.L.R. 315; *Edward Owen Engineering Ltd v Barclays Bank International Ltd* [1978] Q.B. 159.

¹²⁰ *Montrod Ltd v Grundkötter Fleischvertriebs GmbH* [2002] 1 W.L.R. 1975.

¹²¹ *United City Merchants (Investments) Ltd v Royal Bank of Canada, The American Accord* [1983] 1 A.C. 168 at 183-184 *per* Lord Diplock.

¹²² The leading decision is *Sztejn v J Henry Schroder Banking Corp* (1941) 31 N.Y.S. 2d 631. Also, X. Gao, *The Fraud Rule in the Law of Letters of Credit-A Comparative Study* (Kluwer, 2002).

¹²³ Reinhard Langerich "UCP Should Not Deal With Fraud. Right? Wrong," (2000) Vol. 6, No. 3, *Insight*, p. 9.

¹²⁴ "Shiao-Lin Kuo, "Scope of letter of credit fraud" (1995) *Documentary Credits Insight*, published by ICC, Vol. 1, No. 4; "Simon Jones "Reports on Court Cases dealing with L/C Fraud" (1999) Vol. 5, No. 2 *Documentary Credits Insight*, published by ICC; Spring; "P.K. Mukundan Warns About Cybercrime, Phony bills of Lading and Other Scams", (1999) Vol. 5 *Documentary Credits Insight*, published by ICC

jurisdictions accept the English courts' view that banks must pay for documents which are nullities provided the seller and his or her agents have acted in good faith and the document appears conforming.¹²⁵ Furthermore, it is unclear whether the notion of fraud could be drawn to encompass more than dishonesty on the part of the beneficiary. In Australia, for example, there have been suggestions that unconscionable conduct of a gross nature might suffice.¹²⁶ The drafters of the new revision were wise to leave the fraud exception to the law of various jurisdictions. It must be recalled that the UCP is concerned with matters of good banking practice, which the parties voluntarily incorporate into their contracts; it would be a futile exercise to draft provisions which conflicted with domestic law.

Fraud is an especially complex problem and the risk is best thrown on to applicants and their advisers who are in the best position to check on the people they choose to do business with. Banks can also play a significant role by scrutinising documents carefully, particularly the bill of lading.¹²⁷ One possible method of tackling the risks of fraud is to require the beneficiary to warrant that the documents presented are not forged or otherwise fraudulent. The advantage of such a warranty is that it gives a bank more power to refuse documents because it can rely upon the warranty alone rather than the fraud exception. However, neither the UCP500 nor the UCP600 deal with warranties. Its omission does not indicate disapproval. The UCP does not

¹²⁵ *Montrod Ltd v Grundkötter Fleischvertriebs GmbH* [2002] 1W.L.R. 1975. This decision was distinguished by the Singapore Court of Appeal on the basis that it concerned an unauthorised document rather than a forged one: *Beam Technologies v Standard Chartered Bank* [2003] 1 S.L.R. 597; L. Y. Chin and Y. K. Wong, "Autonomy-A Nullity Exception at Last?" [2004] L.M.C.L.Q. 14.

¹²⁶ *Hortico (Australia) Pty Ltd v Energy Equipment Co (Australia) Pty Ltd* (1985) 1 N.S.W.L.R. 545; *Inflatable Toy Co v State Bank of NSW* (1994) 34 N.S.W.L.R. 243; contrast *Olex Focas Pty Ltd v Skodaexport Co* (1996) 134 F.L.R. 331. Also See X. Gao, *The Fraud Rule in the Law of Letters of Credit--A Comparative Study* (Kluwer, 2002), pp.94-96.

¹²⁷ P. Holst, (n 36). It should be noted that Art.19 of the UN Convention on Independent Bank Guarantees and Standby Letters of Credit 1995 recognises a fraud exception.

cover every issue and some matters may be best left to domestic courts which are free to accept an express warranty, or to imply one, where appropriate.¹²⁸

Apart from established fraud, there have been other situations where the courts have suggested that an injunction could be granted to prevent the bank paying on a letter of credit. One example is total failure of the basis of the contract¹²⁹; another is illegality, if it can be proved.¹³⁰ Both exceptions are controversial and their scope is uncertain. No mention of such matters is made in the UCP. It can be argued that, for the foreseeable future, the position in relation to any exceptions to the autonomy principle is best left to be regulated by market forces. If courts in a particular country provide wide-ranging exceptions, beneficiaries will demand that their credits are confirmed by banks located in other jurisdictions.¹³¹

B. Conflict of Law

Another issue is the conflict of laws. The UCP 600 (and its predecessors) does not contain any governing law or jurisdiction clauses. This is because the credit law found in the UCP is based upon *lex mercatoria*. However, although there are some internationally accepted banking standards and practice, there is no separate body of *lex mercatoria*. Although the majority of credit problems can be dealt with by reference to the articles, there will inevitably remain some issues that will fall outside the UCP and be governed by domestic legal systems.¹³² In failing to

¹²⁸ *Bayerische Vereinsbank Aktiengesellschaft v National Bank of Pakistan* [1997] 1 Lloyd's Rep. 59; Dolan, above fn.17, pp.536-537.

¹²⁹ *Elian and Rabbath v Matsas* [1966] 2 Lloyd's Rep. 495; contrast *Howe Richardson Scale Co Ltd v Polimex-Cekop* [1978] 1 Lloyd's Rep. 161.

¹³⁰ *Mahonia Ltd v JP Morgan Chase Bank* [2004] EWHC 1938 at [427]-[428] (violation of US security laws); N. Enonchong, "The Autonomy Principle of Letters of Credit: an Illegality Exception?" [2006] L.M.C.L.Q. 404.

¹³¹ J. F. Dolan, (n 28) at pp.533-534

¹³² Such as the fraud exception, and the controversial illegality and nullity exceptions.

regulate the governing law and jurisdiction that is to govern documentary credit disputes, the UCP ignores the situation whereby plaintiffs will bring their claims in a forum most likely to grant a favourable remedy rather than the forum with the closest relationship to the credit transaction.¹³³ This decreases certainty in commercial relationships and allows a plaintiff to dictate where a dispute will be resolved to the detriment of the defendant.

C. Money Laundering

There is no reference to money laundering legislation in the UCP600 despite the fact that international trade offers myriad opportunities for storing, moving and converting assets into money. English banks are affected in three ways by domestic legislation. First, they must have “know your client” (KYC) procedures to check upon the identity of new customers.¹³⁴ Secondly, they are expected to report suspicious activity transactions to the Serious Organised Crime Agency where they know or suspect, or objectively have reasonable grounds to know or suspect that a person is engaged in money laundering¹³⁵; suspicious activities would include, for example, unusual manipulations of money or obvious under-valuations of cargoes. Finally, bank officers can be guilty of a criminal offence if, for example, they receive “dirty money” or assist in transferring the money abroad which they knew or suspected was derived from criminal activity.¹³⁶ Consequently, if the applicant for a credit seems to have inexplicably obtained large amounts of money, banks should enquire further in order to protect themselves from exposure to criminal liability.

¹³³ P Ellinger (n 14) 43-44

¹³⁴ Money Laundering Regulations 2003 (2003/3075), s.4; J. Ulph, *Commercial Fraud--Civil Liability, Human Rights, and Money Laundering* (OUP, London 2006), paras 3.09 to 3.11.

¹³⁵ Proceeds of Crime Act 2002, ss.330 and 331.

¹³⁶ Proceeds of Crime Act 2002, as amended by the Serious Organised Crime and Police Act 2005, ss.327-329.

Although there is a *force majeure* clause in Art.36 of the UCP600, it is submitted that the drafters were right not to attempt to extend it to protect a bank from civil action by its customer whilst the account is frozen; this is something which should be governed by a country's domestic law. It would seem odd to include the detailed requirements of criminal money laundering offences (including *mens rea*) within a code of banking practice. It is therefore submitted that the drafters of the UCP600 were right to exclude any detailed consideration of money laundering measures. It is a fast-moving area of law and it may well have been difficult to discern some general principles which would not have rapidly become outdated.¹³⁷ On the other hand, some brief reference to the guidance provided from time to time by the Joint Money Laundering Steering Group¹³⁸ in the introduction to the UCP600 might have been useful in order to acknowledge the challenges posed by money laundering and international criminal activity.

D. Acceptance Credit and Deferred Payment Credit.

A regrettable omission in the new UCP is its failure to define “acceptance credit” and “deferred payment credit”.¹³⁹ Although there is a general view that these terms are notorious in banking practice, as far as legal implications are concerned a recent Chinese case demonstrates how problematic such terms can be. In *Finanz AG Zurich v Guangdong Development Bank* (Beijing Branch),¹⁴⁰ the issuing bank had refused to pay an acceptance at maturity to a “holder in good faith” on the basis that the draft was not stamped or signed. It argued that there was thus no

¹³⁷ E.g. Regulation 1781/2006 of November 15, 2006, which requires banks to provide information concerning the payer in an international transaction.

¹³⁸ The website is: <http://jmlsg.org.uk>

¹³⁹ Jason Chuah, “UCP 600 New Challenges and Issues” (2007) 13 (2) JIML, at p74.

¹⁴⁰ As abstracted in Documentary Credit World (2006) April Issue .p 11

acceptance. The Chinese court sensibly ruled in favour of the holder but as the dispute demonstrates, there is no universal definition of what constitutes “acceptance”.¹⁴¹

In general, though, the new revision adheres closely to the pattern and spirit of the earlier revisions, it constitutes a step in the right direction but a great deal of work has been left for future draftsmen. Some, undoubtedly, will be required in consequence of future developments in technology and business practice. However, many current imperfections have not been tackled in the instant exercise.

In the first place, the draftsmen set out to proscribe certain practices but, regrettably, did not perfect the prohibitions by adding “teeth” to the respective provisions. A striking example is the treatment of letters of credit available by the acceptance of bills of exchange drawn on the applicant. Article 6(a) proscribes their use but fails to state the consequences of a failure to comply.

In the second place, the new revision fails to tackle the problem of letters of credit opened by institutions that are not banks. Indeed, the term “bank” remains undefined.¹⁴² In some countries, it encompasses not only trading and merchant banks, which are in the business of issuing letters of credit, but also savings and investments banks which in other jurisdictions, may be regarded as specialised financial institutions outside the regime provided for ordinary banks.¹⁴³ Occasionally, “banks” might be given diverse constructions even in one specific jurisdiction. In English law, for instance, a given institution may constitute a bank for the purposes of the

¹⁴¹ Jason Chuah, (n 139) at p74.

¹⁴² Commentary on UCP 600 by the UCP 600 drafting group, p.17.

¹⁴³ *ibid* at p18.

Banking Act 1987 but fail to satisfy the common law definition employed in the Bills of Exchange Act 1882. The absence of a definition of such an ambiguous word in statutory provisions suggests that it is used in a generic sense. On this basis, it is arguable that the word “bank” in the UCP is used to describe any financial institution that is in the business of issuing documentary credits.¹⁴⁴

In the third place, the meaning of “negotiation” is less clear under UCP 600 than under its predecessor. Indeed, the ambiguity of the definition in UCP 600, Art 2 is bound to constitute a source of litigation. In the fourth place, the draftsman has not synchronized UCP 600 and the ISBP. The exercise may be undertaken in the future but, at this stage, the ensuing lacuna leaves many banks and lawyers puzzled. A harmonization exercise is, furthermore, required in respect of the UCP. There is another concern that has not yet been resolved. Article 28(h) refers to ‘all risk’ insurance, but because of differences in liabilities between countries, it is unclear as to what the article intends. Indeed, the ICC itself is now suggesting that “a documentary credit should not call for an insurance coverage against ‘all risks’ because there are various types of ‘all risk coverage in different markets.’”¹⁴⁵

Finally, UCP 600 constitutes to treat the code as a source of standard terms application by incorporation. Undoubtedly, the recognition of the UCP as an independent source of law requires an international agreement or treaty, followed by ratifications and local Acts. Art 1, though, may

¹⁴⁴ P. Ellinger, “The Uniform Customs and Practice for Documentary Credits (UCP): Their Development and the Current Revisions” [2007] L.M.C.L.Q. 152, 178.

¹⁴⁵ ICC, 2007, p133.

preclude courts of justice from taking the independent step of recognising the code as an autonomous source of law.¹⁴⁶

Apart from the observations respecting the code, it is important to bear in mind that many disputes arise from inadequacies in the drafting of specific letters of credit or, even, from deficiencies in banks' standard terms and condition in point. *Kumagai's case*¹⁴⁷ demonstrates the point. If, in that case, the issuing bank had refused to incorporate non-documentary requirements in the letter of credit there under consideration, the dispute would not have arisen. In this case the letter of credit included a number of conditions without making provisions for documents to be tendered in respect thereof. Notwithstanding UCP500, Art 13 (c), under which non- documentary conditions were to be treated as unread, it was held that the express terms of the letter of credit manifested the intention of the parties. Accordingly, under the doctrine of freedom of contract, the express terms took priority over a standard term, such as Art 13 (c), incorporated by reference.

Forestall Mimosa v Oriental Credit,¹⁴⁸ provides another example of a poorly drafted letter of credit. It is believed that many disputes could be avoided if banks exercised greater caution in their daily practice or in the periodic revision of their standard forms. It would, for instance, be advisable to include in standard forms a clause subjecting any specific provision in an individual letter of credit to the provisions of the code.¹⁴⁹ Undoubtedly, some technical provisions of the

¹⁴⁶ P. Ellinger, "The Uniform Customs and Practice for Documentary Credits (UCP): Their Development and the Current Revisions" [2007] L.M.C.L.Q. 152, 163

¹⁴⁷ *Kumagai- Zenekon v. Arab Bank* [1997] 3 SLR770.

¹⁴⁸ [1986]1 WLR 631

¹⁴⁹ Such a clause would have solved the issues arising in cases such as *kumagai- Zenekon v Arab Bank* [1997] 3 SLR 770. It would not necessarily solve problems arising where a credit calls for a draft to be drawn on the applicant.

code will require re-visiting in the course of the next decade. It is to be hoped that working groups would, in the future, include a wider spectrum of members.

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Chapter Five

Conclusion

The revisions of the UCP have been regularly praised when promulgated. There is no doubt that the 2007 revision – UCP 600 is progressive and ought to advance the uniformity of the law and practice respecting letters of credit. In many regards it has tightened the language and clarified obscurities left in UCP 500. The major achievements of UCP 600 are the exclusion of revocable credits from the framework of the code, the relaxation of the prescribed rejection procedure, the introduction of concept of “honour”, and the provisions respecting “availability”.¹⁵⁰ The new rules of the UCP 600 signal a move towards more certainty in letter of credit law. It clarifies the positions of each of the parties involved in the use of credits; that is the bank, the applicant and the beneficiary. This is achieved through the new Articles 2 and 3, the clarification of both the standard of examination of the documents and the documents that can be accepted as original.

Accordingly, it was reasonable for the drafters of the new UCP to seek to alleviate the negotiating banks' pain. In some respects, they have successfully done so. It is evident that Art.7 (and other provisions) increases the overall abstraction of the credit from the underlying transaction. Further, Art.12 plainly deals with the authorisation point from *Banco Santander*, which also increases the abstraction of the credit (although issues of authorisation to discount should rarely be affected by the underlying sale transaction). However, several problems remain. First, there is the simple issue of definitions and their consequent effects. If a confirming bank presents forged documents, then this will not be a “complying presentation”, and there may be an

¹⁵⁰ Such as the International Standby practices (the ISP98)

argument for an issuing bank that wishes to deny payment. Further, the “prepayment” terminology will undoubtedly cause problems for the courts, and again, issuing banks may seek to slip out of their payment undertakings on the basis of this loose wording (“prepay” versus “agreeing to advance funds” early). More importantly, it is difficult to see how the UCP 600 can be said to have dealt with the assignment point. Some commentators seem simply to have assumed that it does, without considering the finer details of the provisions and their relationship with the “subject to equities” rule. It is highly likely that if a confirming bank, having taken an assignment, presented documents and awaited payment, an issuing bank would seek to raise a fraud defence if present on the facts. Moreover, it would have a solid argument that the UCP 600 has not catered for that eventuality, and that the omission was deliberate (especially in comparison with the express reference to assignment in the UCC).

However, some of the changes made by the new UCP may have little effect on the percentage of documents rejected on first presentation as discrepant.¹⁵¹ This is particularly true in relation to linkage between documents: the strict requirements that documents must not be inconsistent with each other could have been dropped.¹⁵² The UCP has never been a comprehensive code; not only will users be obliged to refer to domestic law on particular matters, such as the fraud exception, but also to the ISBP in relation to the banks' examination of documents. Despite these criticisms, if the revised UCP provides certainty and predictability in relation to the application of its rules, it will save unnecessary litigation and will make documentary credits a more attractive choice. The fact that there has been confusion in the past over quite basic matters, such as the concept of

¹⁵¹ G. Collyer, (n 47) at p.23 ; P. Taneja, (n 64)

¹⁵² *ibid*

negotiation, convincingly supports the argument that the structure and style of the UCP needed revision. In general, vague words have been eradicated; those that have been retained appear to favour the banks. For example, banks are still required to communicate with each other “without delay”¹⁵³; as no period of time is specified, it will be difficult to challenge a bank's actions in this regard. Nevertheless, the drafters appear to have largely succeeded in their aim of creating provisions which are free from ambiguity, thereby minimising the risk of national courts offering different interpretations of its rules.

Moreover, these measures are movements in the right direction to ensure that the documentary credit procedure remains as expedient as possible. There are some issues that are not dealt with by the UCP 600, however, which continue to cause controversy and confusion in the law of documentary credits. One such issue is the ambit of the fraud exception to the autonomy principle, which is not even mentioned in the UCP. Instead each jurisdiction takes a different approach to fraud resulting in uncertainty in this area of the law.

Another issue is the conflict of laws. The UCP 600 (and its predecessors) does not contain any governing law or jurisdiction clauses. This is because the credit law found in the UCP is based upon *lex mercatoria*. However, although there are some internationally accepted banking standards and practice, there is no separate body of *lex mercatoria*. Although the majority of credit problems can be dealt with by reference to the articles, there will inevitably remain some issues that will fall outside the UCP and be governed by domestic legal systems.¹⁵⁴ In failing to regulate the governing law and jurisdiction that is to govern documentary credit disputes, the

¹⁵³ UCP600, Arts 8, 9, 10, 11 and 35; UCP500, Arts 7, 9, 11, 12, 14 and 16.

¹⁵⁴ Such as the fraud exception, and the controversial illegality and nullity exceptions.

UCP ignores the situation whereby plaintiffs will bring their claims in a forum most likely to grant a favourable remedy rather than the forum with the closest relationship to the credit transaction.¹⁵⁵ This decreases certainty in commercial relationships and allows a plaintiff to dictate where a dispute will be resolved to the detriment of the defendant.

All in all, the UCP 600 makes positive strides towards greater certainty in letter of credit law, despite the fact that some key opportunities were missed. It is hoped that these issues will come to the fore in future revisions. Arguably, even if the number of documents rejected is not reduced significantly after the UCP600 is used, it will still be judged a success. Like its predecessors, it can be seen as harmonising rights, duties and practice in relation to the operation of documentary credits, thereby aiding cross-border business. However, the biggest achievement of this revision is the introduction of a clear, light and open style which will aid comprehension and predictability.

Gary Collyer, Head of the ICC group that drafted the rules, says the new UCP has obvious advantages, including an easier-to-read text and a simplified structure. Without UCP 600, the use of Documentary Credits would continue to decline, and banks would lose significant trade finance revenue. The UCP 600 does provide an improvement to the previous version of the rules, but a new set of rules means that there is room for uncertainty. A revision of the rules was undoubtedly needed to modernise the provisions and in doing so reassess, clarify, consolidate and improve the UCP and international practice regarding documentary credits.

¹⁵⁵ P. Ellinger (n 14) 43-44.

In conclusion, one might say that the UCP 600 certainly represents a significant improvement to the UCP 500. The precise effect of the changes it has brought has been very difficult to judge. Nonetheless, the UCP 600 has addressed a genuine fear that the commercial value of letters of credit might be undermined by too frequent rejections of documents presented under letters of credit. There is a fine balance to be struck because discrepancies may affect the integrity of a credit. Strict compliance in relation to conforming documents, therefore, remains essential. The UCP 600, whilst still upholding the need for strict compliance in relation to genuine inconsistencies in documents, has undoubtedly impacted upon the approach to be taken by the banks and enabled a distinction to be drawn between unnecessary rejections on entirely technical grounds and truly non-compliant presentations.¹⁵⁶

¹⁵⁶ The long-established "doctrine of strict compliance" was considered at some length in *Soproma SpA v Marine & Animal By-Products Corporation* [1966] 1 Lloyd's Rep 367.

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