

C. Report of the Working Group on International Contract Practices on the work of its nineteenth session
(New York, 24 May-4 June 1993) (A/CN.9/374 and Corr.1)
[Original: English]

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[A/CN.9/374]

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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 then 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

¹Official Records of the General Assembly, Forty-third Session, Supplement No. 17 (A/43/17), para. 22.
²Ibid., Forty-fourth Session, Supplement No. 17 (A/44/17), para. 244.

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 the Group at 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 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, and at its seventeenth session (A/CN.9/361), draft articles 14 to 27 of the uniform law prepared by the Secretariat (A/CN.9/WG.II/WP.73 and Add.1). The Secretariat was requested to prepare, on the basis of the deliberations and conclusions of the Working Group, a revised draft text. At the end of its sixteenth session, the Working Group decided to 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 (A/CN.9/361, para. 147).

7. At its eighteenth session (A/CN.9/372), the Working Group examined articles 1 to 8 of the draft Convention prepared by the Secretariat (A/CN.9/WG.II/WP.76). The Working Group also had before it draft rules on stand-by letters of credit as proposed by the United States of America (A/CN.9/WG.II/WP.77). It was noted that those draft rules were based on the assumption that independent guarantees and stand-by letters of credit would be dealt with in separate parts of the future Convention. It was agreed that the need for such treatment in separate parts could appropriately be determined only when it was clear which, and how many, provisions should be applicable exclusively to bank guarantees or to stand-by letters of credit. The Working Group thus focused its discussion on the draft articles prepared by the Secretariat, with special attention to the question whether a given rule was appropriate for both types of undertakings or for only one of them.

8. The Working Group, which was composed of all States members of the Commission, held its nineteenth

session in New York, from 24 May to 4 June 1993. The session was attended by representatives of the following States members of the Working Group: Argentina, Austria, Bulgaria, Cameroon, Canada, Chile, China, Costa Rica, Ecuador, Egypt, France, Germany, Hungary, India, Iran (Islamic Republic of), Italy, Japan, Kenya, Mexico, Morocco, Nigeria, Poland, Russian Federation, Saudi Arabia, Singapore, Slovakia, Spain, Sudan, Thailand, Togo, Uganda, United Kingdom of Great Britain and Northern Ireland, United Republic of Tanzania, United States of America and Uruguay.

9. The session was attended by observers from the following States: Algeria, Australia, Bolivia, Botswana, Brazil, Central African Republic, Côte d'Ivoire, Czech Republic, El Salvador, Finland, Indonesia, Iraq, Jordan, Kuwait, Myanmar, Pakistan, Panama, Peru, Philippines, Republic of Korea, Romania, Sweden, Switzerland, Tunisia, Turkey and Ukraine.

10. The session was attended by observers from the following international organizations: International Monetary Fund (IMF), Banking Federation of the European Community, Cairo Regional Centre for International Commercial Arbitration, International Bar Association (IBA), International Chamber of Commerce (ICC) and Grupo Latinoamericano de Abogados para el Derecho de Comercio Internacional (GRULACI).

11. The Working Group elected the following officers:

Chairman: Mr. J. Gauthier (Canada)

Rapporteur: Mr. A. Faridi Araghi (Islamic Republic of Iran)

12. The Working Group had before it the following documents: provisional agenda (A/CN.9/WG.II/WP.78), a note by the Secretariat containing the revision of a draft Convention on international guaranty letters (A/CN.9/WG.II/WP.76 and Add.1) and a note containing a proposal of the United States of America relating to draft rules on stand-by letters of credit (A/CN.9/WG.II/WP.77).

13. The Working Group adopted the following agenda:

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

I. DELIBERATIONS AND DECISIONS

14. The Working Group examined articles 9 to 17 of the draft Convention prepared by the Secretariat (A/CN.9/WG.II/WP.76 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 9 to 17 of the Convention.

II. CONSIDERATION OF ARTICLES OF A DRAFT CONVENTION ON INTERNATIONAL GUARANTY LETTERS

Chapter III. Effectiveness of guaranty letter (continued)

Article 9. Transfer of rights

15. The text of draft article 9 as considered by the Working Group was as follows:

Variant A: The beneficiary's right to demand payment under the guaranty letter may be transferred only if so, and to the extent and in the manner, authorized in the guaranty letter.

Variant B: (1) The beneficiary's right to demand payment under the guaranty letter may not be transferred unless so expressly authorized by the issuer in the guaranty letter [or by prior consent in a form referred to in paragraph (1) of article 7].

(2) Partial or successive transfers are permitted only if so expressly authorized by the issuer.

(3) If a guaranty letter is designated as 'transferable' [or contains words of similar import,] without specifying whether or not the consent of the issuer [or another authorized person] is required for the actual transfer,

Variant X: the issuer must, and any other authorized person may, within the limits of the authorization [effect] [implement] the transfer.

Variant Y: no such consent is needed.

Variant Z: neither the issuer nor any other authorized person is obliged to effect the transfer except to the extent and in the manner expressly consented to by it."

16. The Working Group considered the utility on a general basis of including a provision on transfer of the rights of the beneficiary under a guaranty letter. It was reported in that connection that bank guarantees were rarely issued in a transferable form, but that in stand-by letter of credit practice, in particular in the case of financial stand-bys, the stipulation of transferability was frequently found. Accordingly, it was generally felt to be desirable to formulate unified rules in that respect for the guaranty letter, rather than to leave the matter to be resolved by divergent national laws.

17. A question was raised as to whether it was necessary to divide the provisions on transfer of rights and the provisions on assignment of proceeds into two different articles, as had been done pursuant to a suggestion at the sixteenth session. It was stated in response that the question of transfer of rights and the question of assignment of proceeds should continue to be treated in separate articles in order to underscore and make clearer their distinct character. It was suggested that the distinction might be highlighted by revising the title of article 9 along the lines of "Transfer of beneficiary's right to claim payment".

18. As to the content of article 9, the Working Group considered which of the two approaches presented in the draft text would be preferable, particularly from the stand-

point of how the two variants treated the question of whether a guaranty letter designated as transferable still required a specific consent by the issuer to an actual transfer. It was noted that variant A might not determine that question clearly, whereas paragraph (3) of variant B did do so.

19. Differing views were expressed on that question, namely, whether in addition to the authorization in the guaranty letter a consent to the actual transfer would be required. Under one view, the requirement of an additional consent to an actual transfer would be an unjustified restriction on transferability that had already been conceded by the issuer of a transferable guaranty letter. According to that view, at least the issuer and probably also any confirmer of a transferable guaranty letter should be bound to implement a transfer without any additional consent being required.

20. The prevailing view, however, was that the consent requirement should be retained since it was an approach widely used in practice, and that a contrary approach would create an undesirable inconsistency with the Uniform Customs and Practice for Documentary Credits (UCP), to which many stand-by letters of credit were subject. It was also suggested that the consent requirement established some modicum of protection for the principal. A view was that it permitted the issuer to obtain further specific authorization of the principal prior to granting its own consent, a procedure that was reported to be used in stand-by practice. It was stated that such a procedure would be appropriate since what was at stake for both the principal and the issuer was the trustworthiness and reliability of the second beneficiary with respect in particular to any documents to be presented in order to claim payment. It was emphasized that the revision of article 9 should take into account the revision of article 8—as regards the position of the principal—in accordance with the discussions and deliberations at the eighteenth session.

21. In line with the above prevailing view, the Working Group took the position that a main purpose of article 9 should be to provide a rule of interpretation as to whether an additional, specific consent was required for a transfer under a guaranty letter that was designated as transferable, but that contained no provisions as to the procedures to be followed in order to implement a transfer. It was noted that, while in practice a substantial portion of transferable stand-by letters of credit contained specific provisions on transfer procedures (which might be contractual variations of UCP), there were cases of transferable instruments that did not specify actual transfer procedures.

22. Accordingly, it was decided that the approach to consent that should be retained was the one embodied in variant Z of paragraph (3) of variant B. It was also decided that retention of variant A would be sufficient to cover cases in which the guaranty letter contained more than a mere designation "transferable", addressing also other procedural questions for the implementation of the transfer. A suggestion that the words, at the end of variant A, "in the guaranty letter" be deleted did not receive support; it was noted that the wording did not preclude the possibility that transferability could be agreed upon following the issuance of the guaranty letter by virtue of an amendment.

23. As regards paragraphs (1) and (2) of variant B, the Working Group decided that those provisions could be dispensed with since the situations referred to therein were provided for in variant A. The Working Group did not reach a final decision as to whether to retain in paragraph (3) of variant B the words in square brackets, "or contains words of similar import". In support of deletion, it was stated that the words could be removed since, according to the principle established in UCP, the use of terms intended to be synonymous with the word "transfer" would not be deemed to add any meaning. It was pointed out in response, however, that the function of the words in question in the context of article 9 was to ensure the application of article 9 when words synonymous to transfer were used to indicate the transferability of a guaranty letter. A decision was also not reached with respect to the retention, in paragraph (3) of variant B, of the words "or another authorized person".

24. In the course of the discussion of article 9, reference was made to a number of questions to which answers were not expressly given in the present draft. They included whether a transfer would automatically extinguish the right of the original beneficiary to draw under the guaranty letter; who would be entitled to exercise the rights of the beneficiary in the event of the death of the beneficiary or the cessation of its functioning by operation of law; whether a request for a transfer under a guaranty letter not designated as transferable would be treated under article 8; whether the issuer was entitled to pay the transferee even if the issuer was aware that the transfer was unauthorized; and when should the issuer's consent be required to be given.

Article 9 bis. Assignment of proceeds

25. The text of draft article 9 *bis* as considered by the Working Group was as follows:

"(1) The beneficiary may assign to another person any proceeds to which it may be [, or may become,] entitled under the guaranty letter.

(2) *Variant A:* If the issuer, or another person obliged to effect payment, has received a notice in a form referred to in paragraph (1) of article 7 of the beneficiary's [irrevocable] assignment, payment to the assignee discharges the obligor [, to the extent of its payment,] from its liability under the guaranty letter.

Variant B: An assignment obliges the issuer or other person authorized to effect payment to honour a demand made by the beneficiary in conformity with the terms and conditions of the guaranty letter by payment to the assignee, when the recipient of the demand acknowledges the [notified] assignment in a form referred to in paragraph (1) of article 7; the acknowledgement may be made dependent on an agreement with the beneficiary on procedural and similar points with a view to ensuring certainty of, and to preventing measures conflicting with, the assignment and its implementation.

(3) The issuer or other person effecting payment may

Variant X: exercise any right of set-off with a claim against the beneficiary within the limits of article 20.

Variant Y: invoke towards the assignee any right of set-off referred to in article 20."

Paragraph (1)

26. The Working Group discussed whether it was appropriate for the draft Convention to establish as a general principle that proceeds under a guaranty letter were assignable. The view was expressed that the matter should rather be addressed by national legislation in the general law of assignment. The prevailing view, however, was that paragraph (1) contained a useful statement of policy, in line with a principle already expressed in the UCP and in the Uniform Rules for Demand Guarantees (URDG) adopted by the International Chamber of Commerce.

27. A question was raised as to whether the general principle expressed in paragraph (1) should be interpreted as being mandatory. It was generally agreed that parties should be free to agree that proceeds would not be assignable or to lay down any procedures relating to the implementation of an assignment. As to possible conflicts between the draft Convention and national laws regulating the assignability of proceeds, differing views were expressed. Under one view, the rule established in the draft Convention regarding assignment should not affect the applicability of general rules on assignment, since such rules might involve public policy considerations. The prevailing view, however, was that it was useful to seek unification of the law of assignment with respect to guaranty letters. It was noted that the scope of the draft Convention did not encompass the general law of assignment. It was also noted that, in commercial law matters, there seemed to exist few examples of a legislation precluding the assignability of proceeds. The Working Group decided that the provision of paragraph (1) should prevail over contrary law, except for certain provisions of public policy.

28. After deliberation, the Working Group adopted paragraph (1), including the wording between square brackets, "or may become", to make the provision clearly applicable to assignments made before the beneficiary demanded payment.

Paragraph (2)

29. It was explained that variant A did not attempt to unify the disparate national laws on assignment, for example by making notice to the issuer a requirement of validity of the assignment. It rather limited itself to addressing the effect of an assignment known to the issuer by providing that payment to the assignee discharged the issuer's liability towards the beneficiary. Variant B, while touching upon issues regarding the law of assignment, constituted an attempt to take into account such questions as what would be the obligations of the issuer regarding payment upon receipt of several assignment notices exceeding the amount of the guaranty letter.

30. The view was expressed that variant B was preferable as it might better protect the issuer against forged assignments or other misuses of assignment. It was stated in reply that, while the rights of the issuer, principal and beneficiary needed to be protected, it was inappropriate to attempt to solve all private law issues connected with the general law

of assignment. It was also stated that the reference to article 7(1) gave sufficient protection to parties against fraud.

31. The prevailing view was that a more simple provision along the lines of variant A was preferable, since it would not interfere with general provisions on assignment that might already exist. In particular, it was noted that variant A would not attempt to answer the question whether payment to the original beneficiary would also operate to discharge the issuer's obligations.

32. It was noted that the text of variant A did not indicate by whom notice of the assignment should be given. While it was generally assumed that notice should be given to the issuer by the beneficiary, the view was expressed that notification by the assignee should also be possible in certain cases, particularly where the beneficiary was negligent. It was also stated that in certain cases, for example where the assignee held a copy of an authentic contract or another authentic title to the proceeds, it would seem appropriate to allow notification by the assignee. However, it was generally felt that, as a general rule, the obligations of the issuer should not be affected by notification from an assignee, since such person was not a beneficiary under the guaranty letter and only had a contingent right to the proceeds. The Working Group decided that the text should indicate more clearly that the notice should be given by the beneficiary.

33. With respect to the reference to the irrevocability of the assignment, it was noted that, under many national laws, irrevocability would be part of the nature of the assignment. The Working Group decided that the word between square brackets, "irrevocable", should be retained.

34. With respect to the reference to partial assignment, it was widely felt that the wording between square brackets, "to the extent of its payment", should be retained. The reference to the extent of the payment was designed to match the amount of the payment with the extent of the discharge. That reference would become relevant where the assigned proceeds were less than the amount available under the guaranty letter.

Paragraph (3)

35. The Working Group was agreed that the issue of set-off should be reconsidered in the context of the general debate on article 20.

Article 10. Cessation of effectiveness of guaranty letter

36. The text of draft article 10 as considered by the Working Group was as follows:

"(1) The guaranty letter ceases to be effective when:

(a) the issuer receives from the beneficiary a statement of release from liability in a form referred to in paragraph (1) of article 7;

(b) the beneficiary and the issuer agree on the termination of the guaranty letter [in a form referred to in paragraph (1) of article 7];

(c) *Variant A:* the issuer [, or other person authorized to effect payment,] pays the amount [available] [owed] under the guaranty letter; or

Variant B: the issuer pays

- (i) the maximum amount as stated in the guaranty letter or as reduced according to an express provision in the guaranty letter that sets forth a clear [and readily workable] method of reduction by a specified or determinable amount on a specified date or upon presentation to the issuer of a required document;
- (ii) if a part of the maximum amount has previously been paid, the remaining balance;
- (iii) if the beneficiary of a guaranty letter [that does not provide for partial demands] demands payment of only part of the maximum amount and consents to the release of the issuer from liability as to the remaining balance, the requested partial amount,

unless the guaranty letter provides for its automatic renewal or for an automatic increase of the amount available or otherwise provides for continuing effectiveness; or

(d) the validity period of the guaranty letter expires in accordance with the provisions of article 11.

(2) The provisions of paragraph (1) of this article apply irrespective of whether any document embodying the guaranty letter is returned to the issuer, and the retention of any such document by the beneficiary does not preserve any rights of the beneficiary under the guaranty letter, unless the guaranty letter stipulates [otherwise] [that it does not cease to be effective without the return of the document embodying it]."

Paragraph (1)

37. A question was raised as to the use of the expression "ceases to be effective" in the *chapeau*. It was suggested that the use instead of the term "termination" might be clearer. It was also suggested that the expression "cessation of effectiveness" should be clarified so as to make it clear that what would terminate is the ability of the beneficiary to make a drawing under the guaranty letter, but that the expression did not cover any rights or obligations of other persons (e.g., confirmer, adviser) according to the guaranty letter, and that it did not affect rights of the beneficiary accrued before the termination.

38. The Working Group considered at the outset a proposal to combine subparagraphs (a) and (b). This proposal was not accepted, in particular because the Working Group felt that the distinct character of the two methods of termination described therein would be made clearer through the use of separate provisions.

39. Differing viewpoints were expressed as to whether to retain the form requirement referred to at the end of subparagraph (b). On the one hand, support was expressed for retention of the form requirement, with a view to consistency with subparagraph (a), as well as with the approach in articles 7(1) and 8(1), and avoidance of unnecessary uncertainty and evidential problems. In response it

was pointed out that the purpose of subparagraph (b) was to establish a substantive rule of validity for a certain type of termination event, and not to set rules of evidence. It was said further that banks would continue to establish formalities felt to be required by practice. Other concerns were: that the form requirement might limit flexibility, for example by possibly precluding other grounds for termination, in particular tacit agreement and estoppel, though admittedly estoppel could properly be dealt with elsewhere in the Convention; that additional flexibility might be achieved by using instead an expression such as "a form consistent with international banking practice"; that the interests of the principal would not be served by the imposition of form requirements, since such requirements might delay the entry into effect of the termination agreement, while the costs of the guaranty letter being borne by the principal continued to accumulate; and that deletion of the form requirement might spawn the inclusion of non-documentary conditions in guaranty letters. It was stated that article 10(1)(b) was not intended to introduce non-documentary conditions. After deliberation, the Working Group decided to retain the form requirement in subparagraph (b) in square brackets pending further deliberations.

40. The Working Group had before it two variants with respect to subparagraph (c). Variant A, favoured by the Working Group, contained a simpler formulation than variant B, which described the payment situations giving rise to termination in greater detail. It was recognized that a detailed approach would usefully clarify the methods of reduction of the amount available under the guaranty letter. A concern was expressed, however, that a detailed listing rather than a general formulation would create an impression of completeness but might not cover all types of possible payment cases.

41. The Working Group was sensitive to a concern that the inclusion, in variant A, of the words "or other person authorized to effect payment" might generate more questions than it would answer. It was decided that it would be clearer to use a formulation along the lines of "when the amount is paid". It was further decided that the term "amount available" was preferable over the term "amount owed".

42. The view was expressed that the proviso at the end of subparagraph (c), which applied to both variants, was unnecessary since it reflected techniques rarely used in guarantee practice; in any event, article 10 should be regarded as non-mandatory. However, an objection was raised to the deletion of the proviso on the ground that it usefully recognized techniques used in stand-by letter of credit practice. The Working Group decided to retain the proviso.

Paragraph (2)

43. Differing views were expressed as to paragraph (2). One view was that the paragraph could be deleted in its entirety because it was redundant, in that the return of the guaranty instrument was not one of the required events for termination under paragraph (1). A second view was that the provision should be retained in its entirety, including the long version of the proviso permitting party autonomy, since it set forth a progressive general rule, which was at

the same time usefully made non-mandatory. The non-mandatory character of paragraph (2) was said to be necessary in order to take account of the fact that guaranty instruments would continue to be issued with clauses linking expiry to return of the instrument in countries that imposed a return requirement.

44. A third view, which received considerable support, was that paragraph (2) should be retained, but that the party-autonomy proviso should be deleted. Grounds cited for this proposal included: that non-effect of the return of the guaranty instrument should be a mandatory rule so as to resolve an issue that received different treatments in national laws and that created uncertainty in practice; that the proviso would leave the duration of the issuer's obligation to the exclusive wish of the beneficiary, thus raising the spectre of perpetual duration, and that a separate rule might therefore be needed for stand-by letters of credit mandatorily prohibiting perpetual undertakings. However, some proponents of the third view were not in favour of the mandatory character of the rule but merely wanted to make the non-mandatory character less apparent.

45. Considerable interest was generated in a fourth possible approach, which grew out of the above discussion. Under this approach, article 10 would establish the events referred to in paragraph (1) as grounds for termination and indicate that, as a general rule, non-return of the guaranty instrument would have no effect, including in the case where the guaranty letter contained no provision on the effect of non-return. At the same time, it would recognize that the parties may wish to agree that return of the guaranty instrument, either alone or in addition to the events referred to in paragraph (1)(a) or (b), would be required in order to terminate the guaranty letter. However, any such agreement would have no effect beyond the expiry date or, if no expiry date was stipulated, beyond the five-year period established in article 11(c).

46. After deliberation, the Working Group requested the Secretariat to present for its further consideration two variants of paragraph (2), taking into account the discussion that had taken place. One variant would delete the word "otherwise" and retain in square brackets the long version of the party-autonomy proviso, along the present lines. In this connection, a proposal had been made to broaden the formulation of the proviso so as to encompass the possibility of mechanisms equivalent to the return of the instruments for cases of guaranty letters issued in EDI form, as well as to accommodate the existing practice of concluding agreements on termination elsewhere than in the instrument itself. The other variant would be based on the approach described above in paragraph 45.

Article 11. Expiry

47. The text of draft article 11 as considered by the Working Group was as follows:

"The validity period of the guaranty letter expires:

(a) at the expiry date, which may be a specified calendar date or the last day of a fixed period of time

stipulated in the guaranty letter, provided that, if the expiry date is not a business day at the place of business of the issuer, expiry occurs on the first business day which follows;

(b) if expiry depends according to the guaranty letter on the occurrence of an event, when the guarantor receives confirmation that the event has occurred by presentation of the document specified for that purpose in the guaranty letter [or, if no such document is specified, of a certification by the beneficiary of the occurrence of the event];

(c) *Variant A:* if the guaranty letter does not contain a provision on the time of expiry, when five years have elapsed from the date at which the guaranty letter had become effective.

Variant B: if the guaranty letter states neither an expiry date nor an expiry event, or if a stated expiry event has not yet been established by presentation of the required document, five years after the establishment of the guaranty letter, unless the guaranty letter [is issued in the form of a demand guarantee or bond and] contains an express stipulation of indefinite validity."

Subparagraph (a)

48. The Working Group found the substance of the provision contained in subparagraph (a) to be generally acceptable. Several suggestions were made regarding possible refinements of the text.

49. A first suggestion was that subparagraph (a) should include a rule, as found in some countries, that would extend the validity period of counter-guaranty letters for a number of days (period of grace). The Working Group did not adopt that suggestion.

50. Another suggestion was to clarify in all language versions the meaning of the term "business day", especially whether it referred to days that were not official holidays or whether it covered all days where business was in fact conducted. It was agreed that the matter should be dealt with by the Drafting Group with due regard to other texts elaborated by the Commission.

51. Another suggestion was that the text of subparagraph (a) should reflect the possibility that, as stated in article 14, a demand might not have to be made at the issuer's place of business but, if so stipulated in the guaranty letter, the demand should be made with another person or at another place. The Working Group was agreed that such an addition would be useful. It was further agreed that the expiry date constituted the last day of the validity period.

52. Yet another suggestion was that, where the issuer is prohibited from paying the amount of the guaranty letter by a court, the expiry date of the guaranty letter should be extended until the prohibition is removed. In response to this suggestion, it was recalled that a provision to that effect had been suggested by the Secretariat in an earlier draft (article 22; A/CN.9/361, paras. 115 and 116) but that the Working Group had decided not to include rules of such procedural detail.

Subparagraph (b)

53. It was stated that, with respect to expiry events, bank guarantee practice differed from stand-by letter of credit practice. While stand-by letters of credit stipulated an expiry date (a practice reflected in article 42 of the draft UCP 500), expiry events were often found in demand guarantees (a practice reflected in article 22 of the URDG).

54. The discussion focused on the wording between square brackets, "or, if no such document is specified, of a certification by the beneficiary of the occurrence of the event". Differing views were expressed with regard to the proposition that a statement from the beneficiary as to the occurrence of the expiry event could be relied upon by the issuer when no document was specified. It was suggested that, since it could be assumed that the issuance of such a statement would not be in the interest of the beneficiary, the reference to the beneficiary's statement was of limited value. It was also suggested that entrusting the beneficiary with the decision as to the expiry of the guaranty letter in such a manner would raise the possibility of a fraudulent call by a beneficiary that, rather than issuing the statement after the occurrence of the expiry event, made a demand for payment. In response to those observations, it was pointed out that, precisely because the expiry of the guaranty letter was not in the beneficiary's interest, the beneficiary's statement could be considered the most reliable evidence of the occurrence of the expiry event.

55. While doubts were expressed regarding the practical relevance of the wording between square brackets, it was generally felt that the whole of subparagraph (b) was acceptable, in view of the fact that subparagraph (c) established a five-year limit and that stand-by letters of credit would ordinarily be governed by the UCP, which did not permit expiry events.

Subparagraph (c)

56. There was general agreement with the basic proposition that the draft Convention should provide for a maximum period of validity of five years for guaranty letters that did not state an expiry date or event.

57. The discussion focused on the question as to whether the draft Convention should admit the possibility that certain guaranty letters could be of unlimited duration. The attention of the Working Group was drawn to the fact that there were cases in which the parties intended that a guarantee should be of indefinite duration, and that such arrangements were sometimes used in response to administrative requirements (see A/CN.9/358, para. 151). It was noted, however, that certain, but not all, legal systems empowered courts to relieve debtors of indefinite obligations.

58. The attention of the Working Group was also drawn to the fact that the possibility that an undertaking could be established for an indefinite period of time created the risk of perpetual undertakings, which would be contrary to stand-by letter of credit practice since no credit assessment was possible for such cases. It was stated in reply that the same problem existed in respect of bank guarantees. In that connection, it was recalled that there existed stand-by letters of credit containing "evergreen clauses", which

provided, upon expiry, for the repeated, automatic extension of the period of validity, an indefinite number of times. However, such instruments stipulated that they could be terminated upon notice and were thus not to be confused with guarantees that contained no expiry provision.

59. Several suggestions were made, based on the text of variant B. One suggestion was to delete the reference to an express stipulation of indefinite validity at the end of the text. While support was expressed in favour of that suggestion, it was realized that the effect of the deletion was unclear. While some representatives concluded that this would disallow indefinite obligations, a result which was objected to by proponents of party autonomy, other representatives thought that deletion would merely make the possibility of indefinite validity less conspicuous and thus come close to the general solution suggested in variant A.

60. Another suggestion was to retain in the draft Convention the words between square brackets in variant B, "is issued in the form of a demand guarantee or bond and", which were designed to exclude stand-by letters of credit from the application of a proviso admitting the existence of perpetual instruments, as suggested at the sixteenth session (A/CN.9/358, para. 152). That suggestion was opposed to on the ground that the Working Group should attempt to promote, to the widest extent possible, a unified regime that would apply to both bank guarantees and stand-by letters of credit. In that connection, it was recalled that stand-by letters of credit were submitted to the UCP, which excluded the possibility that such instruments could be issued without an expiry date being stipulated. It was also suggested that the reference to the terms "demand guarantee" and "bond" was problematic as neither term had been defined in the Convention. A further concern was expressed that, should the draft Convention expressly mention instruments that might be stipulated with an indefinite validity period, the text might be misinterpreted as creating the possibility that instruments in the form of stand-by letters of credit could be issued with an indefinite validity period.

61. Yet another suggestion was to take the text of variant A and add to it the reference, contained in variant B, to an agreed expiry event that had not been established during the five-year time period. Support was expressed in favour of that suggestion, which was said to avoid the drawbacks of placing too much attention on instruments of indefinite validity and, at the same time, might avoid the need to create separate legal regimes for bank guarantees and stand-by letters of credit. However, a concern expressed in this context was that the parties may sometimes want to allow for an expiry event to take place after more than five years. The Working Group did not reach a consensus on the question.

62. After deliberation, the Secretariat was requested to prepare alternative drafts reflecting the two suggestions referred to in paragraphs 60 and 61.

Chapter IV. Rights, obligations and defences

Article 12. Determination of rights and obligations

63. The text of draft article 12 as considered by the Working Group was as follows:

"(1) Subject to the provisions of this Convention, the rights and obligations of the parties are determined by the terms and conditions set forth in the guaranty letter, including any rules, general conditions or usages [specifically] referred to therein.

(2) *Variant A:* The parties are considered, unless otherwise agreed, to have impliedly made applicable to [their relationship] [the guaranty letter] a usage of which the parties knew or ought to have known and which in international [trade and finance] [guarantee or stand-by letter of credit practice] is widely known to, and regularly observed by, parties to guaranty letters.

Variant B: [In interpreting terms and conditions of the guaranty letter and] in settling questions that are not addressed by the terms and conditions of the guaranty letter or by the provisions of this Convention, regard [may] [shall] be had to generally accepted international rules and usages of guarantee or stand-by letter of credit practice."

64. The view was expressed that the substance of what was currently contained in article 12 would be better placed before articles 8 to 11, since the rules set forth in article 12 would be used for interpreting articles 8 to 11.

Paragraph (1)

65. It was generally agreed that a provision along the lines of paragraph (1) should be included. However, a question was raised as to whether the meaning of the wording at the beginning of paragraph (1) might not be made clearer by substituting the words "*mandatory* provisions of this Convention" for the words "provisions of this Convention". In response to this suggestion, it was stated that what needed to be made clearer was that, as pointed out in remark 1 to article 12, in addition to the mandatory provisions of the Convention and to the terms of the guaranty letter, non-mandatory provisions of the Convention also applied. However, unlike mandatory provisions, non-mandatory provisions of the Convention would not prevail over party agreement. It was noted that a decision remained to be taken as to the mandatory or non-mandatory character of the provisions of the Convention.

66. It was stated that the meaning of the words "the parties" was not clear, in particular as to whether the expression referred only to the issuer (and confirmer) and the beneficiary, or also to the principal. The Working Group noted that, in the text before it, the answer to this question was given in a general manner in article 6; however, pursuant to a decision taken at the sixteenth session, the parties being referred to would be expressly designated in each relevant provision of the draft Convention (A/CN.9/372, para. 89).

67. The Working Group considered whether there was a need for the addition of the word "specifically" in order to make it clear that what was contemplated was reference by the parties to specific usages, not simply a general reference by them to usages. In this connection, a doubt was expressed as to whether it was appropriate at all to speak in terms of a "reference" to usages, if it were assumed that

the word "usages" meant unwritten customs, rather than written sets of rules. It was agreed that the matter could be addressed further at the drafting stage.

Paragraph (2)

68. A view was expressed that the Convention should support only usages expressly incorporated by the parties, rather than also providing for the applicability of usages not referred to by the parties. It was suggested that such a limited approach would create less uncertainty and would promote fairness, in particular in the case where the parties did not possess a similar degree of familiarity with trade usages. The widely prevailing view, however, was that some weight should be accorded to usages that were not specifically alluded to in the guaranty letter.

69. It was noted that paragraph (2) presented two variants. Variant A provided for the incorporation of such usages as implied terms of the guaranty letter. Variant A failed to attract wide support, in particular because it was felt to be inflexible and because of a concern that the reference in variant A to the knowledge of the parties might inject an undesirable degree of subjectivity. Variant B, however, did attract the support of the Working Group. It was felt that it assigned a more appropriate role to usages not expressly alluded to, namely, as a residual source in determining the rights and obligations of the parties, below the level of the suppletive provisions of the Convention.

70. After deliberation, the Working Group decided to retain variant B of paragraph (2), including the words "in interpreting terms and conditions of the guaranty letter and", which had been suggested as an addition to broaden the field of application of usages. It was also agreed that the words "regard *shall* be had" should be used instead of the words "regard *may* be had", since it was not intended to make optional the obligation to take account of generally accepted international rules and usages of guarantee or stand-by letter of credit practice. The Working Group based its decision on an understanding that the obligation to have regard was not equivalent to an obligation to apply and follow in every case and in all respects these rules and usages.

Article 13. Liability of issuer

71. The text of draft article 13 as considered by the Working Group was as follows:

"(1) The issuer shall act in good faith and exercise reasonable care [as required by good guarantee or stand-by letter of credit practice].

(2) *Variant A:* Issuers [and instructing parties] may not be exempted from liability for their failure to act in good faith or for any grossly negligent conduct.

Variant B: The issuer may not be exempted from liability [towards the beneficiary] for failing to discharge its obligations under the guaranty letter in good faith and [, subject to the provisions of paragraph (1) of article 16,] with reasonable care. However, the extent of liability may be limited to [the amount of the guaranty letter] [foreseeable damages]."

Paragraph (1)

72. The view was expressed that paragraph (1) was inappropriate because of its general and abstract nature and therefore should be deleted. However, the Working Group generally favoured the retention of a provision of the type found in paragraph (1). It was then suggested that paragraph (1) should be limited to a statement on good faith, and the reference to the exercise of reasonable care should be deleted. Instead, the application of a standard of reasonable care should be dealt with elsewhere in the Convention, linked to specific activities and relationships of the issuer, in particular those in articles 16 and 17, which could be expanded if necessary. It was suggested that, in implementing such an approach, the URDG and UCP might serve as useful models. In support of the suggestion it was asked whether, in fact, any duties of the issuer other than payment-related duties would be subject to a reasonable-care standard, and whether the standard would extend, for example, to assistance by banks given to principals in drafting the terms of the guaranty letter. Another example was that the reasonable-care standard could be applied to an issuer's payment to a place that had become unsafe, but was otherwise in accord with the guaranty letter. In response, it was stated that this illustrated problems that would arise with a reasonable-care standard. A concern was also voiced that the inclusion of a general standard of reasonable care would impede practice since in some cases circumstances necessitated party agreement to a lower standard of care in the examination of documents.

73. In response to the concerns raised about the reasonable-care standard, it was stated that such a standard was appropriate and necessary since the Convention, unlike the URDG and UCP, was a legal text at the level of statute and not contract rules; thus, it would be looked to as a source of rules for issues not effectively covered by the terms of the guaranty letter or by any associated contract rules. Contractual rules could not, for example, establish unbreakable liability provisions. As to the question of which activities were to be covered, it was pointed out that the premise behind the provision was that all typical activities of the issuer, not merely examination of documents, should be conducted with reasonable care; and that understanding might be clarified by including the reference currently found in variant B of paragraph (2) to the discharge of the issuer's obligations under the guaranty letter. Consideration should also be given to recognizing the autonomy of the parties to agree to lower the standard in specific instances. It was further noted that additional flexibility could be ensured by way of a rule in paragraph (2) permitting some degree of exemption and limitation of liability.

74. The Working Group also exchanged views on the wording in square brackets at the end of paragraph (1), which was intended to add more detail and objectivity by describing the standard of reasonable care in terms of good guarantee or stand-by letter of credit practice. Concerns were expressed that, at least as currently formulated, the wording might disproportionately elevate practice at the expense of judicial determination. It was also suggested that the reference to practice was superfluous because article 12 had already brought practice into play. If the reference to practice were to be kept, it should be clear that

practice was not the sole source of authority. The prevailing view was that wording of the type in the square brackets was desirable, though it could be made clearer by replacing the words "as required by good..." by wording such as "as determined with due regard to good...".

75. After deliberation, the Working Group decided to retain paragraph (1), containing a reference both to good faith and to reasonable care in the discharge of the issuer's obligations under the guaranty letter, and requiring due regard for practice. It was also decided that the applicability of the general standard of care set forth in paragraph (1) would have to be verified with respect to the individual provisions of the Convention.

Paragraph (2)

76. The Working Group had before it two variants in paragraph (2) concerning the extent to which exemption from liability would be permitted. While some support was expressed for variant B on the ground that the limitation on exemptions should conform with the statutory standard of liability and thus include ordinary negligence, the prevailing view was that variant A was preferable. Variant A was perceived to be clearer and simpler, and reflective of the generally accepted view that issuers should not be exempted for failure to act in good faith and for grossly negligent conduct. It was also felt that variant A would be more harmonious with the traditional working, pricing and risk assumptions of guarantee and stand-by letter of credit practice, in particular since it did not purport to restrict party autonomy with respect to lowering of the reasonable care standard. The Working Group did not accept the proposed addition at the beginning of variant A of the words "and instructing parties". It also noted that, in implementing variant A, it would be necessary to ensure harmony between paragraph (2) and article 16.

77. The Working Group considered whether it would be desirable or feasible to add to variant A a provision authorizing contractual limitation of liability. In this discussion the Working Group considered whether there would be any limitation permitted for acts of bad faith or gross negligence and, if so, whether that limitation would be the same as the limitation envisaged for ordinary negligence. It was suggested in this regard that the provisions might simply authorize contractual limitations of liability, leaving to the agreement of the parties and to the applicable law the exact level of the limitation, whether it should be set, for example, as the amount of the guaranty letter or as foreseeable damages. The Working Group concluded that a liability limitation should not be added to variant A since the Convention should not authorize limitation of liability for acts of bad faith and gross negligence. With such conduct excluded from its scope, the limitation provision could be dispensed with since it would relate only to areas where the parties were already authorized to go so far as to exempt liability totally.

Article 14. Demand

78. 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 and conditions of the guaranty letter. In particular, any certification or other document required by the guaranty letter [or this Convention] shall be presented, within the time of effectiveness of the guaranty letter, to the issuer at the place where the guaranty letter was issued, unless another person or another place has been stipulated in the guaranty letter. If no statement or document is required, the beneficiary, when demanding payment, is deemed to impliedly certify that payment is due."

First sentence

79. A suggestion was made that the words between square brackets, "for payment", should be deleted since they insufficiently reflected the practice of stand-by letters of credit, which often involved acceptance of a bill of exchange (or "draft"). However, the attention of the Working Group was drawn to the fact that reference to "payment" was found in various other articles where it appeared to be necessary. It was suggested that the reference to "payment" could be retained in view of the decision made by the Working Group at its previous session to consider the possible inclusion, in article 2(2) or in article 6, of a definition of the notion of payment that would embrace the acceptance of a bill of exchange and other types of obligations of the issuer in terms of payment modalities (see A/CN.9/372, paras. 51-52). That suggestion was found to be generally acceptable. In connection with the above discussion, a view was expressed that the question as to whether the acceptance of a bill of exchange discharged the obligation of the issuer or whether dishonour of an accepted bill of exchange would result in a separate cause of action under the Convention might be considered at a later stage.

Second sentence

80. As regards the words between square brackets, "or this Convention", it was explained that those words had been introduced at a time when the draft text envisaged that possible non-documentary conditions should be treated as documentary conditions by means of a conversion mechanism. It was generally agreed that, in view of the decision made by the Working Group at its previous session that the draft Convention should not cover non-documentary conditions of payment (see A/CN.9/372, paras. 63-65), the words between square brackets should be deleted.

81. As regards the time of presentation of the demand for payment and the stipulated documents, a proposal was made that the draft Convention should establish as a rule that, while the demand itself should be presented before expiry of the validity period, the beneficiary should be allowed, even without stipulation to that effect in the guaranty letter, to present some or all of the stipulated documents at a later time. The Working Group did not adopt that proposal.

Third sentence

82. A suggestion was made that, where a demand for payment was made and no statement or other document

was required under the guaranty letter, the draft Convention should establish an obligation for the beneficiary to issue a statement indicating the reasons for which payment was due. While some support was expressed for the proposal, the prevailing view was that the suggestion would produce the undesirable result of prohibiting simple demand guarantees and clean stand-by letters of credit. It was recalled that the Working Group, at a previous session, had discussed extensively the manner in which guaranty letters payable on simple demand should be accommodated by the draft Convention and decided that it would not be appropriate for a legislative text such as the draft Convention to encourage or discourage the use of any specific type of guaranty letter. Instead, the draft Convention should take into account, and provide certainty for, all types of guarantees in use (see A/CN.9/361, paras. 20-21).

83. As regards the implied certification by the beneficiary that payment is due, it was recalled that the sentence was intended 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. A concern was expressed that such certification, irrespective of its implied or express nature, might be interpreted as creating a cause of action not only for the principal who could request a court injunction restraining payment, based on an allegation that the beneficiary had issued a false certification, but also for the issuer and thus jeopardize the finality of payment.

84. It was suggested that the sentence should be deleted since it had been introduced for clarification purposes and was not intended to create any separate cause of action for the principal or the issuer. It was also stated that the sentence was redundant since, even without it, the very same implication would be drawn. In response it was stated that the above concern would not be met by deleting the sentence and that there was nothing peculiar about the sentence compared with the other references to certifications.

85. Another suggestion was to replace the words "payment is due" by a mention that the demand was not in bad faith or otherwise improper, thereby linking the proviso more closely with article 19. After discussion, the Working Group decided that the proviso should be redrafted along those lines.

Article 15. Notice of demand

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

"[Without delaying the fulfilment of its duties under articles 16 and 17, the issuer shall promptly upon receipt of the demand give notice thereof to the principal or, where applicable, its instructing party, unless otherwise agreed between the issuer and the principal. Failure to give notice does not deprive the issuer from its right to reimbursement but entitles the principal to recover from the issuer damages for any loss suffered as a consequence of that failure.]"

87. The Working Group noted that article 15, which was patterned on article 17 URDG, appeared in brackets as opinion had been divided at the previous sessions on whether the uniform law should impose an obligation on the issuer to give notice to the principal of a demand made by the beneficiary. At the current session, opinion was again divided as to the desirability of imposing such an obligation, mostly for reasons already expressed in detail at the seventeenth session (see A/CN.9/361, paras. 26-27).

88. In support of the deletion of article 15, it was stated that the imposition of a statutory duty to give notice to the principal would compromise the integrity, independence and reliability of the issuer's undertaking, in particular by facilitating the initiation by the principal of steps to block payment. It was also stated that, at least in certain countries, agreeing to give notice before deciding was a procedure that was foreign to stand-by letters of credit and might, in some jurisdictions, raise regulatory concerns. 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. However, it was noted that a similar result would obtain if the article were not retained since then notice would probably be required for bank guarantees (by virtue of the URDG) but not for stand-by letters of credit (by virtue of the UCP).

89. Support for retaining the obligation to give notice was expressed on the ground that notice to the principal was a common practice, not only with respect to bank guarantees but also with respect to stand-by letters of credit in certain countries. It was also stated that the giving of notice was a matter of fairness and did not compromise the independence of the issuer's undertaking because the obligation to give notice was not linked in terms of time to the duty of examining the claim and deciding about payment. The text made it clear that non-compliance with the duty of notification would not affect the effectiveness of payment and the issuer was not required to give notice before payment. The provision was further softened by the rule in the second sentence that the issuer would not be deprived of its right to reimbursement. A suggestion was made to delete the reference to damages and to leave that issue to the applicable general law.

90. The Working Group considered how some of the concerns that had been raised about article 15 might be addressed, short of deleting the provision. One suggestion was to redraft article 15 to the effect that, while the issuer would have to give notice of a demand for payment unless otherwise stipulated in the text of the guaranty letter or in any agreement concluded between the principal and the issuer, such a contrary stipulation would be implied from the mere reference to operational rules such as the UCP that do not foresee the issuance of a notice. A countervailing suggestion was to replace article 15 by the following text: "Where applicable international rules or practice permit or require, the issuer may or must give notice to the principal of its receipt of a demand as long as the notice does not delay the fulfilment of its duties under the guaranty letter."

91. Another suggestion was based on the view that divergencies in opinion regarding the appropriateness of the rule

expressed in article 15 were not purely linked to differences in existing practices regarding stand-by letters of credit and bank guarantees. Such divergencies rather reflected the different approaches taken by different national laws and banking practices with respect to the situations of the principal, the issuer and the beneficiary. It was suggested that the Working Group should consider the possibility that reservations to the applicability of article 15 could be made by States when the draft Convention was open for signature and ratification.

92. Since none of the above suggestions attracted sufficient support, 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.

Article 16. Examination of demand and accompanying documents

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

“(1) *Variant A:* The issuer shall examine documents in accordance with the standard of conduct referred to in paragraph (1) of article 13 [, unless the principal has agreed to a lower standard]. In determining whether the documents are in facial conformity with the terms and conditions of the guaranty letter, the issuer shall observe the [pertinent] [applicable] standard of international guarantee or stand-by letter of credit practice.

Variant B: The issuer shall examine the demand and accompanying documents with the professional diligence required by international guarantee or stand-by letter of credit practice [, unless the principal has consented to a lesser duty of care,] to ascertain whether they appear on their face to conform with the terms and conditions of the guaranty letter and to be consistent with one another.

(2) Unless otherwise stipulated in the guaranty letter, the issuer shall have reasonable time, but not more than seven days, in which to examine the demand and accompanying documents and to decide whether or not to pay.”

Paragraph (1)

94. Two variants of paragraph (1) were presented. The Working Group noted that variant A embodied the division proposed at the seventeenth session between, on the one hand, the standard of care applicable to the examination of documents and, on the other hand, the test to be used in determining whether the submitted documents are in conformity with the terms of the guaranty letter. The question was asked why two possibly different standards were imposed in variant A. Another concern was that the reference to the standard of international practice was vague and would not provide sufficient guidance for the intended purpose. As a consequence it was suggested that the approach agreed upon for article 12(2) should be followed here as well, namely, to use wording such as “having due

regard to” the standard of international practice. Another suggestion was to follow the single-standard approach used in variant B.

95. The prevailing view, however, was that the two-pronged approach set forth in variant A should be retained. It was pointed out that variant A usefully distinguished between standards applicable to two distinct phases of the document examination process: the standard of good faith and reasonable care to be followed by the issuer in examining demands, i.e., in looking for any discrepancies; and the measure to be used in determining the weight or significance to be attached to certain minor discrepancies that may be found, i.e., whether the discrepancies should result in rejection of the demand. It was noted that this type of approach reflected practice, and was incorporated in article 13 of UCP 500.

96. The Working Group next turned its attention to the express reference in the first sentence of variant A to agreements between the issuer and the principal to lower the standard of care applicable to examination of the demand. It was noted that the purpose of the wording was to accommodate a practice reported to be relatively widespread in stand-by letter of credit practice, used when the principal wished to lower costs by reducing examination fees or when time was of the essence, and often in the context of longstanding relationships between the principal and the beneficiary. This type of lowering of the standard was usually not reflected in the terms of the instrument.

97. Divergent views were expressed as to the reference to lowering of the standard. One view was that the wording should be deleted because it was not appropriate to refer to the matter since it dealt with the issuer-principal relationship, a relationship on which it had been decided the Convention should not focus. It was further suggested that the lowering of the standard as described would as a rule not adversely affect the interests of the beneficiary since the lowering of the standard would make it more likely that a discrepant demand would be accepted. A second view, also favouring deletion of the wording, was that lowering the standard was a practice that should not be envisaged or encouraged in the Convention. Doubts were raised as to whether it could be justifiably assumed that a lowering of the standard would uniformly work to the advantage of beneficiaries, who were entitled to an expectation of reasonable care in the examination. A third view was that the practice was sufficiently significant to warrant treatment in the Convention and that the wording should therefore be retained. It was suggested that the provision might even be expanded to envisage the possibility of agreeing with the beneficiary on an even higher standard of examination.

98. After deliberation, the Working Group decided that the wording in question should be deleted, in particular since the general thrust of the Convention was to focus on the issuer-beneficiary relationship. It was stated that deletion of the wording should not be construed as preventing the principal and the issuer from establishing agreed standards. The Working Group based its decision on the understanding that such lowering of the standard of examination

should not be disadvantageous to the beneficiary and should not adversely affect the beneficiary without its consent.

99. The Working Group agreed that wording should be added to variant A to the effect that the issuer was also obligated to determine whether the documents were consistent with each other, a duty also imposed by the UCP. It was further decided that, in the second sentence, the expression "applicable standard" should be used rather than "pertinent standard" and that the words "shall observe" might be replaced by words such as "shall have due regard to".

Paragraph (2)

100. The Working Group noted that paragraph (2) combined approaches as suggested during the previous discussion of a rule on the time allowed for examination, namely, the notion of reasonable time with an outer limit. The Working Group, noting that this type of approach was also found in UCP 500, affirmed the basic thrust of paragraph (2).

101. Views were exchanged as to whether the outer limit should be expressed in terms of "days" (i.e., calendar days) or in terms of "business days". It was pointed out that the latter approach was followed in the UCP, while the more common practice in UNCITRAL legal texts was to express time periods of the length referred to in paragraph (2) (i.e., periods longer than a day or two) in terms of calendar days. After deliberation, the Working Group decided to retain subparagraph (2) in its current form.

Article 17. Payment or rejection of demand

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

"(1) The issuer shall pay against a demand

Variant A: in conformity with the terms and conditions of the guaranty letter.

Variant B: made by the beneficiary in accordance with the provisions of article 14.

(2) The issuer shall not make payment if

Variant X: it knows or ought to know that the demand is improper according to article 19.

Variant Y: the demand is manifestly and clearly improper according to the provisions of article 19.

(3) If the issuer decides to reject the demand [on any ground referred to in paragraphs (1) and (2) of this article], it shall promptly give notice thereof to the beneficiary by teletransmission or, if that is not possible, by other expeditious means. Unless otherwise stipulated in the guaranty letter, the notice shall

Variant A: indicate the reason for the rejection.

Variant B: , if non-conformity of documents with the terms and conditions of the guaranty letter constitutes the reason for the rejection, specify each discrepancy and, if the rejection is based on another ground, indicate that ground.

[(4) If the issuer fails to comply with the provisions of article 16 or of paragraph (3) of this article, it is precluded

Variant X: from claiming that the demand was not in conformity with the terms and conditions of the guaranty letter.

Variant Y: from invoking any discrepancy in the documents not discovered or not notified to the beneficiary as required by those provisions.]"

Paragraph (1)

103. The Working Group expressed a general preference for the approach taken in variant B, which contained a general reference to the requirements set forth in article 14, including those relating to the form of the demand and the place of presentation. While the view was expressed that not all requirements set forth in article 14 were of equal importance, it was generally felt, consistent with a decision made by the Working Group at its seventeenth session, that the obligations of the issuer addressed in article 17 were to constitute a "mirror image" of the obligations of the beneficiary stated in article 14, which established as a general rule that a demand for payment had to conform with the terms of the guaranty letter (see A/CN.9/361, paras. 49-50).

104. The suggestion was made that the reference contained in variant B to a demand made "by the beneficiary" was inappropriate in view of the fact that a demand could be made not only by the beneficiary but also by one or several transferees or by any other person designated under the guaranty letter. Moreover, the reference might be misunderstood as attempting to provide a solution to the unsettled question of a demand made by an imposter. After discussion, the Working Group adopted the suggestion to delete those words.

105. It was noted that the text of paragraph (1) left open the question whether the issuer, in the exceptional case where it would not be obliged to pay, would have an obligation or a mere authorization to refuse payment. In that connection, the Working Group identified two distinct types of situations where the issuer would not be obliged to pay. One such situation was the case where the demand was improper under article 19. That situation was addressed in paragraph (2), which constituted an exception to the rule in paragraph (1). The other type of situation was the case where a demand, while not improper under article 19, did not conform with the terms and conditions of the guaranty letter or other requirements set forth in article 14.

106. It was suggested that, for the situation where a demand was not in conformity with the terms and conditions of the guaranty letter, the draft Convention should establish whether the issuer would be faced with an obligation not to pay or whether it could exercise its discretion. Differing views were expressed in respect of that issue. One view was that the draft Convention should avoid dealing with that issue, since the consequences of payment or non-payment under such a demand were of relevance only to the relationship between the issuer and the principal, which was not the focus of the draft Convention. Another view was that, where the demand did not conform with the terms

and conditions set forth in the guaranty letter, the issuer should be obliged not to pay since there would seem to exist no legal grounds on which payment could be based. Yet another view was that the issuer should be free to decide as to whether it would pay under a non-conforming demand, and it might do so, for example, if it considered payment necessary to preserve its international reputation as a reliable paymaster. It was stated that the only implication of a decision by the issuer to pay under a non-conforming demand was with respect to the reimbursement obligation of the principal. Another statement was made, to the effect that whatever would be the solution for non-conforming demands it should be the same as the solution for improper demands.

107. After deliberation, the Working Group was agreed that, where a demand was neither improper nor in conformity with the terms and conditions of the guaranty letter, the issuer would be free to exercise its discretion in deciding whether or not to pay. However, where the issuer chose to pay upon such a demand, payment should not prejudice the rights of the principal. The Secretariat was requested to prepare a draft provision to that effect for consideration by the Working Group at its next session.

Paragraph (2)

108. Some support was expressed in favour of variant X, which was said to place appropriate focus on the particular issuer by requiring it to reject the demand if it knew, or should have known, that the demand was improper. It was stated that it would be inappropriate to impose on the issuer an obligation to refuse payment without requiring that it knew, or without deeming that it should have known, of the impropriety of the demand. It was said to be particularly important to disallow any act of wilful blindness by which the issuer might choose to ignore the impropriety of the demand.

109. Considerable support was expressed, however, in favour of variant Y, which was said to set forth an objective criterion on which to base rejection of the demand. It was stated that the concept of knowledge of a person or institution, as embodied in variant X, created difficulties of proof because of its subjective character. Moreover, the reference in variant X to what the issuer ought to know might be misinterpreted as requiring investigations on the part of the issuer to determine whether the demand was improper, which would be contrary to the independent and documentary nature of the undertaking.

110. The view was expressed that variant Y was inappropriate, particularly because the general reference to a "manifestly and clearly improper" demand did not establish clearly that the determination of the "manifestly and clearly improper" character of the demand should be made by the issuer. It was stated that it should not be assumed that determination of the "manifestly and clearly improper" character of the demand would be of the type made by an ordinary person, but that it should be made by the issuer as a professional person. A suggestion was made to replace the current text of paragraph (2) by wording based on the text of variant A of draft article 19(1), as follows:

"The issuer shall not make payment if, having due regard to the independent and documentary character of

the undertaking, it is clear and beyond doubt to the issuer that the demand is improper according to article 19."

111. In response to that suggestion, a concern was expressed that, by linking the determination of the improper character to the person of the issuer, the text could be misunderstood as inviting the issuer to exercise its discretion when assessing the improper nature of the demand, thereby allowing for imprudent or unscrupulous behaviour by the issuer. It was stated that a more objective standard was needed.

112. With a view to achieving objectivity in the standard and, at the same time, to maintaining a reference to the need for the issuer to know that the demand was improper, a number of other suggestions were made, for example: to inject the concept of knowledge by the issuer that the demand was improper into the text of variant Y; to add to the text of variant X the opening words "having due regard to the documentary and independent character of the undertaking"; to delete the words "manifestly and clearly" from the text of variant Y; to replace the text of the variants by the words "the issuer has a well-founded reason to believe that the demand is improper" or "the issuer ascertains that the demand is improper".

113. During the discussion, it was realized that the concerns expressed related to two different aspects of the rule. It was generally felt that it would be useful to distinguish analytically between, on the one hand, the facts, usually apparent from documents, that constituted the basis for a legal determination as to the impropriety of a demand and, on the other hand, the making of that very determination. It was agreed that, as to the facts, it was necessary that the issuer be aware of them or that they be within the issuer's sphere of awareness, and that it was not sufficient that only other persons knew about them. However, the second aspect, namely the drawing of the conclusion that those facts amounted to an impropriety of the demand, should not be left to the exclusive judgement of the issuer; the drawing of such a conclusion should be based on whether such facts would be generally considered to be a case of manifest impropriety. In the light of that realization, it was suggested and agreed to use the following wording:

"(2) The issuer shall not make payment if it is shown facts that make the demand manifestly and clearly improper according to article 19."

Paragraphs (3) and (4)

114. The Working Group reaffirmed its support for the inclusion of a requirement of notice to the beneficiary of a rejection of the demand. Views were exchanged, however, as to whether the notice requirement should apply only when the ground for rejection was discrepancies in the documents, or whether the notice requirement should be broader, and be applicable even in cases of improper demand.

115. One view was that the notice requirement, which included an obligation to indicate to the beneficiary the reasons for the rejection, should be limited to cases of discrepant documents. The particular concern underlying that view was that application of the preclusion rule set forth in

paragraph (4) to a failure by the issuer to give notice of impropriety as grounds for rejection would have the unintended effect of aiding those engaging in fraud, or simply attempting to obtain payment under guaranty letters that were invalid or non-existent. It was suggested that imposing the obligation without providing in the Convention for preclusion in such instances would not necessarily deter a court from imposing a sanction such as preclusion.

116. The prevailing view, however, was that the notice requirement should apply to all situations of rejection of the demand, including non-compliance with article 16(2) or invalidity or non-existence of the guaranty letter. It was stated that, even for the case of impropriety, one could not assume that the beneficiary would, as a general rule, have no legitimate interest in being informed of the ground for the rejection, since in some cases the beneficiary might itself be a victim of the fraud. It was suggested that the application of the preclusion rule could be limited to discrepant documents so as to address the concerns that had been raised. The Working Group noted that the extent of the notice requirement was closely linked to the scope of any preclusion requirement agreed in paragraph (4).

117. Before it moved on to the discussion of paragraph (4), the Working Group considered a number of observations concerning other aspects of paragraph (3). One was that in revising the text harmony should be sought between the first sentence in paragraph (3) and the deadline set in article 16(2). In that light the question was raised as to whether the word "promptly" was sufficiently clear. Other questions were whether notice was required when the ground for rejection was the passing of the expiry date, and whether the Convention should include a provision obligating the issuer to hold the documents at the disposal of the beneficiary in case of rejection. As regards the alternative formulations in paragraph (3), both of which required the notice to set forth the reasons for rejection, there was a preference for the simpler approach in variant A. The Working Group agreed to a suggestion to replace the words "decides to reject" by the word "rejects", as the former formulation might be interpreted as suggesting an undue degree of discretion for the issuer.

118. As regards paragraph (4), differing views were expressed as to whether to retain the preclusion rule envisaged therein. One view was that the paragraph should be deleted, since the matter of sanctions could be sufficiently addressed under national law, where the beneficiary would find remedies, and that mention of the preclusion rule was therefore unnecessary in the Convention. A second view, also accepting deletion, was that, while the preclusion rule was necessary in particular for stand-by letter of credit practice, mention of the rule could be removed from the Convention without harming practice since the preclusion rule would apply to stand-by letters of credit by virtue of the UCP. A third view was that, both in the case of violations of article 16(2) and in the case of violations of article 17(3), the Convention should not contain a preclusion rule but should instead provide for damages.

119. A fourth view, one that attracted wide support, was that mention needed to be made of the preclusion rule since

this was a linchpin provision that gave meaning to the obligations imposed on the issuer. It was suggested that failure to include the provision would leave a serious gap in the Convention. However, the Working Group recognized that paragraph (4) should not be drawn so broadly as to apply the preclusion rule to failure to give notice of impropriety or invalidity. It was generally agreed that such a result was not intended or desired and that it should be made clear that the preclusion rule was not meant to apply to such cases. It was also agreed that the provision should be made clearer by referring specifically to paragraph (2) of article 16.

120. Different possible approaches were considered as to how to treat the question of sanctions for any notification duties not made subject to the preclusion rule. One approach was simply to leave the matter to national law, where the beneficiary might be able to obtain the remedies of damages and interest (for example, the amount of the guaranty letter and interest for failure to give notice of defects that might have been cured). That approach was criticized on the ground that it would do relatively little to achieve certainty, since this was an area not specifically addressed in the laws of many countries, and that uniformity of law should be achieved on this important point. Another approach, one that attracted the support of the Working Group, was to consider including in the Convention a provision on sanctions covering those aspects of the notice requirement not covered by the preclusion rule.

121. After deliberation, the Working Group made the following decisions with respect to paragraphs (3) and (4). It was agreed that in paragraph (3) the issuer should be required to give notice of all grounds for rejection, not merely notice of any discrepancies that may have been found in the documents. The Working Group, subject to further consideration, tentatively affirmed that a preclusion rule should be included, but that it should apply only to discrepant documents and to non-compliance with article 16(2). So as to facilitate further deliberations by the Working Group, the Secretariat was requested to prepare a draft provision concerning damages as an alternative provision to the preclusion rule as well as a provision on sanctions for those aspects of the notice requirement not subject to the preclusion rule.

122. The Secretariat was further requested to prepare a tentative version of a provision concerning the time when payment of the guaranty letter was due. It was suggested that such a provision could usefully make it clear that the obligation of the issuer involved prompt payment, not merely a timely decision as to whether to accept the demand for payment. It could further provide clarity as to the use of deferred payment in stand-by letter of credit practice, since that technique was still unfamiliar in a number of countries. The Secretariat was similarly requested to prepare for consideration by the Working Group a provision concerning the obligation of the issuer to pay despite the insolvency of the principal, and despite similar circumstances that might arise affecting the security of the issuer such as failure on the part of the principal to pay the commission.

III. FUTURE WORK

123. The Working Group decided, subject to approval by the Commission, that the next session would be held from 22 November to 3 December 1993 at Vienna.

124. The Working Group noted that it was the intent of the Secretariat to prepare a revised version of draft articles 1 through 17, taking into account the discussion and deliberations at the eighteenth and nineteenth sessions, and that the revised text would be available for the twentieth session. It was agreed that the Working Group, at that session, would first consider articles 18 through 27 as set forth in

A/CN.9/WG.II/WP.76 and Add.1, and thereafter review revised draft articles 1 through 17.

[A/CN.9/374/Corr.1]

Corrigendum

Page 18

Paragraph 85 *should read*

85. Another suggestion was to replace the words "payment is due" by a mention that the demand was not in bad faith or otherwise improper thereby linking the proviso more closely with article 19. After discussion, the Working Group decided that the proviso should be re-drafted along those lines.

D. Working papers submitted to the Working Group on International Contract Practices at its nineteenth session

1. Independent guarantees and stand-by letters of credit: revised articles of draft Convention on international guaranty letters

(A/CN.9/WG.II/WP.76 and Add.1) [Original: English]

2. Independent guarantees and stand-by letters of credit: proposal of the United States of America

(A/CN.9/WG.II/WP.77) [Original: English]

The two working papers, which had already been submitted to the eighteenth session of the Working Group, are reproduced in this *Yearbook*, part two, II, B.1 and 2.