Variant C: result by implication from the terms of the guaranty letter. [3]

References

A/CN.9/345, paras. 84-94, 102-103
A/CN.9/WG.II/WP.71, paras. 5-21, 36-43

Remarks

1. As indicated in remark 3 on article 1, the issue of the territorial scope of application of the uniform law, if adopted in the form of a model law, would be settled by conflict-of-laws rules as presented here. It may be noted, however, that the territorial scope of application thus settled by articles 26 and 27 does not encompass these two articles themselves, nor does it encompass the provisions on jurisdiction as they are addressed to the courts of the State implementing the model law.

2. The parties designating (*i.e.* agreeing on) the applicable law are the guarantor and the beneficiary, as made clear in article 6(*c*). That might raise the question as to whether such designation would be relevant to the legal position of the principal, for example, where the solution adopted in the designated law is less advantageous than the solution obtaining from the otherwise applicable law. It is submitted that, from a practical point of view, the problem is of limited importance since the guarantor is unlikely to include, without instructions or consent by the principal, in the guaranty letter the choice of a law, at least not that of a State other than where the guarantor has its place of business. Apart from that, the designated law applicable to the guaranty letter is unlikely to interfere with the separate relationship between the guarantor and the principal in that it limits itself to regulating the rights and obligations under the guaranty letter; such regulation, as illustrated by the substantive provisions of the uniform law, may, however, affect in an indirect manner the legal position and interests of the principal, and it often takes into account any agreement between the guarantor and the principal.

3. Variants A, B and C are based on the various suggestions, made at the fifteenth session, as to which non-express modalities of choice should be allowed (A/CN.9/345, para. 93).

Article 27. *Determination of applicable law*

Failing a choice of law in accordance with article 26, [the rights and obligations arising out of] [the rights, obligations and defences relating to] a guaranty letter are governed by the law of the State where the guarantor has its place of business or, if the guarantor has more than one place of business, where the guarantor has that place of business at which the guaranty letter was issued. [1] [However, if according to the guaranty letter the examination of the demand and any required documents takes place in another State the law of that State applies to the standard of care and responsibility for such examination, failing a specific agreement to the contrary.] [2]

References

A/CN.9/345, paras. 95-103
A/CN.9/WG.II/WP.71, paras. 22-35, 38

Remarks

1. Consideration might be given either to using one of the shorter wordings presented in article 25 or to consolidating all provisions dealing with a plurality of places of business in a single provision within article 6, if the same criterion were deemed appropriate in all cases (see remark 2 on article 4).

2. The sentence between square brackets has been added to invite consideration of a suggestion made at the fifteenth session (A/CN.9/345, para. 99, based on the discussion in A/CN.9/WG.II/WP.71, paras. 32 and 38).

C. Report of the Working Group on International Contract Practices on the work of its seventeenth session

(New York, 6-16 April 1992) (A/CN.9/361) [Original: English]

CONTENTS

INTRODUCTION

1. Pursuant to a decision taken by the Commission at its twenty-first session,[1] the Working Group on International Contract Practices devoted its twelfth session to a review of the draft Uniform Rules on Guarantees being prepared by the International Chamber of Commerce (ICC) and to an examination of the desirability and feasibility of any future work relating to greater uniformity at the statutory law level in respect of guarantees and stand-by letters of credit (A/CN.9/316). The Working Group recommended that work be initiated on the preparation of a uniform law, whether in the form of a model law or in the form of a convention.

2. The Commission, at its twenty-second session, accepted the recommendation of the Working Group that work on a uniform law should be undertaken and entrusted this task to the Working Group.[2]

3. At its thirteenth session (A/CN.9/330), the Working Group commenced its work by considering possible issues of a uniform law as discussed in a note by the Secretariat (A/CN.9/WG.II/WP.65). Those issues related to the substantive scope of the uniform law, party autonomy and its limits, and possible rules of interpretation. The Working Group also engaged in a preliminary exchange of views on issues relating to the form and time of establishment of the guarantee or stand-by letter of credit. The Working Group requested the Secretariat to submit to its fourteenth session a first draft set of articles, with possible variants, on the above issues as well as a note discussing other possible issues to be covered by the uniform law.

4. At its fourteenth session (A/CN.9/342), the Working Group examined draft articles 1 to 7 of the uniform law prepared by the Secretariat (A/CN.9/WG.II/WP.67). The Secretariat was requested to prepare, on the basis of the deliberations and conclusions of the Working Group, a revised draft of articles 1 to 7 of the uniform law. The Working Group also considered the issues discussed in a note by the Secretariat relating to amendment, transfer, expiry, and obligations of the guarantor (A/CN.9/WG.II/WP.68). The Secretariat was requested to prepare, on the basis of the deliberations and conclusions of the Working Group, a first draft of articles on the issues discussed. It was noted that the Secretariat would submit to the Working Group, at its fifteenth session, a note on further issues to be covered by the uniform law, including fraud and other objections to payment, injunctions and other court measures, conflict of laws and jurisdiction.

5. At its fifteenth session (A/CN.9/345), the Working Group considered certain issues concerning the obligations of the guarantor. Those issues had been discussed in the note by the Secretariat relating to amendment, transfer, expiry, and obligations of the guarantor (A/CN.9/WG.II/WP.68) that had been submitted to the Working Group at its fourteenth session but had not then been considered, for lack of time. The Working Group then considered the issues discussed in a note by the Secretariat relating to fraud and other objections to payment, injunctions and other court measures (A/CN.9/WG.II/WP.70). The Working

[1] *Official Records of the General Assembly, Forty-third Session, Supplement No. 17* (A/43/17), para. 22.

[2] Ibid., *Forty-fourth Session, Supplement No. 17* (A/44/17), para. 244.

Group also considered the issues discussed in a note by the Secretariat relating to conflict of laws and jurisdiction (A/CN.9/WG.II/WP.71). The Secretariat was requested to prepare, on the basis of the deliberations and conclusions of the Working Group, a first draft set of articles on the issues discussed.

6. At its sixteenth session (A/CN.9/358), the Working Group examined draft articles 1 to 13 of the uniform law prepared by the Secretariat (A/CN.9/WG.II/WP.73).

7. The Working Group, which was composed of all States members of the Commission, held its seventeenth session in New York, from 6 to 16 April 1992. The session was attended by representatives of the following States members of the Working Group: Bulgaria, Cameroon, Canada, China, Cyprus, Czechoslovakia, Egypt, France, Germany, India, Iran (Islamic Republic of), Iraq, Japan, Kenya, Libyan Arab Jamahiriya, Mexico, Morocco, Nigeria, Russian Federation, Spain, United Kingdom of Great Britain and Northern Ireland and United States of America.

8. The session was attended by observers from the following States: Albania, Algeria, Australia, Austria, Bahamas, Brazil, Côte d'Ivoire, Ecuador, Ethiopia, Finland, Gabon, Guinea-Bissau, Haiti, Holy See, Indonesia, Pakistan, Paraguay, Poland, Romania, Senegal, Sudan, Sweden, Switzerland, Thailand, Uganda, Ukraine, United Republic of Tanzania and Viet Nam.

9. The session was attended by observers from the following international organizations: United Nations Industrial Development Organization (UNIDO), Asian-African Legal Consultative Committee (AALCC), Hague Conference on Private International Law, Banking Federation of the European Community, International Chamber of Commerce (ICC).

10. The Working Group elected the following officers:

Chairman: Mr. J. Gauthier (Canada)

Rapporteur: Mr. A. Ogarrio (Mexico)

11. The Working Group had before it the following documents: provisional agenda (A/CN.9/WG.II/WP.72) and a note by the Secretariat containing tentative draft articles of a uniform law on international guaranty letters (A/CN.9/WG.II/WP.73 and Add.1).

12. The Working Group adopted the following agenda:

1. Election of officers.
2. Adoption of the agenda.
3. Preparation of a uniform law on international guaranty letters.
4. Other business.
5. Adoption of the report.

I. DELIBERATIONS AND DECISIONS

13. The Working Group examined draft articles 14 to 27 of the uniform law prepared by the Secretariat (A/CN.9/WG.II/WP.73 and Add.1). The deliberations and conclusions of the Working Group are set forth below in chapter II. The Secretariat was requested to prepare, on the basis of those conclusions, a revised draft of articles 14 to 27 of the uniform law.

II. CONSIDERATION OF DRAFT ARTICLES OF A UNIFORM LAW ON INTERNATIONAL GUARANTY LETTERS

Chapter IV. Rights, obligations and defences

Article 14. Demand for payment

14. The text of draft article 14 as considered by the Working Group was as follows:

> "Any demand for payment under the guaranty letter shall be made in a form referred to in paragraph (1) of article 7 and in conformity with the terms of the guaranty letter. In particular, the demand shall be made, and received by the guarantor, within the time of effectiveness of the guaranty letter and shall be accompanied by any statement or document required by the guaranty letter [or this Law]. [If no statement or document is required, the beneficiary, when demanding payment, is deemed to impliedly certify that payment is due.]"

First two sentences

15. As regards the words "demand for payment", a concern was expressed that the draft article might insufficiently reflect the practice of stand-by letters of credit. It was explained that the beneficiary of a stand-by letter of credit, when seeking payment, would often present a bill of exchange (or "draft"), in which case the beneficiary would not make a formal demand for payment. The Working Group was agreed that the provision should be redrafted so as to encompass all possible forms in which payment might be requested from the guarantor.

16. As regards the words "any statement or document required by the guaranty letter [or this Law]", a concern was expressed that the current provision might be misinterpreted as recognizing demands for payment accompanied by non-documentary statements. The Working Group recalled that, at its sixteenth session, it had decided that the provisions in the uniform law should focus on instruments containing only documentary conditions (see A/CN.9/358, para. 61).

17. As regards the words "and received by the guarantor", it was stated that the current wording might not clearly accommodate situations where payment was claimed not directly from the guarantor or a confirming bank but from another bank which could either be a bank specifically designated in the text of a stand-by letter of credit as an agent of the guarantor, or any other bank, in the rare case where a stand-by letter of credit was issued in a freely negotiable form.

18. It was noted that article 19 of the draft Uniform Rules for Demand Guarantees (URDG) prepared by the International Chamber of Commerce (ICC), on which article 14 of

the draft uniform law was modelled, mentioned the place where a demand for payment should be presented. It was generally agreed that a mention along those lines should be added in the text of article 14.

Third sentence

19. It was recalled that the sentence between square brackets had been added to clarify, especially in the case of a guaranty letter payable on simple demand, that any demand for payment implied the assertion that payment was due, as might, for example, be relevant in determining whether the demand was improper according to article 19.

20. Differing views were expressed as to the manner in which guaranty letters payable on simple demand should be accommodated by the uniform law. Under one view, the uniform law should focus on guaranty letters payable upon presentation of documents in connection with the non-performance of the underlying commercial obligation. It was thus suggested that article 14 should be redrafted along the lines of article 20 of the draft URDG to the effect that the beneficiary had at least to present a bona fide statement about the principal's default unless the guaranty letter expressly provided otherwise.

21. The prevailing view, however, was that it would not be appropriate for a legislative text such as the uniform law to encourage or discourage the use of any specific type of guaranty letter. It was recalled that guaranty letters payable on simple demand were widely used in practice and that, irrespective of the frequency of use, the Working Group, at its twelfth session, had felt that a legal rule should take into account, and provide certainty for, all types of guarantees in use and leave the choice of the type of guarantee to be used to the credit decision of the parties involved (see A/CN.9/316, para. 89).

22. While some doubts were expressed as regards the substance and wording of the third sentence, the Working Group, after deliberation, agreed to retain the sentence without square brackets.

23. The Working Group requested the Secretariat to prepare a revised draft of article 14 in the light of the above deliberations and decisions.

Article 15. Notice of demand

24. The text of draft article 15 as considered by the Working Group was as follows:

> "[Without prejudice to the provisions of articles 16 and 17, the guarantor shall promptly upon receipt of the demand give notice thereof to the principal or, where applicable, its instructing party, unless otherwise agreed between the guarantor and the principal.]"

25. The Working Group noted that article 15, which was patterned on article 17 URDG, appeared in brackets as opinion had been divided at the fifteenth session on whether the uniform law should impose an obligation on the guarantor to give notice to the principal of a demand made by the beneficiary. At the present session, opinion was again divided as to the desirability of imposing such an obligation.

26. The concerns cited in support of the deletion of article 15 included the following: that the imposition of a statutory duty to give notice to the principal would compromise the integrity, independence and reliability of the guarantor's undertaking, in particular by facilitating the initiation by the principal of steps to block payment; that the only type of contact between the guarantor and the principal concerning the demand for payment should be in the case of a request by the guarantor for a waiver by the principal of discrepancies identified by the guarantor; that the inclusion of an obligation to give notice would run counter to the objective of providing a unified regime covering both guarantees and stand-by letters of credit, since, it was stated, the giving of notice was a procedure that was foreign to stand-by letters of credit and might, in some jurisdictions, raise regulatory concerns, and that the giving of notice was not an established practice as regards guarantees; and that the nature of the notice obligation set forth in article 15 was vague, in particular as to the content of the notice, its timing, and the legal consequences of a failure to give notice. Finally, it was suggested that the principal and the guarantor were free to agree on a notice procedure, that the obligation to give notice could in fact be placed on the beneficiary and that the guaranty letter could always require that documentary evidence of the fulfilment of that obligation accompany the demand for payment, all of which minimized the need to include in the uniform law an obligation to give notice. It was suggested that, in the event the Working Group decided to retain the provision, stand-by letters of credit would need to be exempted.

27. Support for retaining the obligation to give notice was expressed on the grounds that such a procedure enhanced the possibility of negotiated settlements of disputes between the principal and the beneficiary and helped to balance the positions of the two parties. It was also stated that notice to the principal prior to payment was a common practice, that it served to inform the principal that its account was to be debited and that it was a precondition to enable the principal to protect itself in cases of manifestly improper demands. It was also stated that the giving of notice did not compromise the independence of the guarantor's undertaking because the obligation to give notice, as had been decided at the fifteenth session, would not be linked in terms of time to the duty of examining the claim and deciding about payment. In this connection, it was suggested that it should be made clear that non-compliance with the duty of notification would not affect the effectiveness of payment and that the proviso should be reformulated so as to make it abundantly clear that the guarantor was not required to give notice before payment. It was further suggested that the notice procedure, while possibly foreign to stand-by letters of credit, might nevertheless usefully be applied to them.

28. The Working Group considered how some of the concerns that had been raised about article 15 might be addressed, short of deleting that provision. One suggestion was to make the provision more precise as to the consequences of a failure to give notice by providing that the guarantor would be liable for damages. Damages would be available, for example, when the principal could prove that, had timely notice been provided, it could have recovered from the beneficiary the amount paid out by the guarantor.

It was also suggested that it should be made clear that the principal would not be entitled, solely by virtue of a failure to give notice, to refuse to reimburse the guarantor after a claim under the guaranty letter had been paid. Another suggestion was that it should be made clearer that article 15 also applied to counter-guarantors.

29. After deliberation, the Working Group decided to postpone, pending further review, a final decision as to whether it would be desirable to retain a provision along the lines of article 15. It was therefore decided to retain the article in square brackets. The Secretariat was requested, meanwhile, to refine article 15 to address issues that had been raised, including sanctions for failure to give the notice and the independence of the undertaking to pay from the notice requirement.

Article 16. Examination of demand

30. The text of draft article 16 as considered by the Working Group was as follows:

"(1) *Variant A:* In examining the demand and any required statement or document accompanying it, the guarantor shall comply with the standard of reasonable care prevailing in international guaranty and stand-by letter of credit practice to ascertain their facial conformity with the terms of the guaranty letter, which are to be construed strictly.

Variant B: The demand and any required statement or document accompanying it shall be examined by the guarantor with the professional diligence of a knowledgeable, prudent guarantor to ascertain whether they appear on their face to conform with the terms of the guaranty letter and to be consistent with one another.

"(2) Unless otherwise agreed by the parties, the guarantor shall have

Variant X: reasonable time

Variant Y: [four] business days

Variant Z: reasonable time, but not more than [seven] business days in which to examine the demand and to decide whether or not to pay."

Paragraph (1)

31. The Working Group considered two variants of paragraph (1), which is intended to set forth the standard for the conduct of the guarantor in examining a demand for payment and determining whether the demand complied with the terms of the guarantee.

32. Support was expressed for variant A on the ground that it included a reference to an established, internationally recognized standard, namely, the standard of reasonable care prevailing in international guaranty and stand-by letter of credit practice. It was suggested that such an approach, with its implicit reference to UCP, was the more objective of the two variants and would thus protect against the intrusion of exorbitantly strict or unduly lenient standards of examination. It was said that objectivity would be strengthened by virtue of the fact that the revision of UCP currently being carried out was likely to result in more explicit standards concerning the elements to be reviewed when examining principal types of trade documents. Furthermore, the view was expressed that reference to an internationally recognized standard was desirable from the viewpoint of certainty and harmonization. If multiple standards were injected, disputes might arise, in particular as to the right of the guarantor to reimbursement. A view was expressed that there was no substantial difference between variants A and B since the professional diligence of the guarantor could only be determined by reference to the standard of care prevailing in international practice.

33. Reservations were expressed as to variant A on the ground that the uniform law would not fulfil its mandate to establish a standard of conduct for the guarantor if it merely referred to international practice, thus leaving the standard to be developed elsewhere. The concern was also expressed that the reference to international practice was vague and that the use of the word "prevailing" might suggest that the international standard was a changing one. Moreover, support was expressed for variant B on the ground that it was consistent with an analogous provision in URDG article 9, that variant B rather than variant A was the more objective alternative, that it took better account of the needs of the users of the uniform law and that the drafting style was preferable.

34. A view was expressed that the provision found in both variants to the effect that the demand was to be judged only for its apparent or facial conformity with the terms of the guaranty letter should be replaced by a rule requiring the guarantor to ascertain to the greatest extent possible that the demand conformed in fact to the terms of the guaranty letter. That view did not receive support, as the Working Group considered it essential, in view of the independent nature of the undertaking, to limit the scope of the examination to apparent or facial compliance.

35. The Working Group next considered proposals aimed at capturing the advantages of both variants of paragraph (1). Those proposals ranged from a suggestion that the uniform law should not express a preference for either approach to a proposal that the two variants be combined. Furthermore, a note of caution was struck that the uniform law should avoid adding to the existing number of different formulations concerning the standard of care of the guarantor. These already included the standards found in UCP article 15, URDG article 9 and the draft revision of the UCP.

36. One suggested approach for combining variants A and B was to add words such as "having due regard to prevailing international standards" to the language in variant B concerning professional diligence. Such a combination, it was said, would usefully promote internationalization of standards applicable to examination of demands for payment. The concern was raised that the combined approach might be confusing, although the extent to which confusion could ensue was disputed on the ground that the reference to the internationally recognized standard would, in effect, be to internationally recognized contractual rules such as UCP. It was also cautioned that any combination should retain the emphasis on facial conformity of the demand for payment with the terms of the guaranty letter.

37. The discussion of the standards set forth in variants A and B revealed a close link between the provisions of article 16, dealing with examination of the demand for payment, and article 13, dealing with the liability of the guarantor. However, in addition to this issue shared with article 13, article 16 also addressed the standard to be used to determine whether a demand and any accompanying documents were in conformity with the terms of the guaranty letter. Accordingly, it was proposed that the provision of paragraph (1) that established the standard of care to be followed in examining the demand might be incorporated into article 13 or should at least be aligned with that article. With such a division, paragraph (1) in its variant B would focus on the standard to be used in determining whether the demand and any accompanying documents were in conformity with the terms of the guaranty letter.

38. A view was expressed that the proposed division was complicated because article 13 was said to focus on the relationship between the principal and the guarantor, and between the counter-guarantor and the guarantor, while article 16 dealt with issues related to the relationship between the guarantor and the beneficiary. On this point it was observed that it might be useful to examine further the extent to which the uniform law should or should not encompass the principal-guarantor relationship. A further matter was whether the standards in question should be mandatory, or subject to contractual variation.

39. The Working Group, after deliberation, decided to reconsider the matter at a future session on the basis of draft provisions to be prepared by the Secretariat along the lines of the suggested division.

Paragraph (2)

40. The Working Group expressed its agreement with the provision in the *chapeau* recognizing the right of contractual modification of the time-limit set forth in paragraph (2) for the examination of the demand for payment. A suggestion was made, however, to use the words "unless otherwise stipulated in the guaranty letter", so as to make it clear that this provision only dealt with an agreement between the guarantor and the beneficiary. The Working Group then considered three variants as to the length of time to be allowed for the examination of the demand for payment.

41. Some support was expressed for variant X, which provided the guarantor with "reasonable time", on the ground that the flexibility inherent therein would permit adequate recognition of the circumstances in each individual case, since cases might, if complex, require more than the time provided for in variant Y. Variant X was said to be preferable also because it would be difficult to fix a general maximum limit of the type envisaged in variant Z. However, objections were raised to variant X, in particular that the provision would, due to its imprecision, not deliver the desired degree of certainty. A measure of support was found for variant Y also on the ground that the four-day period envisaged therein accurately reflected typical banking practice. However, it was observed that it was not bank practice to allow examinations of demands for payment to drag on, and that the need for an absolute time-limit was questionable.

42. Support was also expressed in favour of the approach taken in variant Z, which attempted to combine the flexibility offered by the "reasonable time" provision in variant X with the certainty offered by the fixed time-limit in variant Y.

43. The Working Group, after deliberation, decided to retain variant Z, without thereby foreclosing reconsideration at a future session.

Article 17. Payment or rejection of demand

44. The text of draft article 17 as considered by the Working Group was as follows:

"(1) The guarantor shall make payment as demanded by the beneficiary, unless:

(a) the guaranty letter is non-existent, invalid or unenforceable; or

(b) the demand does not meet the requirements referred to in article 14 [; or

Variant A: (c) the demand is [manifestly] [clearly and obviously] improper according to article 19].

"(2) *Variant B:* [The guarantor may make payment despite an assertion by the principal that the demand is improper according to article 19, provided that the guarantor acts in good faith. However, if]

[If] the principal asserts that the demand is improper according to article 19 and the guarantor decides not to reject the demand, the guarantor shall promptly inform the principal about its decision [and, if so requested by the principal, defer payment for [three] business days].

"(3) If the guarantor decides to reject the demand on any ground referred to in paragraph (1) *(a)* and *(b)* of this article, it shall promptly give notice thereof, indicating, where appropriate, the reasons for the decision, to the beneficiary by teletransmission or, if that is not possible, by other expeditious means.

"[(4) If the guarantor fails to comply with the provisions of article 16 or paragraph (3) of this article, it shall be precluded from claiming that the demand is not in conformity with the terms of the guaranty letter.]"

Paragraph (1) (a) *and* (b)

45. As regards subparagraph *(a)*, concerns were expressed that the reference to legal concepts such as non-existence, invalidity or unenforceability might result in uncertainty or disparities as to the rules applicable in different jurisdictions. It was stated that certain instances of "non-existence" of a guaranty letter recognized in particular jurisdictions might be regarded in other jurisdictions as instances of absolute nullity or invalidity of the guaranty letter. Examples of uncertainty concerning "non-enforceability" included boycott and the case where the text of the guaranty letter stipulated payment in a non-convertible currency but did not establish a conversion mechanism for payment in another currency. It was thus suggested that the uniform law, rather than focusing on concepts of legal doctrine, should list the factual situations that could justify the rejection of a demand for payment.

46. The prevailing view was, however, that no attempt should be made to list within the uniform law all factual situations where the guarantor would be justified to refuse payment since it would be difficult, if not impossible, to establish an exhaustive list. Furthermore, any attempt to list the cases where the guarantor would be obliged or entitled not to pay might raise difficulties as regards the determination of the applicable law since the conflict-of-laws rules would be different depending upon whether the nullity of the undertaking resulted from violation of legal requirements concerning the personal capacity of the parties, the form in which the undertaking was agreed upon or the substance of the undertaking.

47. Reference was made to circumstances generally described as *force majeure* where the guarantor would be faced with an absolute impossibility to make payment. A suggestion was made that the uniform law should address those situations. In that connection, a view was expressed that the uniform law might indicate more clearly, in the case of a temporary obstacle, whether the obligation of the guarantor would be only temporarily suspended until such time as the impediment disappeared or whether the obstacle should be viewed as terminating the obligation of the guarantor.

48. In support of the current wording of subparagraph *(a)*, it was explained that, while such concepts as "non-existence", "invalidity" and "unenforceability" might be interpreted differently in different jurisdictions, such differences would not affect the application of the provision in so far as the undertaking was vitiated by, and the non-payment based on, circumstances to which at least one of those three concepts was applicable. However, it was stated in reply that the provision was inappropriate where the events or circumstances that vitiated the undertaking fell outside the scope of paragraph (1)*(a)* in some jurisdictions but were retained within that scope in others.

49. The view was expressed that the obligations of the guarantor addressed in article 17 were a "mirror image" of the obligations of the beneficiary stated in article 14, which established as a general rule that a demand for payment presented by the beneficiary had to conform with the terms of the guaranty letter. It was suggested that article 17 should be redrafted along the same lines to state in general terms that the guarantor was obliged to pay against a demand in conformity with the terms of the undertaking. It was stated that a reference to the obligation to pay pursuant to and in accordance with the terms of the undertaking would encompass not only subparagraph *(b)* but also the cases currently addressed in subparagraph *(a)*, as questions relating to the issuance, the existence, the validity and the enforceability of the undertaking would be raised in connection with the terms of the undertaking.

50. While it was observed that the suggested formulation could not easily embrace a reference to article 19 on improper demand, the Working Group, after deliberation, adopted the suggested structure as outlined in paragraph 49 and requested the Secretariat to prepare a revised draft of the paragraph. It was noted that the new structure left open the question as to whether the guarantor, in the exceptional circumstances where it would not be obliged to pay, would have an obligation or a mere authorization to refuse payment. It was generally felt that question should be addressed in the context of the discussion on variants A and B.

Variants A and B

51. As regards the substance of the tests contained in variants A and B, it was stated that the difference was minimal since it was difficult to conceive of circumstances in which a demand was manifestly or clearly and obviously improper but the guarantor nevertheless paid in good faith. However, variants A and B were seen as differing in their scope. Variant A stated as a general principle that the guarantor should not pay in case of a manifest fraud, while variant B addressed the exceptional situation where the guarantor was instructed by the principal not to pay, based on the assertion that the demand was improper.

52. Divergent views were expressed as to whether the guarantor, faced with a manifestly improper demand, should be obliged to refuse payment or whether he should have discretion to pay or not to pay. It was noted that this question had repercussions on the relationship between the guarantor and the principal, in particular as regards the right of the guarantor to obtain reimbursement from the principal and on the principal's right to apply for injunctive relief as suggested in article 21.

53. In favour of granting the guarantor discretion, it was stated that a fundamental principle of the uniform law was that payment by the guarantor should be the norm and non-payment a rare exception. It was suggested that purpose of the uniform law might be defeated if the guarantor was under an obligation not to pay since that would encourage the guarantor not to pay. It was also stated that the guarantor should be allowed to rely on the facial conformity of the documents, unless the principal obtained a court decision enjoining the guarantor from paying under the guaranty letter. The prevailing view, however, was that the guarantor should be obliged to refuse payment in blatant fraud or abuse situations that could be perceived by anyone.

54. While some doubts were expressed as to whether the test provided in variant A would be applied uniformly in all jurisdictions, it was noted that the concept of bad faith might lend itself to even greater divergence in interpretation. It was agreed that the common core of the tests contained in variants A and B consisted of the fact that the improper nature of the demand was known to the guarantor or was beyond any reasonable doubt, without any investigation on the part of the guarantor.

55. After deliberation, the Working Group was agreed that the uniform law should contain a rule to the effect that, where the guarantor knew or ought to have known that the demand for payment was improper, the guarantor would have an obligation not to pay. In all other cases, i.e., not only in case of facial conformity of the demand and documents but also in case of a doubt, irrespective of whether the guarantor was faced with an allegation that the demand was improper, the general rule would apply and the guarantor had to pay. The Working Group decided to reconsider the matter at a future session on the basis of a revised provision to be prepared by the Secretariat in the light of the above deliberations and decisions.

Last sentence of paragraph (2)

56. The provision deferring payment for a very limited number of days was supported on the ground that it attempted to strike a balance between the need for prompt payment of the independent undertaking and the interest of the principal to submit documentary evidence to the guarantor or, if feasible within that short period, to seek injunctory relief from a court.

57. However, the prevailing view was that the provision was likely to encourage systematic deferral of payment and that the sentence should be deleted. It was also stated that there should be no obligation imposed on the guarantor to inform the principal if it is decided not to reject the demand. Another argument for the deletion of the provision was that it was contrary to the practice of stand-by letters of credit which did not allow any time for possible negotiation.

Paragraph (3)

58. A concern was raised that the words "where appropriate" would give the guarantor the option not to inform the beneficiary of the reasons why it had decided not to pay under the guaranty letter. It was stated that paragraph (3) might seem inconsistent with the preclusion rule contained in paragraph (4) for the cases where the guarantor had failed to comply with the provisions of article 16 and paragraph (3).

59. Accordingly, one view was that, following the approach of article 10*(b)* URDG, the requirement of giving notice to the beneficiary should not embrace the giving of reasons. However, the prevailing view was that the guarantor should give reasons in all cases. It was suggested that the uniform law should provide some guidance in that respect, for example by requiring, in the case of non-conformity, a statement as to the specific discrepancy, and in the case of an improper demand or of a fundamental defect, a general statement to that effect.

60. The Working Group requested the Secretariat to prepare a revised version of paragraph (3) in the light of the above deliberations.

Paragraph (4)

61. Divergent views were expressed as regards the rule of preclusion contained in paragraph (4). One view was that the preclusion rule was too harsh and that the uniform law should remain silent on that point. That would still allow parties to agree on the preclusion rule contained in the Uniform Customs and Practice for Documentary Credits (UCP). It was stated in support of that view that the idea of finality underlying the preclusion rule was of greater importance in the context of payments under commercial letters of credit than under guaranty letters.

62. Another view was that the rule of preclusion should be retained since finality was essential for guaranty letters as well, at least for stand-by letters of credit. It was stated in support of that view that it was not sufficient to leave the matter to the UCP since preclusion was an important rule of traffic that had to be made known to all parties potentially involved in the transaction.

63. After discussion, the Working Group decided that the text of paragraph (4), possibly to be refined by the Secretariat, would remain between square brackets.

Article 18. Request for extension or payment

64. The text of draft article 18 as considered by the Working Group was as follows:

"If the beneficiary [demands in the alternative payment or] [combines a demand for payment with a request for] an extension of the validity period of the guaranty letter, the guarantor shall comply with the following rules, unless otherwise agreed by the parties:

(a) The guarantor shall give prompt notice of the alternative demand for extension or payment to the principal [directly or through an instructing party];

(b) The guarantor may not extend the validity period without the consent of the principal; however, even if the principal consents to the extension, the guarantor is not obliged to extend the validity period, unless so required by an agreement with the principal;

(c) The guarantor shall examine the demand for payment in accordance with article 16 and decide whether to pay or to reject that demand; if the guarantor decides not to reject the demand, it [shall] [may] defer payment until [ten] business days have elapsed after [giving notice to the principal] [receiving the alternative demand from the beneficiary] and then make payment, unless the guarantor extends the validity period."

65. As had been the case when the Working Group first discussed "extend-or-pay" requests at the fifteenth session (A/CN.9/345, paras. 73-77), opinions differed as to whether the uniform law should contain specific provisions on such requests. Doubts were expressed as to the need for article 18 on the ground that the circumstances addressed therein were already adequately covered by other provisions in the uniform law. In particular, it was suggested that a request to extend or to pay could properly be classified as a request for an amendment of the guaranty letter falling under article 8. According to this view, if the uniform law contained an adequate amendment procedure providing for notice and consent of the parties, the need for article 18 would diminish. To the demand-for-payment component of an extend-or-pay request, article 14 might be applied. The necessity of including article 18 was also questioned on the ground that the need for the procedures envisaged in subparagraphs *(a)* through *(c)* could be seen as sufficiently covered by the general standards of conduct imposed by the uniform law.

66. The primary factors cited in favour of retaining article 18 included uncertainty surrounding extend-or-pay requests and the guarantor's response thereto, along with the frequency with which such requests occurred. It was stated that, accordingly, the uniform law would have, either in article 18 or in some other provision, to address such requests. It was said that extend-or-pay requests could not be treated as simple requests for amendment and that specific rules were desirable to regulate the legal effect and procedures of those types of requests. The rules would help to address the problems that arose when, after an extend-or-

pay request was refused, the guaranty letter expired without payment having been made. Retention of article 18 was also supported on the ground that extend-or-pay requests, rather than being viewed in all cases with apprehension as a practice to be discouraged by the uniform law, might be regarded as potentially useful steps towards negotiated settlement of disputes between the principal and the beneficiary. In that respect, the provision of subparagraph *(c)* to defer payment for a certain number of days was regarded as a useful device.

67. A number of additional observations were made, to be considered were article 18 to be retained. One such suggestion was that the scope of the article should be limited to bank guarantees, thus excluding stand-by letters of credit, in particular because the extend-or-pay procedure was incompatible with financial stand-by letters of credit, since the expectation of the parties was that the bank would pay immediately upon demand. In response, it was stated that the extend-or-pay situation was one which arose not only in relation to bank guarantees, but might also arise under stand-by letters of credit, and that therefore no limitation on the scope of article 18 would be warranted.

68. The Working Group noted that it was not the intent of article 18 to confer a right on the beneficiary to obtain an extension of the validity period of the guaranty letter merely by virtue of making an extend-or-pay request. Another area of potential clarification was the effect on the counter-guaranty letter of an extend-or-pay request under the indirect guaranty letter. It was also suggested that additional clarity might be achieved by modifying the title of article 18 to read along the lines of "request for extension or demand for payment", as well as by placing it in closer proximity to or incorporating it in article 8 or 14.

69. The Working Group then turned to a discussion of whether an extend-or-pay request should be regarded as containing a firm demand for payment, such that, were the extension to be denied, the beneficiary would not have to make any additional demand for payment in order to receive payment. It was noted that this was the approach underlying article 18. Support was expressed for that approach. A differing view was that extend-or-pay requests should not be regarded as demands for payment as this would run counter to the notion of strict compliance of the demand for payment with the terms of the guaranty letter. It was pointed out that such an approach had been taken by a number of jurisdictions. Mention was also made of the distinction between those cases in which the contingency secured by the guaranty letter had occurred and those cases in which the contingency had not occurred. In the latter type of case, for example when an extend-or-pay request was made merely because the duration of the underlying contract was being extended, the demand for payment might be considered abusive.

70. After deliberation, the Working Group decided, in order to facilitate further consideration, to request the Secretariat to present it with two possible approaches. Under the first approach, a request to extend or to pay would not be regarded as a proper demand for payment. It was observed that this approach, while possibly leading to the elimination of extend-or-pay requests in their present form, would not prevent beneficiaries from achieving the same result by first requesting extension of the guaranty letter prior to a specified deadline, and then, if the validity period was not extended by the deadline, filing a demand for payment. Under the second approach to be presented in the next draft, the demand for payment portion of an extend-or-pay request would not be vitiated.

71. In reviewing article 18, the Working Group had occasion to engage in a discussion of the manner in which the uniform law might establish a unified set of rules governing guarantees and stand-by letters of credit while at the same time taking account of various peculiarities of those types of instruments. It was noted that, with respect to several draft articles, questions had been raised as to the feasibility of applying the same rule both to bank guarantees and to stand-by letters of credit. Such questions had arisen not only with respect to the extend-or-pay procedure in article 18, but also regarding requirements elsewhere in the uniform law, for example, the notice of a demand for payment to be given by the guarantor to the principal, the treatment of non-documentary conditions, the question of limiting transfers and the rule of preclusion. In each of those cases, it was suggested that the distinction previously made between stand-by practice and guarantee practice did not adequately account for differences among those who utilized guarantees. Rather than utilize terms such as "hard" or "soft" which had pejorative connotations, it was asked whether it might not be better to think of undertakings which were directed to immediate payment by a neutral paymaster based on a purely documentary demand as opposed to instruments which were intended to assure a solvent paymaster after a process of negotiation between the parties. As to the former, the beneficiary would hold the funds during any negotiation between the parties to the underlying transaction, whereas in the latter, the paymaster would withhold payment. The two approaches contained many similarities as well as significant differences. It was suggested that evidently some guarantees fell within the former category and some within the latter, which explained the differences in position among those using guarantees with regard to the various issues such as notice to the applicant before payment and extend-or-pay requests. The distinction, it was suggested, was not between guarantees and stand-by letters of credit but between payment-oriented instruments, with stand-by letters of credit and some guarantees falling within the former category and other types of guarantees falling within the latter.

72. A view was expressed that, in view of the above, perhaps consideration might have to be given to excluding from the scope of the uniform law instruments that did not, with respect to both purpose and function, fall within the scope of the traditional bank guarantee. That approach, however, was objected to on the ground that instruments such as financial stand-by letters of credit represented a large volume of the undertakings intended to be covered by the uniform law. Furthermore, it was suggested that it would be inappropriate for the uniform law to distinguish instruments such as financial stand-by letters of credit from bank guarantees and to attempt to apply separate rules for each type of instrument. It was reported that bank guarantees were used, like financial stand-by letters of credit, in financial markets and were accepted by beneficiaries as

offering the required high degree of firmness in the undertaking. Accordingly, it was suggested that it might be more fruitful for the uniform law to take the necessary account of the different purposes that an undertaking covered by the uniform law could serve, as well as possible attendant differences in the certainty of the guarantor's undertaking. Under this approach, the uniform law would take account of the essential features both of undertakings used in financial markets and of undertakings whose purpose was to secure performance — irrespective of whether those financial or performance assurances took the form of bank guarantees or the form of stand-by letters of credit. The Working Group was urged at the same time not to overemphasize differences between financial and performance stand-bys, in view of the established classification of financial stand-bys as a species of stand-by letters of credit, which themselves were generally regulated under the umbrella of letters of credit.

73. It was agreed that the effort would continue to be made to formulate rules of general application, and that in that process account should be taken of the differing purposes and features of the various instruments covered by the uniform law. It was also recalled that one of the guiding notions of the uniform law was that of party autonomy to agree on the terms of the guaranty letter. That autonomy, the extent of which remained to be determined in respect of each article, was an avenue through which differences in practice could be accommodated, in particular, as regards the choice of particular types of undertakings and of particular payment conditions.

Article 19. Improper demand

74. The text of draft article 19 as considered by the Working Group was as follows:

"*Variant A:* A demand for payment is improper if:

(a) any certification by the beneficiary or any required document accompanying the demand is [untrue] [essentially incorrect] or forged; or

(b) the demand falls clearly outside the purpose for which the guaranty letter was given or otherwise lacks any plausible basis.

"*Variant B:* (1) [Same as variant A]

(2) A demand has no plausible basis, for example, where:

(a) in the case of a guaranty letter that [supports] [backs up] the financial obligation of a third party, the principal amount is not due;

(b) in the case of a tender guaranty letter,

(i) the contract has not yet been awarded; or

(ii) the contract has been awarded to a tenderer other than the principal; or

(iii) the contract has been awarded to the principal and the principal has [accepted] [signed] the contract and secured any required performance guaranty letter;

(c) in the case of a repayment guaranty letter, no advance payment has been made;

(d) in the case of a performance guaranty letter,

(i) a competent court or arbitral tribunal has determined [in a final decision] that the obligations of the principal towards the beneficiary, the performance of which the guaranty letter was intended to secure, do not exist or are unenforceable on the ground that the underlying transaction [between the principal and the beneficiary] is non-existent, violates public policy or is otherwise invalid;

(ii) the principal has completely [to the satisfaction of the beneficiary] fulfilled its obligations the performance of which the guaranty letter was intended to secure;

(iii) the beneficiary has prevented the principal from fulfilling its obligations, the performance of which the guaranty letter was intended to secure, by a [wilful] [serious] breach of its own [fundamental] obligations of the underlying transaction;

[(iv) the amount demanded is [grossly disproportionate to] [at least five times higher than] the damage suffered due to the failure of the principal to fulfil its obligations;]

(e) in the case of a counter-guaranty letter, the beneficiary of the counter-guaranty letter has paid [or intends to pay] to its beneficiary under its guaranty letter, the reimbursement for which constitutes the purpose of the counter-guaranty letter, upon a demand that is [evidently] affected by one of the infirmities referred to in paragraph (1) of article 17, provided that the beneficiary of the counter-guaranty letter

Variant X: acted in collusion with its beneficiary.

Variant Y: [acted in bad faith] [failed to exercise professional care].

Variant Z: is by virtue of the counter-guaranty letter or any reimbursement agreement with the counter-guarantor or by virtue of law [entitled] [under a duty] to reject the demand because of such infirmity].

"*Variant C:* (1) A demand for payment is improper if making it constitutes fraud or an abuse of rights.

(2) The making of a demand constitutes fraud where:

(i) the beneficiary [has no belief that the amount demanded is due] [knows or cannot be unaware of the fact that the amount demanded is not due] on the basis asserted in the demand and any supporting statements and documents; or

(ii) any supporting statement or document is [untrue] [essentially incorrect]; or

(iii) any supporting document is forged.

(3) The making of a demand constitutes an abuse if:

Variant X: the beneficiary exercises its right for a purpose other than that for which the guaranty letter was given.

Variant Y: the contingency against the consequences of which the guaranty letter was designed to indemnify the beneficiary has undoubtedly not materialized or has clearly been brought about by a fundamental breach of the underlying transaction wilfully committed by the beneficiary.

"*Variant D:* The guarantor [may] [shall] reject a demand as improper if, having due regard to the independent [and essentially documentary] character of its undertaking, the guarantor concludes that the demand is made in bad faith or fraudulently, including fraud or forgery relating to the documents or fraud in the underlying transaction, or that the making of the demand constitutes an abuse of rights by the beneficiary, provided that the facts constituting the basis of that conclusion are clearly and convincingly established without investigation by the guarantor."

75. Four variants of article 19 were presented to the Working Group, reflecting various proposals that had been made at the fifteenth session (see A/CN.9/345, para. 51). Variants A through C contained definitions of the term "improper demand". Variant D, rather than setting forth a definition of that term, gave a general guideline.

76. In the review of the variants, a number of factors were identified as relevant to defining or describing an "improper demand". Prominent among these was the distinction that sometimes had to be drawn between fraud in the underlying transaction and fraud in the documents presented to the guarantor in order to obtain payment. In this regard, it was recognized that, in cases of fraud in the documents, a degree of tension existed with the principle of examination of the demand on the basis of facial compliance and, in cases of fraud in the transaction, with the principle of independence of the undertaking. It was the general view of the Working Group that the circumstances in the underlying transaction had to be given some opportunity to affect the guaranty transaction so that in a limited number of cases the demand for payment could be treated as improper. Thus the notion of "improper demand" would be limited to cases where the misconduct could be described by terms such as "manifest" or "beyond doubt" and "egregious". It was also suggested that one of the ways of focusing article 19 would be to indicate that demands for payment that fell clearly outside the purposes of the guaranty letter were improper.

77. An important related factor was the difference in terminology used by legal systems to refer to improper demands. Notably, in some legal systems, the use of the term "fraud" was confined to cases of forgery of documents presented to the guarantor, while demands for payment related to fraud in the underlying transaction fell under the notion of "abuse of rights". In other legal systems, both aspects fell under the umbrella notion of fraud. While some consideration was given to elaborating definitions of terms such as "fraud" and "abuse", the general preference of the Working Group was to attempt to bridge those differences in terminology by avoiding the use of such terms and to aim instead at a commonly understood description of the improper demand.

78. Also said to be relevant were differences among legal systems as to procedural and substantive rules under which guarantors operated. For example, in some countries, efforts to prevent payment of an allegedly improper demand typically took the form of applications to the court for preliminary injunctive measures, while in certain other jurisdictions such preliminary measures were not available for cases of this type. It was also noted that the circumstances in each case of improper demand differed, and that this affected the ease with and the extent to which the guarantor could become cognizant of the irregularity in the demand for payment. The Working Group noted that in a usual case the guarantor would not be kept informed as to the implementation of the underlying transaction.

79. An observation of a more general type was that the working assumption in the uniform law should be that the parties generally act in good faith. A concern was also raised that, in formulating the uniform law, adequate account should be taken of the beneficiary's perspective, in particular since the guaranty letter was the product of the negotiated agreement of commercial parties and was often the only source of monetary compensation for a default in the underlying transaction. The Working Group was urged to search for a formulation of article 19 that was as objective as possible, avoiding terms such as "concludes", which might suggest not only that the process was subjective in character, but also that the guarantor was to conduct an investigation of the fraud. It was also suggested that the formulation of variant D might be simplified by deletion of the words "demand is made in bad faith or fraudulently, including fraud or forgery relating to the documents or fraud in the underlying transaction, or that the".

80. As to the specific evaluation and comparison of the variant versions of article 19, as noted above, the Working Group generally preferred that article 19 should avoid attempting to define terms such as "fraud" that might be the subject of traditionally divergent interpretations. Accordingly, the Working Group preferred the approach taken in variant D over the definitional approach in the other variants. Variants A and B drew criticism on the ground that the significance of the words "plausible basis" found therein was not clear and seemed overly broad. It was suggested that clear language was needed in order to indicate whether the guarantor was to judge only whether there was any basis at all for the demand for payment, or whether the guarantor was to evaluate the sufficiency of any basis that did exist for the demand for payment.

81. The approach used in variant B, that of providing an illustrative list of cases of improper demand, was not regarded as appropriate for the uniform law. Concerns included the possibility that the list of examples would not be comprehensive and might not take adequate account of the circumstances of individual cases, and that the use of such a list was incompatible with the legislative drafting tradition in a number of States. The suggestion was made that a list of examples such as that in variant B might usefully be included in a commentary.

82. The Working Group also considered possible modifications and refinements of variant D beyond the avoidance of terms such as "fraud" or "abuse". In doing so, it sur-

veyed the various cases of improper demand specified or referred to in the other variants in order to determine which of these situations should be covered by the broad rule along the lines of variant D. In connection with paragraph (1)*(a)* in variant A, the Working Group considered what the notion of fraud in the documents should encompass. It was agreed that the case of forged documents should be included. The case of false or inaccurate documents seemed less clear. The Working Group noted that in some jurisdictions the notion of forgery encompassed false or inaccurate documents, while in others it did not. Enunciating general rules for such cases was complicated by the fact that the falsity or inaccuracy might not always be tantamount to the fraud to be sanctioned by the uniform law. It was suggested that for such cases it might be helpful to provide in article 19 that, for a false or inaccurate document to render the demand improper, the beneficiary must have intended to deceive.

83. In this regard, the Working Group noted that the courts of some jurisdictions have held that in such cases the guarantor was obligated to pay if the beneficiary was unaware of the tampering with the documents. Such holdings raised the broader question of whether the uniform law should generally limit itself to cases in which the beneficiary was involved in or otherwise aware of the fraud. There was general agreement that demands for payment in such cases should be deemed improper. No final conclusions were reached, however, as to whether the awareness of involvement of the beneficiary would be a prerequisite for action pursuant to article 19. The Working Group did agree, though, that, as a whole, the situations addressed by variant A should fall within the purview of article 19.

84. The view was expressed that the situation envisaged in paragraph (2)*(a)* of variant B would not in all cases constitute an improper demand. It was pointed out that it indeed might be the purpose of a guaranty letter to provide for payment even before the sum in the underlying transaction became due (e.g., when the principal became insolvent). It was suggested that the problem might be solved by linking such a ground for impropriety to the terms and conditions of the guaranty letter.

85. While support was expressed for the general thrust of paragraph (2)*(d)*(i) of variant B, the Working Group was reminded that it might be the purpose of a guaranty letter to cover the risk of the occurrence of the type of situation referred to in that paragraph (invalidity, unenforceability of the underlying transaction). It was pointed out that payment under such circumstances has withstood judicial scrutiny in a number of jurisdictions.

86. Some hesitation was expressed with regard to the type of situation referred to in paragraph (2)*(d)*(iii), which concerned prevention by the beneficiary of performance of obligations in the underlying transaction that were secured by the guaranty letter. It was suggested that the assessment of that type of situation tended to be particularly subjective and linked to the circumstances of the particular case and should therefore not be covered by article 19.

87. Reservations were expressed as to the coverage of the situation addressed in paragraph (2)*(d)*(iv) of variant B, which referred to disproportionality between the damage suffered and the amount claimed under the guaranty letter. One concern was that assessment of the demand in such terms would involve a value judgement by the guarantor. Another concern was that the integrity of the undertaking would be undermined if payment could be refused on grounds other than complete lack of any basis for the demand. It was pointed out that the risk of disproportionality could be dealt with by the principal by seeing to it that the guaranty letter contained a mechanism for reduction of the guaranty amount and called for the presentation of documents certifying the amount due.

88. Differing views were expressed as to whether rejection of an improper payment demand should, under article 17 in tandem with article 19, be mandatory or discretionary. Some support was expressed for a discretionary approach, in particular because of a concern that a mandatory approach would accentuate uncertainty as to whether the law governing the underlying transaction or the law governing the guaranty letter would be used for resolving the concepts of fraud and abuse of rights contained in variant D. The prevailing view, in line with the decision in respect of article 17, was that rejection should be mandatory for the kind of cases of manifest fraud or abuse being contemplated by article 19. Such an approach was said to have the benefit also of avoiding uncertainty that would result were the principal's obligation to reimburse the guarantor to be linked to the proper exercise of discretion in such cases by the guarantor.

89. The Working Group agreed that the case of the counter-guaranty letter should be encompassed in article 19. It was noted that fraud in the counter-guaranty context may centre on the counter-guaranty itself, for example, when a demand for payment under the counter-guaranty letter was made without there having been a demand under the indirect guaranty letter. In other cases, payment under the indirect guaranty letter took place, but was tainted with fraud of the ultimate beneficiary.

90. As to the formulation concerning counter-guaranty letters found in paragraph (2)*(e)* of variant B, it was suggested that the text in that paragraph should be reworded in order to take better account of differences in national law concerning the room to manoeuvre allowed to the guarantor confronted with an improper demand for payment. The Working Group reviewed the three variants set forth in paragraph (2)*(e)* concerning the circumstances in which article 19 would apply to the counter-guaranty context. variants X and Y raised some hesitation, in particular because they contained terms of uncertain meaning, including "collusion", "bad faith" and "professional care". Regarding variant Y, a view was expressed that the reference to failure to exercise professional care might suggest that a guarantor had to engage in more than an examination of the demand for payment. The remaining approach, in variant Z, which avoided the use of uncertain terms, was considered preferable. It was noted that the word "not" had inadvertently been left out before the words "[entitle] [under a duty]".

91. After deliberation, the Working Group requested the Secretariat to revise article 19 based on the preference that

had been expressed for the approach in variant D. As had been discussed, the provision would concern cases in which the impropriety of the demand was clear and unambiguous or beyond doubt to the guarantor. It would also avoid defining terms such as "fraud" and "abuse of right", focusing rather on a description of the improper demand and taking into account various types of instruments and their different possible purposes. The provision further would treat counter-guaranty letters, drawing some of its features from paragraph (2)*(e)* of variant B, including the substance of variant Z in that paragraph.

Article 20. Set-off

92. The text of draft article 20 as considered by the Working Group was as follows:

"*Variant A:* Unless otherwise [expressly] agreed by the parties, the guarantor may not avail itself of a set-off with any claim against the demand for payment under the guaranty letter.

"*Variant B:* Unless otherwise agreed by the parties and subject to the provisions of the law of insolvency, the guarantor may discharge its payment obligation under the guaranty letter by means of a set-off with any claim not assigned to it by the principal, provided that the claim of the guarantor is [liquidated and] certain or undisputed.

"*Variant C:* Unless otherwise expressly agreed by the parties, the guarantor is precluded from discharging its payment obligation under the guaranty letter by means of a set-off with any claim, except where:

(a) the beneficiary is insolvent; or

(b) the guaranty letter is designed to secure the fulfilment of a financial or payment obligation of the principal or the guarantor and that obligation could have been discharged by means of a set-off with the claim of the guarantor."

93. As had been the case at the fifteenth session, divergent views were expressed as to whether the uniform law should include a provision on set-off. In support of deletion of article 20, reference was made to divergencies among national laws as to the extent to which set-off was permitted. For example, in some countries set-off was only permitted in cases of insolvency. In the face of diversity, a rule in the uniform law would be certain to contradict the jurisprudence and laws of a number of countries. Other factors said to favour deletion of article 20 included the relatively low frequency with which cases of set-off arose in the guaranty context and the fact that set-off might be regarded merely as a method of execution of payment under the guaranty letter.

94. The prevailing view was in favour of retaining a provision on set-off in the uniform law. It was stated that a clear solution of the issue of set-off was one that was of importance to the integrity of the guaranty letter. Set-off was a commonly used extrajudicial remedy that should not fall outside the uniform law. Whereas inclusion of a rule of common understanding would foster harmonization and uniformity, the absence of such a rule in the uniform law might contribute to uncertainty and inconsistency. It was also felt that such a rule might usefully clarify matters not covered in the laws of all States, for example, whether the guarantor was permitted to set off a claim assigned to the guarantor by the principal.

95. As to the content of the rule on set-off, the view was expressed that variant A, which prohibited set-off, should be chosen, though modified to permit set-off in cases of insolvency of the beneficiary. A rationale behind a prohibition of set-off was that the guaranty letter was essentially a substitute for placing money in escrow and that, therefore, payment needed to be carried out when it fell due. Reference was also made to judicial decisions in the analogous area of documentary credits prohibiting set-off and to the uncertainty that might arise for holders of security interests in the guaranty amount, were set-off to be envisaged.

96. The prevailing view, however, was that such an attempt to prohibit set-off would not be reflective of practice and would diminish the acceptability of the uniform law. According to that view, set-off was not incompatible with the purposes of the guaranty letter and therefore the permissive approach in variant B was preferable. It was also suggested that an inability to set off would lead to difficulties related to the tracing of assets and might increase the incidence of double payment. The Working Group also expressed its support for the prohibition in variant B of the set-off of claims assigned by the principal to the guarantor. It was felt that such set-off would run counter to the purpose of the guaranty letter and to the principle of independence. A related question concerned the manner in which the notion of claims of the principal would be defined, for example, whether it would include claims of a company in which the principal had an interest.

97. Divergent views were expressed as to certain aspects of variant B. Some support was expressed for the reference at the end of variant B to the liquid, certain or undisputed nature of claims that might be set off. Deletion of that language was widely urged on the ground that such detailed aspects of set-off were treated in national law and it was not necessary to address them in the uniform law, thereby running the risk of conflict with national law.

98. It was reported that in the laws of some countries set-off was restricted to claims of the guarantor arising out of the same transaction as the beneficiary's claim. While there was some support for such a restriction in the uniform law, it was widely regarded as a matter to be left to the general law of set-off in each country. It was suggested that it might be useful to indicate that set-off had to be against a party that was claiming payment. Such a limitation would be necessary to cope with cases of assignment or transfer of the guaranty letter. Such a rule would prohibit a guarantor, for example, from setting off its claim involving the original beneficiary against a demand for payment made by a transferee.

99. After deliberation, the Working Group requested the Secretariat to revise article 20 in line with the preference that had been expressed for variant B.

Chapter V. Provisional court measures

Article 21. Preliminary injunction against guarantor

100. The text of draft article 21 as considered by the Working Group was as follows:

"(1) Where, on an application by the principal,

Variant A: strong prima facie evidence is produced to the satisfaction of a competent court

Variant B: clear and liquid proof is presented to a court of competent jurisdiction

Variant C: it is manifestly shown by documentary means, including [sworn witness statements] [affidavits]

that a demand made [or anticipated to be made] by the beneficiary constitutes an improper demand, the court may issue a preliminary order enjoining the guarantor from meeting the demand [or from debiting the account of the principal], provided that [the court is satisfied that] the refusal to issue such an order would cause the principal [serious harm] [irreparable loss] which would be [clearly] more substantial than the loss that might be suffered by the beneficiary as a result of the issuance of such an order.

"(2) Before deciding on the application of the principal, the court [may hear the guarantor] [shall provide the guarantor with an opportunity to be heard]. It may also [, if so permitted under its procedural law,] consider the advisability of hearing the beneficiary or of allowing the principal to seek injunctive relief against the beneficiary as co-defendant.

"(3) An order referred to in paragraph (1) of this article shall be issued for a specified period of effectiveness not exceeding [six] months. An extension of that period may be made dependent on the initiation by the principal of proceedings other than preliminary proceedings against the guarantor or the beneficiary.

"(4) The court may make the effect of an order referred to in paragraph (1) of this article subject to the furnishing by the principal of such security as the court deems appropriate."

General Remarks

101. The Working Group noted that article 21 and the two other articles in the present chapter were particularly preliminary in nature, meant to reflect various views that had been expressed at the fifteenth session and to facilitate further consideration by the Working Group as to whether and how the uniform law should treat provisional court measures, in particular the preliminary injunction.

102. As had been the case at the fifteenth session, various opinions were expressed on the question of preliminary injunctions. There was a degree of hesitation to incorporate article 21 and its companion provisions, in particular to the extent that they contained procedural rules that differed from State to State and that might better be left to local law. It was suggested that the acceptability of the uniform law would be adversely affected if it presented legislatures with the prospect of having to revamp established rules governing injunctions for one particular area of the law. It was also pointed out that for some States the injunctive relief envisaged in the draft articles would be foreign. In the light of the above, it was suggested that the articles in question might be deleted, or at least directed only at those States in which injunctions were a recognized measure.

103. In favour of retaining a provision on injunctions, it was stated that such a provision was an integral element of the provisions in the uniform law dealing with fraud and abuse. It was also suggested that it was not the intent of the draft articles to bring about drastic changes in current national procedures, although it was said to be precisely because of the diversity in national approaches that it would be salutary to include the provisions in question in the uniform law. To the extent that injunction procedures did not exist in some States, retention of provisions on injunctions was said to have the benefit of providing guidance to those States in formulating such provisions. Both with respect to such States, as well as to the problem of diversity of national approaches, inclusion of provisions on preliminary injunctions was said to be beneficial for international uniformity and for protection of the integrity of the guaranty letter. It was further noted that the discussion of article 21 was hampered somewhat by uncertainty as to whether the final form of the uniform law would be a convention or a model law.

Paragraph (1)

104. The Working Group considered three variants in paragraph (1) concerning the main requirement that the principal would have to meet in order to obtain an injunction. The first approach, variant A, which required the principal to present strong prima facie evidence, encountered criticism as being too loose. Variant B, which referred to clear and liquid proof, was considered to be a stricter standard and therefore received more support. Reservations were expressed, however, as to the use of the expression "clear and liquid proof", which might not be widely understood. Variant C, which referred to the manifest showing of the impropriety of the demand through documentary means, did receive some support, but was generally regarded as being too strict a standard and potentially harmful to the interests of justice. In particular, it might not be advisable, in court proceedings, to limit to documentary means the manner in which parties may prove impropriety. A question was also raised concerning the appropriateness of referring to affidavits, in view of the unfamiliarity with such instruments in some legal systems. A substantial degree of interest was shown in a proposal to combine variants B and C, so as to provide that the application of the principal must manifestly show that the demand was improper.

105. In the review of the variants in paragraph (1), various observations were made, including the following: that, in view in particular of the diversity of national legal regimes, the provisions in the uniform law on preliminary injunctions should be of a general, skeleton character, and that they should be flexible and avoid impinging on the access of parties to the courts; that it should be made abundantly clear that the preliminary injunction was to be available only in the strictly limited cases that fell under the category of "improper demand" enunciated in article 19 and that the link to article 19 might have to be made more

explicit than it was in the current draft; that the significance of the references to competent courts was not clear; and that the same standard of proof should be applied to both article 21 and to article 22.

106. The Working Group then considered whether article 21 should permit the principal to apply for a preliminary injunction prior to a demand having been made. Deletion of this possibility was urged on the ground that such anticipatory applications would broaden the scope of injunctive relief under the uniform law to an excessive degree. It was also pointed out that the willingness of courts to grant such anticipatory relief would vary from jurisdiction to jurisdiction. A differing view was that the typically short time between the demand and payment made it unrealistic not to permit anticipatory applications for injunctive relief while still hoping to preserve a meaningful remedy for the principal. It was said that this time pressure would be accentuated were the Working Group to finally decide under article 15 not to provide for notice to the principal of the demand for payment. The view was also expressed that the reference to the debiting of the principal's account as one of the acts that an injunction could block should be deleted. The concern behind that view was that, if the guarantor had paid in good faith, the court should not intervene to block the debiting of the principal's account.

107. Differing views were exchanged as to whether to retain the language at the end of paragraph (1) concerning the court's assessment of the relative harm that would be caused to the parties by a refusal to grant the injunctive relief. Concerns in favour of deletion were that the rule enunciated in article 21 might conflict with various approaches to such an assessment that existed in practice and that it was primarily the responsibility of the principal to assess the risks that were inherent in the use of guaranty letters. Proponents of retaining the provision said that it would have the desired effect of narrowing the availability of preliminary injunctions and that it would foster harmonization. It was also noted that the assessment by the court that an injunction should be granted could be balanced by requiring the principal to post a security.

108. The Working Group considered a number of possible ways of expanding the scope of article 21. The first was a proposal to expand the article to deal with provisional measures other than preliminary injunctions, for example, prejudgement seizure or attachment of assets. It was noted that the laws of some States, while not providing for preliminary injunctions, did authorize attachment. Doubts were expressed as to covering attachment, in particular because it was uncertain whether that device would or could be uniformly applied to intangibles such as the obligation to make payment under a guaranty letter or the right to claim payment. Another suggestion was that article 21 should contain a prohibition against the clause, sometimes included in counter-guaranties, requiring the counter-guarantor to pay even in the face of a court order prohibiting payment. Yet another proposal was that article 21 include a provision concerning the response of the guarantor to an application for a preliminary injunction. It was noted that the practice varied from State to State as to the extent to which the guarantor became involved in the defence against an application for a preliminary injunction.

109. Divergent views were expressed as to whether the uniform law should cover injunctions not based on improper demand but on other objections to payment such as non-existence, invalidity or unenforceability of the guaranty letter. One view was that article 21 should be broadened so as to encompass such objections and to subject applications for injunctions to the same requirements, in particular as regards the standard of proof. Another view was that an injunction should be available as an extraordinary measure only in the extraordinary case of an improper demand and that it would be especially disruptive if an injunction were allowed on the ground of non-conformity of documents. Yet another view was that the uniform law should deal only with injunctions based on improper demand and leave the question of the availability of injunctions based on other objections to payment to other provisions of national procedural law. The Working Group, after deliberation, requested the Secretariat to prepare draft provisions reflecting those three views for reconsideration at a future session.

Paragraph (2)

110. The Working Group exchanged views on whether the application for a preliminary injunction should be dealt with in *ex parte* proceedings, or whether the guarantor, and perhaps the beneficiary, should be given an opportunity to be heard. One view was that it was imperative that the opportunity to be heard be given to both sides and that the matter should not be left discretionary. Another view was that, due to the time constraints involved, it would not be realistic to impose an across-the-board requirement that the guarantor, and perhaps the beneficiary, should be given a hearing. It was suggested that the circumstances of each individual case should be permitted to determine the nature of the proceeding. Another suggestion was to accommodate the practice of issuing temporary restraining orders in *ex parte* proceedings.

111. There was a mixture of views also with respect to including a reference to injunctive action against the beneficiary as a co-defendant. It was suggested, in particular, that such a manoeuvre might encounter jurisdictional difficulties.

Paragraph (3)

112. A question was raised as to whether it was appropriate for article 21 to provide the degree of procedural detail contained in paragraph (3). It was stated that the answer depended to some extent on whether the final form of the uniform law would be that of a convention or that of a model law.

Paragraph (4)

113. Some support was expressed for the inclusion of a provision along the lines of paragraph (4), in particular since it helped to underscore the serious and extraordinary character of an injunction that, based on the application by the principal, interrupted the payment process envisaged under the guaranty letter. A suggestion that the uniform law require the principal to post security in all cases did not attract wide support, the preponderant view being that the matter was better left to the discretion of the court.

114. After deliberation, the Working Group requested the Secretariat to revise article 21 to reflect the discussion that had taken place. The revised article would deal less extensively with procedural details than did the current provisions of paragraphs (2) to (4).

Article 22. Preliminary injunction against beneficiary

115. The text of draft article 22 as considered by the Working Group was as follows:

"(1) Where, on an application by the principal, strong prima facie evidence is presented to a competent court that a demand made by the beneficiary constitutes an improper demand, the court may order the beneficiary not to accept payment or to withdraw its demand or, if such a demand is anticipated to be made, not to make the demand, provided that the refusal to issue such an order would cause the principal serious harm that would be more substantial than the loss that might be suffered by the beneficiary due to such an order.

"(2) Before deciding on the application of the principal, the court [may hear the beneficiary] [shall provide the beneficiary with an opportunity to be heard].

"(3) An order referred to in paragraph (1) of this article shall be issued for a specified period of effectiveness not exceeding [six] months. An extension of that period may be made dependent on the initiation by the principal of proceedings other than preliminary proceedings against the beneficiary. [If an order restraining the beneficiary from making a demand is repealed or becomes otherwise ineffective, the period of effectiveness of the guaranty letter shall be deemed to have been extended so as to allow the beneficiary [ten] days after the time of ineffectiveness of that order for making a demand.]

"(4) The court may make the effect of an order referred to in paragraph (1) of this article subject to the furnishing by the principal of such security as the court deems appropriate."

116. There was general agreement that, should the uniform law contain rules on preliminary injunctions against the beneficiary, those rules, particularly as regards the required standard of proof, should be parallel to the rules contained in article 21 on preliminary injunctions against the guarantor. It was stated that an important feature of the uniform law would be to establish a "level playing field", i.e., to provide for equal treatment of both the guarantor and the beneficiary. In that connection, it was agreed that an attempt should be made to merge the provisions of the article with those of article 21 and to reduce the procedural details regulated in paragraphs (2) to (4).

117. As regards the substance of the article, it was stated that rules on preliminary injunctions against the beneficiary were not very common in national legislation and that it might be difficult for national legislators to allow the principal to apply for a court injunction against the beneficiary, i.e., to make it possible for the principal to intervene in the context of a relationship between the guarantor and the beneficiary to which the principal was not a party. It was also stated that in those cases where the beneficiary resided in a foreign country the provision would be of limited use. It was stated in reply that the provision might nevertheless be of some use, particularly in situations where the injunction would be effective and recognized. It was also pointed out that there was some wisdom in providing for injunctive relief within the relationship (between the principal and the beneficiary) where the root of the dispute tended to lie.

118. It was noted that the decision would to some extent depend upon a decision yet to be made as to whether the uniform law would be in the form of a convention or of a model law. The Working Group, after deliberation, agreed to reconsider the matter at a future session on the basis of a draft to be prepared by the Secretariat in the light of the above deliberations.

Article 23. Principles of preliminary proceedings

119. The text of draft article 23 as considered by the Working Group was as follows:

"[(1) Injunctive relief may be sought from a competent court against the guarantor by the principal or by the beneficiary, and against the beneficiary by the principal or by the guarantor, even if the place of business of the applicant is not situated in this State.

"(2) The court shall [endeavour to] deal expeditiously with an application for injunctive relief [and take into due account the special character of the guaranty letter]."

120. It was noted that the draft article was designed to lay down two principles, namely free access to courts for injunctive relief by applicants from within or outside the State in question and an appeal for expeditious proceedings on preliminary injunctions. Reservations were expressed as to the term "competent court" and to the scope of the provision which, unlike articles 21 and 22, embraced not only applications by the principal but also applications by the guarantor and the beneficiary.

121. While support was expressed for the principles underlying the draft article, it was generally felt that there was no need for retaining the draft article in the uniform law. Accordingly, the Working Group decided to delete the draft article.

Chapter VI. Jurisdiction

Preliminary discussion on appropriateness of including in the uniform law provisions on jurisdiction

122. At the outset, it was explained that draft articles 24 and 25 reflected to some extent the uncertainty about the future form of the uniform law and about the extent to which jurisdictional matters should be included in the uniform law. While article 25 and paragraph (3) of article 24 were drafted in the style of a model law, article 24(1) and (2) were reminiscent of conventions. Above all, the draft articles did not cover such important ancillary matters as recognition and enforcement, *res judicata* and stay of proceedings that would more appropriately be dealt with in a convention than in a model law.

123. It was suggested that any future provisions on jurisdiction in the uniform law should be consistent with such international instruments as the 1968 Brussels Convention on Jurisdiction and the Enforcement of Judgements in Civil and Commercial Matters and the 1988 Lugano Convention on Jurisdiction and the Enforcement of Judgements in Civil and Commercial Matters. It was realized that it would be difficult, if not impossible, for a State that adhered to any of those conventions to accept different rules and that difficulty might shape its position on the general question of whether the uniform law should include jurisdiction provisions at all. It was suggested that the Governments of those States might wish to examine this potential conflict and the issue of substantive compatibility, and that the Hague Conference on Private International Law might assist in the process of examination. Another suggestion was that the uniform law should not include provisions on jurisdiction since the above Conventions, while formulated on a regional level, were open for accession by all States.

124. It was stated in reply that the universal composition of the Working Group necessitated due regard to the interests of the many States not adhering to a particular regional convention. A suggestion was made that the Commission might wish to consider in a wider context, not limited to the specific area of guaranty letters, the relationship between universal and regional unification and discuss the desirability and feasibility of providing a universal framework on jurisdictional matters, building on relevant conventions dealing with such matters for regional purposes. As regards the inclusion of provisions on jurisdiction in the uniform law, it was suggested that such provisions should be limited to essential issues of relevance in guaranty contexts along the lines of draft articles 24 and 25. While the formulation of such provisions, because of their close link to substantive and procedural provisions in the uniform law, should be carried out by the Working Group, the Hague Conference on Private International Law could usefully assist in this undertaking at the secretariat level and, if so agreed, at a session of the Working Group with additional or joint participation.

Article 24. Choice of court or of arbitration

125. The text of draft article 24 as considered by the Working Group was as follows:

"(1) The parties may, in the guaranty letter or by a separate agreement in a form referred to in paragraph (1) of article 7, designate a court or the courts of a specified State as competent to settle disputes that have arisen or may arise in relation to the guaranty letter, or stipulate that any such dispute shall be settled by arbitration.

"(2) If the parties have designated a court or the courts of a specified State in accordance with paragraph (1) of this article, only the designated court or courts shall have jurisdiction.

"(3) The provisions of the preceding paragraphs of this article do not constitute an obstacle to the jurisdiction of the courts of this State for provisional or protective measures."

Paragraph (1)

126. The Working Group recalled the decision made at its fifteenth session that arbitration or forum clauses should be allowed (A/CN.9/345, para. 107). As regards forum clauses, a discussion took place as to whether the parties' freedom of choice should be unlimited, as currently provided by article 24, or whether the court chosen by the parties should have a certain connection with the guaranty letter transaction. While there was some support for requiring a certain connection or precluding an unreasonable choice, it was widely felt that the freedom of the parties should be unlimited since any kind of limitation would create undesirable uncertainty and because there might be a practical need to allow parties to choose a forum that bore no connection with the transaction, for example, because it was perceived as neutral by the parties. It was also stated that unlimited freedom of choice would be more consistent with the general principle of party autonomy expressed in the uniform law. It was noted that unlimited recognition of forum clauses did not preclude a designated court from declining to take jurisdiction where appropriate, as provided in article 25(1). After discussion, the Working Group decided to maintain the paragraph.

Paragraph (2)

127. It was explained that paragraph (2) was modelled on a similar provision in article 17 of the Convention on Jurisdiction and the Enforcement of Judgements in Civil and Commercial Matters (Brussels 1968). While some support was expressed for the retention of the paragraph on the basis of the widest possible recognition of party autonomy, strong reservations were expressed against the recognition of exclusive court jurisdiction clauses. It was stated that such clauses were rejected in a number of jurisdictions. It was also stated that the recognition of such prorogation clauses might be dangerous if it was not coupled with the recognition of foreign court decisions. The example was given of a situation where a decision rendered by a designated court with exclusive jurisdiction in a given country might not be enforceable, for lack of recognition, in the country where the assets of the defendant were located. After deliberation, the Working Group decided that the paragraph should be deleted.

Paragraph (3)

128. It was explained that paragraph (3) was modelled on article 21(3) of the Hamburg Rules and reflected an approach also adopted by the 1968 Brussels Convention and the 1965 Hague Convention on Choice of Court (see A/CN.9/WG.II/WP.71, para. 49). No objection was raised against the text of the paragraph and the Working Group decided that it should be maintained in the draft text.

Article 25. Determination of court jurisdiction

129. The text of draft article 25 as considered by the Working Group was as follows:

"(1) Unless otherwise provided in accordance with paragraph (1) of article 24 [or if a designated court of another State declines to exercise jurisdiction], the courts of this State [may exercise] [have] jurisdiction over dis-

putes between the guarantor and the beneficiary relating to the guaranty letter if [the guaranty letter was issued] [the guarantor has its place of business, where the guaranty letter was issued,] in the territory of this State.

"(2) The courts of this State may also entertain an application by the principal for a preliminary order against the guarantor [or the beneficiary] if the guaranty letter was issued in this State."

130. As regards the substance of paragraph (1), i.e., the determination of jurisdiction failing a choice by the parties or in the situation where a designated court declined to exercise jurisdiction, it was widely felt that such a provision was useful. However, it was agreed that the rule contained in the paragraph should not be understood as providing for exclusive court jurisdiction, for reasons similar to those expressed in the context of the discussion on article 24.

131. It was noted at the outset that, while the scope of article 24 was limited to the relationship between the guarantor and the beneficiary, the scope of article 25 was wider, in that paragraph (2) covered preliminary orders sought by the principal. It was recalled that the paragraph implemented a suggestion made at the fifteenth session in the light of the fact that certain issues relating to the principal and possibly injunctions brought by the principal might be addressed by the uniform law. However, some doubts were expressed as to whether the paragraph should be maintained, particularly in view of the fact that its scope encompassed injunctions sought by the principal against the guarantor or the beneficiary. If the paragraph were to be retained, it should be reviewed for consistency with other pertinent provisions of the uniform law.

132. After discussion, the Working Group requested the Secretariat to prepare a revised draft of article 25 in the light of the above deliberations. It was noted that the Working Group had not yet taken a final decision as to whether provisions on jurisdiction should be included in the uniform law.

Chapter VII. Law applicable to guaranty letters

Article 26. Choice of applicable law

133. The text of draft article 26 as considered by the Working Group was as follows:

"[The rights and obligations arising out of] [The rights, obligations and defences relating to] a guaranty letter are governed by the [rules of] law designated by the parties. Such designation shall be by an express clause in the guaranty letter or in a separate agreement, or

Variant A: result without doubt from the terms of the guaranty letter.

Variant B: be demonstrated by the terms of the guaranty letter [or the circumstances of the relationship between the guarantor and the beneficiary].

Variant C: result by implication from the terms of the guaranty letter."

134. As had been the case at the fifteenth session differing views were expressed as to whether or not to include in the uniform law provisions on applicable law. Those who felt that little or no attention should be given in the uniform law to this question cited the limited extent to which questions of applicable law caused difficulties in practice and the consensus that had developed concerning the law applicable to the primary relationships involved in the guaranty letter. Proponents of retention of provisions on applicable law responded that, owing in particular to the uncertainty that might arise when a multiplicity of relationships and laws were involved, the matter warranted attention in the uniform law. It was generally felt that, were any provisions on applicable law to be included, they should be kept as simple as possible, along the lines of draft articles 26 and 27.

135. Turning to the specific formulation of article 26, the Working Group considered whether it was sufficient to refer at the beginning of the article to the "rights and obligations" arising out of the guaranty letter, or whether it would be preferable to refer to the "rights, obligations and defences" relating to the guaranty letter. Some were of the view that the additional reference to "defences" was helpful, while others felt that, though such a reference might not do any harm, it was unnecessary because the notion of "defences" was encompassed in the notion of "rights and obligations".

136. The bracketed reference to "rules" of law designated by the parties also attracted both supporters and opponents. Supporters of retention of that reference felt that it was useful because it would be read as an affirmation of the parties contractual freedom to make the guaranty letter subject to non-legislative rules such to as the UCP or URDG. The prevailing view was that the reference to "rules" of law may be inconsistent with the domestic legal order of a number of States and that therefore article 26 should be limited to sanctioning the freedom of the parties to choose a particular law.

137. Support was expressed for the basic approach used in the draft prepared by the Secretariat, in particular the recognition of party autonomy. As to the implied designation provision contained in article 26, a view was expressed that provision would lead to uncertainty and should therefore be deleted. A suggestion was made that article 26 should be aligned with the language used in the 1980 Rome Convention on the Law Applicable to Contractual Obligations. In response it was pointed out that, while that Convention did exist in particular for regional application, the aim of the uniform law was to provide a uniform rule for universal application. It was also noted that there was some doubt as to the applicability of that Convention to guarantees and stand-by letters of credit and that it might therefore be preferable to formulate language specifically geared to guaranty letters. The members of the Working Group agreed that they would attempt to gather additional information on the manner in which provisions in the uniform law on applicable law would interact with any conventions on conflicts of law. It was further noted that the question of the final form which the uniform law would take was of relevance to an assessment of the provisions in chapter VII.

138. Of the three variants concerning the manner in which designation could be implied, variant A drew the greatest degree of support, particularly from those whose preferred option would be to exclude article 26 altogether from the uniform law. An appealing feature of this variant was that it was directly linked to the terms of the guaranty letter. Variant A did, however, encounter some reservations on the ground that it was too strict a standard. Variant B met with reservations because of the reference to the circumstances of the relationship between the guarantor and the beneficiary. Some doubt was also expressed as to the feasibility of covering in a single formula the various situations covered by the uniform law, in some of which the laws of a variety of States might be at play. A view was also expressed that the review of the provisions on applicable law highlighted the importance of deciding the extent to which relationships other than the guarantor-beneficiary relationship would be covered in the uniform law.

139. After deliberation, the Working Group decided to retain article 26, a decision that would be open to future review. The Secretariat was requested, in revising the article, to reflect the support given to the principle of party autonomy, to remove the reference to "rules", and to incorporate variant A. The Working Group also agreed that the Secretariat should continue to maintain contact and exchange information with the Secretariat of the Hague Conference on Private International Law concerning the preparation of provisions in the uniform law on applicable law and jurisdiction, and to explore, if necessary, other forms of possible cooperation. It was also felt that issues of applicable law specific to the guaranty letter did not appear to merit treatment in a separate convention and that short, simple rules along the lines of draft articles 26 and 27 could appropriately be included within the uniform law.

Article 27. Determination of applicable law

140. The text of draft article 27 as considered by the Working Group was as follows:

> "Failing a choice of law in accordance with article 26, [the rights and obligations arising out of] [the rights, obligations and defences relating to] a guaranty letter are governed by the law of the State where the guarantor has its place of business or, if the guarantor has more than one place of business, where the guarantor has that place of business at which the guaranty letter was issued. [However, if according to the guaranty letter the examination of the demand and any required documents takes place in another State the law of that State applies to the standard of care and responsibility for such examination, failing a specific agreement to the contrary.]"

141. No objections were raised as to the basic approach in article 27, which provided that, when the parties have not designated an applicable law, the law of the place of business of the guarantor (or the place of issuance if the guarantor had more than one place of business) would be applicable. Questions were raised, however, as to the necessity for setting forth this rule in the uniform law, in particular since it was already generally recognized.

142. Differing views were exchanged as to whether to retain the second sentence of article 27, which provided that, where the examination of the demand for payment took place in a country other than that of the guarantor, the law of that other country would provide the standard of care and responsibility for the examination. The need for such a provision was questioned on the ground that the uniform law already provided, in article 16, a standard of care for the examination and that it was therefore unnecessary to include also a conflict-of-laws rule on the point. It was pointed out, however, that the inclusion of the standard of care in a substantive provision might have the desired effect only if the uniform law took the form of a convention.

143. It was noted here, as in other provisions of the uniform law, that the intent was to cover counter-guaranty letters, as provided for in draft article 6*(a)*, with the result that the law applicable to the relationship between the counter-guarantor and its beneficiary (i.e., the guarantor issuing the indirect guaranty letter) would be that of the place of business of the counter-guarantor.

144. After deliberation, the Working Group decided to retain article 27, subject to deletion of the second sentence and to the alignment of the opening words with those of article 26.

III. FUTURE FORM OF THE UNIFORM LAW

145. It was noted that the views expressed in respect of the need for, and the substance of, provisions on jurisdiction and applicable law as well as some other previously discussed draft articles depended in part on the future form of the uniform law. The Working Group, therefore, engaged in an exchange of views on whether the draft text should eventually be adopted in the form of a convention or in the form of a model law.

146. Some support was expressed for the form of a model law since that provided States with a wider latitude as to which provisions of the text were acceptable and could readily be incorporated into the national law. Somewhat wider support was expressed for the form of a convention since that was more in line with the character of the rules envisaged and since it would foster uniformity which was said to be essential for the smooth operation of international guaranty letter transactions.

147. In the light of the continuing divergence of views on the future form of the text, it was proposed that the Working Group should proceed on the working assumption that the final text would take the form of a convention without thereby precluding the possibility of reverting to the more flexible form of a model law at the final stage of the work when the Working Group would have a clear picture as to the provisions included in the draft text. After deliberation, the Working Group adopted that proposal, with the expectation that it would facilitate its future work by providing a degree of certainty.

148. In connection with the discussion of the future form of the uniform law but as a separate point, a concern was

reiterated that had been voiced in the context of the discussion of "extend-or-pay" requests (see paragraphs 71-72). The concern was, in short, that the draft text disregarded the existing difference in terms of firmness between stand-by letters of credit and European-style bank guarantees and that it might be inappropriate to aim for a unitary set of rules that would do justice to neither type of undertakings, for both of which there was a demand on the market. A suggestion was made therefore to envisage some separate provisions that applied only to firm undertakings, whether or not labelled in the uniform law as stand-by letters of credit, and it was promised, for that purpose, to provide the Secretariat with a list of such provisions and relevant information.

149. It was stated in reply that the degree of firmness was not a valid criterion to distinguish between stand-by letters of credit and bank guarantees as such; differences in firmness existed within each of these two categories that were developed separately for historical reasons. It was also recalled that, during the similar discussion referred to above, suggestions had been made for taking into account practical differences of undertakings according to their purpose and payment conditions and, above all, that it had been agreed to continue with the effort of formulating rules of general application.

IV. OTHER BUSINESS

150. The Working Group decided to hold its next session from 30 November to 11 December 1992 at Vienna, subject to confirmation by the Commission at its twenty-fifth session.

D. Working paper submitted to the Working Group on International Contract Practices at its seventeenth session: independent guarantees and stand-by letters of credit: tentative draft of a uniform law on international guaranty letters: note by the Secretariat

(A/CN.9/WG.II/WP.73 and Add.1) [Original: English]

[Text reproduced in part two, IV, B, pp. 313-327.]