Going Beyond The Four Corners: Reflections On Teaching Letters Of Credit As A Subset Of International Banking Law

James E. Byrne
George Mason University School of Law

Follow this and additional works at: http://digitalcommons.wcl.american.edu/aublr
Part of the Banking and Finance Law Commons, and the International Law Commons

Recommended Citation
Available at: http://digitalcommons.wcl.american.edu/aublr/vol3/iss1/1

This Article is brought to you for free and open access by the Washington College of Law Journals & Law Reviews at Digital Commons @ American University Washington College of Law. It has been accepted for inclusion in American University Business Law Review by an authorized editor of Digital Commons @ American University Washington College of Law. For more information, please contact kclay@wcl.american.edu.
The subject of letters of credit affords an ideal introduction to advanced commercial law studies. Rather than being taught as a traditional case-oriented course, it is best taught by conducting students through discrete problem-oriented experiences that focus on transaction and
litigation skills rather than theory. Otherwise, the basic principles underlying letter of credit law and practice are only superficially grasped. A practice-oriented approach will enable students to discover, interiorize, and apply letter of credit principles in a manner that leads to an appreciation of sound letter of credit law and practice. Such a setting readily reveals the degree to which vocabulary, legal obligations, relevant practice rules, laws, and related issues have been acquired and mastered.

Introduction ................................................................................................................................................3

I. The Inadequacies of the Current Conceptual Framework and Methodological for Teaching Commercial Law .................................................................7
   A. It is Not Contract Law .........................................................................................................................7
   B. Letters of Credit Are Neither Commercial Law Nor Sales Law .............................................................9
   C. The Study of Letters of Credit Is a Useful Basis for Understanding Commercial Transactions ................12
   E. What Are Letter of Credit Law and Letter of Credit Practice? ............................................................14
      1. A Starting Place Is Classification ........................................................................................................14
      2. Deference of LC Law to LC Practice ...................................................................................................17
      3. Encouraging Sound LC Practice .........................................................................................................17
      4. Letter of Credit Law ............................................................................................................................17
      5. Letter of Credit Practice ......................................................................................................................18
   F. Approach to Teaching ...........................................................................................................................20

II. Methodology for Teaching Letters of Credit: A Transactional Approach ...............................................21
   A. Preferred Approach ..............................................................................................................................21
   B. Discussions ........................................................................................................................................21
   C. Two Cautionary Observations for Instructors ......................................................................................22
   D. Assessment ........................................................................................................................................22
   E. Forum and Governing Law ...................................................................................................................22

1. This Article was originally presented to the Transnational Commercial Law Teacher's Conference at the University of Washington School of Law in Seattle, Washington on 19-20 November 2012. It was subsequently presented in modified form at the “Transactional Lawyering: Theory, Practice & Pedagogy” symposium panel discussion entitled “Business Planning and Legal Drafting Pedagogy” at American University on April 5, 2013 in Washington, D.C. This Article represents a revision of these presentations.
INTRODUCTION

This Article addresses teaching letters of credit ("LC") in the context of teaching international commercial law as a two credit hour semester course in light of 30 years of experience teaching commercial law classes of various sizes and experience ranging from undergraduate to skilled bank professionals and attorneys in multiple countries (with and without translation). Part I is a survey of the inadequacies of the conceptual framework for teaching commercial law subjects and of current instruction methods. Part II presents proposals for an alternative method of teaching commercial law and specifically letters of credit through a transactional approach. Finally, Part III discusses several lessons used to teach all grade levels are included to make concrete the abstract points made here.

The goal of the courses envisioned here is to enable the student to appreciate and begin to formulate sound letter of credit law and practice with respect to discrete international issues and indirectly to build a transactional basis towards approaching commercial law.\(^2\)

Because this Article discusses the effective teaching of commercial law from the perspective of teaching a course on LC law and practice, it is helpful to begin with an introduction to LCs.\(^3\)

\(^2\) Because the utility and purpose of this Article relates to its efficacy as a teaching tool, the author will keep much of the substantive legal instruction on letter of credit law and practice confined to the footnotes. The idea is to keep the reader focused on the teaching lessons by not getting bogged down with LC details. However, these details are in the footnotes for those who are interested.

\(^3\) In the United States, letters of credit are governed by U.C.C. Article 5. U.C.C. Article 5 (Letters of Credit) was contained in the original Model U.C.C. that was
The term "letter of credit" and its variations such as "LC" in the context of this paper signifies the family of independent undertakings, (so-called

approved in 1952. In 1957, Model U.C.C. Article 5 was revised extensively as a result of comments by the New York Law Revision Commission. See N.Y. LAW REV. COMM'N REP. 11, 46 (1956); see also Robert Braucher, The 1956 Revision of the Uniform Commercial Code, 2 VILL. L. REV. 3, 4-6, 11-12 (1956). This version was eventually adopted by all 50 states. A non-conforming amendment, styled Section 5-102(4), however, was adopted by Alabama, Arizona, Missouri and New York that displaced U.C.C. Article 5 where the letter of credit was determined to be subject to the Uniform Customs and Practices for Documentary Credits (UCP) published by the International Chamber of Commerce (ICC). See ALA. CODE § 7-5-102 (1966); ARIZ. REV. STAT. ANN. § 47-5102 (1984); MO. REV. STAT. § 400.5-102 (1965); N.Y. U.C.C. LAW § 5-102 (McKinney 1962); U.C.C. § 5-102(4) (1995). A joint American Bar Association/Banking Industry Task Force recommended the revision of original U.C.C. Article 5 in 1990. See Stanley F. Farrar et al., An Examination of U.C.C. Article 5 (Letters of Credit), 45 BUS. LAW 1521, 1536-37 (1990). The revision of U.C.C. Article 5, completed in October 1995, has been adopted by all 50 states, the District of Columbia, and Puerto Rico. See INST. OF INT'L BANKING LAW & PRACTICE, LC RULES & LAWS: CRITICAL TEXTS FOR INDEPENDENT UNDERTAKINGS (James E. Byrne ed., 6th ed. 2014) [hereinafter LC RULES & LAWS] (offering a table of dates of adoption, effective dates, and state citations). For a summary of revised U.C.C., see generally JAMES G. BARNES, JAMES E. BYRNE & AMELIA H. BOSS, THE ABCS OF THE UCC, ARTICLE 5, LETTERS OF CREDIT (Am. Bar Ass'n ed., 1998); James G. Barnes & James E. Byrne, Letters of Credit: 1995 Cases, 51 BUS. LAW. 1417 (1996). This Article refers to the 1957 version of the Model Code as "Prior U.C.C. Article 5" and the 1995 version (including Article 9 amendments) as "Revised U.C.C. Article 5."

4. UCP600 defines "Credit" as "means any arrangement, however named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honour a complying presentation." INT'L CHAMBER OF COMMERCE, PUB'N NO. 600, THE UNIFORM CUSTOMS AND PRACTICE FOR DOCUMENTARY CREDITS art. 2 (2007) [hereinafter UCP600] (Definitions). Revised U.C.C. Article 5 defines "letter of credit" as "a definite undertaking that satisfies the requirements of Section 5-104 by an issuer to a beneficiary at the request or for the account of an applicant or, in the case of a financial institution, to itself or for its own account, to honor a documentary presentation by payment or delivery of an item of value. Revised U.C.C. § 5-102(a) (1995). ISP98 defines "standby letter of credit" as "an irrevocable, independent, documentary, and binding undertaking when issued and need not be state." INT'L CHAMBER OF COMMERCE, PUB'N NO. 590, INTERNATIONAL STANDBY PRACTICES R. 1.06(a) (1998) [hereinafter ISP98] (Nature of Standbys). The UN LC Convention defines "undertaking" as "an independent commitment, known in international practice as an independent guarantee or as a stand-by letter of credit, given by a bank or other institution or person to pay to the beneficiary a certain or determinable amount upon simple demand or upon demand accompanied by other documents, in conformity with the terms and any documentary conditions of the undertaking, indicating, or from which it is to be inferred, that payment is due because of a default in the performance of an obligation, or because of another contingency, or for money borrowed or advanced, or on account of any mature indebtedness undertaken by the principal/applicant or another person." Convention on Independent Guarantees and Stand-by Letters of Credit, art. 2(1), Dec. 11, 1995, 2169 U.N.T.S. 190, 35 I.L.M. 735 [hereinafter UN LC Convention] (Undertaking). URDG 758 defines "Demand guarantee" as "means any signed undertaking, however named or described,
“documentary” letters of credit) including commercial letters of credit, standby letters of credit, independent (bank, first demand) demand


5. The term “documentary” applied to the species instead of the genus is a misnomer since all types of letters of credit are documentary in the sense that they are conditioned on the presentation of a required document. The use of the term “letter of credit” embroils one in a problem of classification because in one sense, “letter of credit” is a name of an independent undertaking, where letters of credit are the best known species of this genus of independent undertakings. However, in a more limited sense, the term is associated with commercial or documentary credits or can include independent guarantees and standbys. Revised U.C.C. § 5-103(a) states that it applies to “letters of credit and to certain rights and obligations arising out of transactions involving letters of credit.” Revised U.C.C. § 5-103(a). This definition includes standby letters of credit, independent guarantees, transferred credits, pre-advices, and reimbursement undertakings under the ICC Uniform Rules for Reimbursement Article 2(g) (Definitions), and an irrevocable undertaking to purchase documents by a nominated bank. Included within the scope of Revised U.C.C. Article 5, but different from “letters of credit,” are obligations such as advices, actions of nominated banks, to an extent the agreement with the applicant, and other undertakings that are not issued by the issuer or do not otherwise fall within the definition of “letter of credit.” There is no formal definition of “commercial letter of credit,” “standby,” or “Independent Demand Guarantee” that distinguishes one undertaking from another. See James E. Byrne, Revised Article 5: Letters of Credit, in 6B HAWKLAND UNIFORM COMMERCIAL CODE SERIES 5-1, 5-200 to -201 (2010) [hereinafter HAWKLAND].

6. A commercial letter of credit is a definite documentary undertaking given by the issuer to a beneficiary that undertakes to honor a presentation of “live” commercial documents as a means of payment for the recent sale of goods or services. It is also sometimes misnamed a “documentary credit,” used to represent the contemporaneous delivery of goods. Historically, “documentary credit” signified an undertaking to pay only against documents of title, but since the acceptance of standbys by the UCP system, this term has come to signify any undertaking to pay against documents, regardless of whether or not they are commercial documents. The definition of “letter of credit” in Revised U.C.C. § 5-102(a)(10) does include a commercial letter of credit. See Revised U.C.C. § 5-102(a)(10); HAWKLAND, supra note 5, at 5-200.

7. Standby letters of credit are definite documentary undertakings by an issuer to honor the presentation of documents that do not represent a demand for immediate payment for a transaction in goods or services. Standbys are not necessarily default undertakings, and are seen with a variety of different terms such as a direct pay element that may be seen in a financial standby, or a standby that functions to ensure payment under a contract for the sale of goods in the event that the buyer fails to pay, distinguishing them from a commercial letter of credit. Under the ISP98, the term “standby” encompasses even “clean” (i.e. demand only) letters of credit, and the Revised U.C.C. Article 5 definition includes standby letters of credit. See ISP98, supra note 4; Revised U.C.C. § 5-102. There is no legal distinction between standby letters of credit and any other type of letter of credit. More colloquial classifications are made between “commercial standbys,” “insurance (or reinsurance) standbys,” “bid/tender bond” standbys or (independent) guarantees, “performance bond” standbys or (independent) guarantees, “supersedes bond” standbys, and “advance payment” standbys or (independent) guarantees. In the United States, banks are required by
The term excludes other undertakings with similar functions.
such as accessory or suretyship undertakings (dependent undertakings), indemnities, insurance, or bilateral contracts.\(^\text{12}\)

I. THE INADEQUACIES OF THE CURRENT CONCEPTUAL FRAMEWORK AND METHODOLOGICAL FOR TEACHING COMMERCIAL LAW

To begin this discussion of effective teaching of commercial law on a transactional basis, it is important to discuss current teaching practices and approaches to material and why they are not effective. Several points need to be made.

A. It is Not Contract Law

In my experience, contract law is inapt for the effective study of LC law.\(^\text{13}\) An LC is only a contract in the sense that it does not fall within the

---

\(^{12}\) The Restatement (Third) of Suretyship and Guaranty specifically states that while "suretyship law is a potential source of generally appropriate analogies[,]" the Restatement does not apply to letters of credit of any type. RESTATEMENT (THIRD) OF SURETYSHIP & GUARANTY § 4 cmt. c (1996). The practical reason for this exclusion is that the law and practice rules governing letters of credit are well-developed, and "[n]o good purpose would be served by disturbing [this] state of affairs." Id. Section 4(d) makes it clear that "instruments analogous to letters of credit[,]" like independent guarantees, are also "beyond the scope" of the restatement. Id. § 4 cmt. d. The basic difference between a suretyship guarantee and a letter of credit is that in a suretyship, any defenses asserted by the primary obligor, even in the underlying transaction may be asserted by the guarantor. In letters of credit, the applicant cannot prevent or assert defenses against the beneficiary in order to prevent the issuer from honoring a complying presentation. The independence principle, that the undertaking by the issuer to pay against a complying presentation is a separate undertaking independent of any underlying contract, is unique to letter of credit practice. See U.C.C. § 5-101 official cmt. ("The objects of the original and revised Article 5 are best achieved by defining the peculiar characteristics of a letter of credit that distinguish it and the legal consequences of its use from other forms of assurance such as secondary guarantees, performance bonds and insurance policies, and from ordinary contracts, fiduciary engagements, and escrow arrangements . . . .").

\(^{13}\) "As is the case with much of letter of credit law, it is futile to look to general
other branch of the law of obligations, namely tort.\(^{14}\) There is no bilateral promise, the beneficiary has no obligation to the issuer/guarantor and

principles of contract or commercial law for antecedents to the law of letter of credit fraud. Its origin lies as much in the mercantile character of the letter of credit as it does in law. It is sui generis.” HAWKLAND, supra note 5, at 5-494. Letters of credit developed not out of contract law per se, but rather as a mercantile specialty. Early English cases have had little impact on the development of letters of credit in business. “[E]nglish case law proved a particularly inapt method to address the fundamental doctrinal questions and challenges that letters of credit presented to the relatively primitive doctrines of bilateral contracts applied to questions such as consideration, characterization, enforceability, mutuality, offer and acceptance, what constitutes a confirmation, and the like.” Id. at 5-23. Letters of credit do not create fiduciary relationships, and the issuer only takes on an obligation to pay according to the terms of the credit. It is up to the applicant to set for the terms of the agreement, what practice rules govern the undertaking, and no terms are truly “bargained for.” If the letter of credit were subjected to traditional bilateral contracts, it is unlikely that such promises made by the applicant/issuer would be enforceable because the traditional law of bilateral contracts has its own formality requirements and also would require that the contract be supported by consideration. Furthermore, letters of credit do not have a requirement that the beneficiary “accept” in the traditional sense of contract formation for the LC to become operative. Some legal systems feel the need to create a fiction of “beneficiary acceptance” because they erroneously believe that the LC is a traditional bilateral contract; however, no such fiction is necessary under Revised U.C.C. Article 5, Prior U.C.C. Article 5, or U.S. common law. HAWKLAND, supra note 5, at 5-23, 5-43, 5-152, 5-298, 5-494; see, e.g., Eastland Bank v. Massbank for Sav., 749 F. Supp. 433 (D.R.I. 1990) (determining whether court could exercise personal jurisdiction over out-of-state LC beneficiary; judge opining that it was inappropriate to compare the relationship between beneficiary and issuing bank with that of two parties in contract).

14. The Official Comment to the Revised U.C.C. § 5-101 (Short Title) describes a letter of credit as an “idiosyncratic form of undertaking that supports performance of an obligation” and seeks to define “the peculiar characteristics . . . that distinguish it and the legal consequences of its use from other forms of assurance . . . .” Revised U.C.C. § 5-101 official cmt. What distinguishes letters of credit is that it is a voluntary obligation, and as such is distinguished from other types of obligations that are imposed by the law like torts. Also, because of a letter of credit’s tripartite nature and the independence of an issuer’s undertaking, it does not fit well within the framework of traditional bilateral contract or any other category of law. The issuer deals “at arm’s length” and is obligated to pay only according to the terms of the letter of credit. The issuer is not a fiduciary for either the beneficiary or the applicant. The relationship is governed by rules of practice and local law, like Revised U.C.C. Article 5. The responsibility to the applicant is set forth in the parties’ agreement, which is how the relationship and terms of payment will be determined. “Because letters of credit are not well understood by lawyers or judges, it is common for judicial opinions to provide a brief introduction to the transaction and the law, often as a preface to explaining the doctrine of independence.” HAWKLAND, supra note 5, at 5-43; see also Confeccoes Texeis De Vouzela, LDA v. Riggs Nat’l Bank of Washington, D.C., 994 F.2d 851 (D.C. Cir. 1993) (confirming bank in letter of credit transaction cannot be sued in tort by account party); In re B.C. Rogers Poultry, Inc., 455 B.R. 524, 564–65 (Bankr. S.D. Miss. 2009) (describing an LC as a three party arrangement); Caroline Apartments v. M&I Bank, 334 Wis. 2d 808 (Wis. Ct. App. 2011) (unpublished) (finding that LCs
perhaps to the applicant (who is, in any event, not a party to the LC undertaking) to perform (draw on the LC), and there is no bargained for agreement between the issuer/guarantor and the beneficiary.

An example is transfer. In contract law, “transfer is used in parallel with ‘assignment’” whereas in LC law and practice, they are very different phenomena. An LC transfer is of the right to draw, namely, the transferee is a new beneficiary. LCs are not transferable undertakings unless they expressly so provide. An “assignment” in LC law and practice is of any proceeds that may result from a drawing on a LC. If an assignment of proceeds by the beneficiary is not acknowledged by the issuer, then the issuer has no obligation to pay proceeds to the assignee.

B. Letters of Credit Are Neither Commercial Law Nor Sales Law

While LCs are a part of commercial law in a broad sense, they are more like pre-modern law in that they are a promise that runs to a unique person that is not freely transferable and calls for a performance that is more precise than substantial. Many, if not most, of the instincts of a modern commercial lawyer or jurist are inapt in the application of LC law.

---

15. As indicated in Chapter 15 of the Restatement 2d of the Law: Contracts, Chapter 15 (Assignment and Delegation), transfer of contractual rights is distinguished between “assignment” of rights and “delegation” of duties. Restatement (Second) of Contracts § 317 (1981). Both of these actions can be loosely referred to as a “transfer.” The Introductory Note to the Chapter explains that the two topics are “part of the larger subject of the transfer of intangible property.” Id. ch.15.

16. See URDG 758, supra note 4, art. 33 (Transfer of Guarantees and Assignment of Proceeds); UCP600, supra note 4, art. 38 (Transferable Credits); ISP98, supra note 4, R. 6 (Transfer, Assignment, and Transfer by Operation of Law); UN LC Convention supra note 4, art. 9 (Transfer of Beneficiary’s Right to Demand Payment); Revised U.C.C. § 5-112.

17. See URDG 758, supra note 4, art. 33 (Transfer of Guarantee and Assignment of Proceeds); UCP600, supra note 4, art. 39 (Assignment of Proceeds); ISP98, supra note 4, R. 6 (Transfer, Assignment, and Transfer by Operation of Law); UN LC Convention, supra note 4, art. 10 (Assignment of Proceeds); see also Revised U.C.C. § 5-114 (Assignment of Proceeds) (generally following the approach with a limited exception where the assignee holds the original LC).

18. At common law, choses in action, including contract rights were not transferrable because debts were believed to be personal to the party that incurred it. If a contract were to be assigned, it was seen as "maintenance-as tending to encourage
One telling example is the LC preclusion rule, a doctrine that operates quite differently than estoppel, to which it is sometimes incorrectly equated. An issuer/guarantor that fails to give adequate and timely notice

19. The ISP98, UCP600, and UCC all include preclusion rules. URDG 758, supra note 4, art. 24(d)-(f) (Non Complying Demand, Waiver and Notice); UCP600, supra note 4, art. 16(c), (f) (Discrepant Documents, Waiver and Notice); ISP98, supra note 4, R. 5.03 (Failure to Give Timely Notice of Dishonour); Revised U.C.C. § 5-108(c) (Issuer’s Rights and Obligations). Preclusion operates as a way to provide certainty and finality with letter of credit practice, and also as a way to ensure rigor and instill confidence. It operates to assure a beneficiary that an issuer will not be complacent with the applicant, and will give the beneficiary “prompt notice of refusal detailing discrepancies and that the [issuer will not wait for] market movements that might be more favorable before taking a position on the presentation.” See HAWKLAND, supra note 5, at 5-440. Preclusion applies both to the failure to examine the documents within a reasonable time, as well as failure to give timely notice of refusal. A bank is not expected to give notice instantaneously, but it may not deliberately delay. The practice rules largely dictate what an issuer must do to give timely notice of dishonor, from calculation of the time to dishonor, with what specificity a notice must contain of discrepancies, and in what medium the notice must come in. At a minimum, the notice must not be ambiguous as to why the presentation is being refused, or provide information on how to cure it. Deference is also given to practice as to what is considered timely and reasonable standards. The practice rules and laws operate without regard to the curability of the discrepancies; however, the notice has at least some relevance to the beneficiary’s ability to cure discrepancies. Failure to state a reason for dishonor will preclude the issuer from asserting the defect at a later date. One of the reasons that the concept has proven difficult for lawyers and courts is that it appears to be contrary to the banks’ interest in that it holds them to their first expression of their response within a relatively narrow time frame and visits on them
of refusal is precluded from asserting that the documents presented are not in compliance with the terms and conditions of the undertaking regardless of whether the discrepancy was curable or there was reliance. The point of this rule is not to give the beneficiary a “free ride”, but to assure the integrity of the LC institution and to require issuers/guarantors to make a timely and complete examination and to give timely notice of the results. While curability is a factor, it is a secondary one.  

In a Sales course, there are other differences with respect to payment terms. The focus in a letter of credit course regarding payment terms should be on the LC terms to be inserted into a contract for payment against the recent shipment of goods or extrapolated from it and inserted into a LC and their interpretation and application. In a Sales-oriented course, the focus would be on the provisions for payment by LC in the sales contract. Most of the materials on Sales that deal with LCs overlook this point and attempt to provide a mini-treatise on letters of credit. Such an approach is inadequate to teach LCs and does not attempt to focus students’ attention on drafting an adequate payments clause or interpreting the inadequate ones that are often drafted. This failure may offer one explanation for the relative lack of sophistication in contract clauses related to payment or assurance of payment by LCs. An example would be whether a standby LC providing for payment 60 days after the date of

---

20. The notion of curability is linked to the concept of separateness of presentation. ISP98 Rule 3.07 (Separateness of Presentation), and URDG Article 18(a) (Separateness of Each Demand) both contain provisions stating that unless the undertaking expressly states, a beneficiary may make multiple presentations under a letter of credit so long as it has not expired. URDG 758, supra note 4, art. 18(a); ISP98, supra note 4, R. 3.07. In theory, a beneficiary could attempt to cure any discrepancies that were the basis for the original dishonor by the bank, and still receive the amount available under the credit. The UCP does not expressly so state, but the ability to cure has been recognized by the ICC. See INT’L CHAMBER OF COMMERCE, PUB’N NO. 371, DECISIONS (1975–1979) OF THE ICC BANKING COMMISSION R. 13 (1980). Preclusion, however, is not based primarily on the right to cure discrepancies but on the importance of forcing an issuer or confirmer to make a timely and complete statement of the grounds for refusal so as to prevent it from raising discrepancies in a piecemeal fashion or from delaying refusal pending shifts in the market price of goods. See JAMES E. BYRNE, THE OFFICIAL COMMENTARY ON THE INTERNATIONAL STANDBY PRACTICES 113–14 (James G. Barnes ed., 1998) [hereinafter THE OFFICIAL COMMENTARY ON THE INTERNATIONAL STANDBY PRACTICES].
delivery on a required copy of a transport document meets a sales contract required of "payment by LC issued by an acceptable bank[;]" i.e., is a "standby" a "letter of credit" in the sense intended? This question is one for Sales law and not LC law.

C. The Study of Letters of Credit Is a Useful Basis for Understanding Commercial Transactions

The study of LCs is an ideal platform from which to describe and discuss commercial transactions because it is highly challenging for even the brightest student at the highest level, but also understandable in a basic, but meaningful way even for students at the beginning of higher education. The study of LCs also brings together all of the aspects of a commercial transaction including sales or service contracts, payment, delivery, terms, obligations of third party intermediaries regarding delivery and inspection, the correspondent banking system, the differences between dependent and independent undertakings, the use of commercial documents in a representational capacity, mechanisms for third party assurance of performance, and mechanisms for assurances of repayment. These observations would also apply to differences with other forms of financial assurance ranging from the performance of obligations to the repayment of funds, whether from simple loans or supporting the bond market.

Furthermore, the study of LCs is a significant instance of workable self-regulation in commercial law. Why it works is another, and charged, question. In my opinion it is because the LC banking community, which has evolved the rule making apparatus, has grasped the essential need for neutral rules as a basis for the credibility of the product and of specific banks. It helps that the banks themselves are often the beneficiary or nominated banks as well as issuers and confirmers and that the applicants are often good customers, thus feeding the desire for neutral rules.

D. Methodologies for Teaching Letters of Credit: The Problem of Using Reported Judicial Decisions

In my opinion, an approach that emphasizes retention and reporting of facts, rules, and data embedded in judicial decisions should be avoided. The result of such an approach is a superficial understanding of LC law and

21. See, e.g., Torco Oil Co. v. Innovative Thermal Corp., 763 F. Supp. 1445, 1445-46 (N.D. Ill. 1991) (denying motions for judgment notwithstanding verdict or new trial and overlooking the significance of UCC Section 2-325 ("Letter of Credit" Term; "Confirmed Credit") for the significance of the term "Letter of Credit" in a contract).
often a misunderstanding of LC practice. To a considerable extent, this approach explains why lawyers and judicial decisions have tended to fail to grasp and apply the principles behind LC law. It is also why, in the opinion of experts, more than half of reported decisions are wrong; and, of those that are correct, more than half are correct for the wrong reason.\(^{22}\)

U.S. law schools can place too much emphasis in their teaching methodology in advanced courses on the use of reported cases as a mechanism for teaching students the “black letter law.” This approach is not optimal if the goal of the course is to elicit critical faculties regarding the subject matter. The tendency of casebook editors is to fill their books with the leading decisions coupled with detailed notes and explanations of the principles contained in the cases.

Instead, casebooks should simply be “bare,” that is, platforms for the classroom experience, and should not be treatises of the subject involved. That function should be left to treatises themselves and students should be left to their own devices in learning how to master and utilize them in understanding the field as they will in practice. Thus, the texts should be excerpts from reported cases or the text of various undertakings that are appropriate platforms for discussion.\(^{23}\) In my opinion, at least one-third of the cases in the materials should be wrong, misguided, or problematic. Otherwise, students are reinforced in the notion that they should take the printed word too seriously, a serious mistake for a lawyer. The notes should pose dilemmas that are not solved in the text, forcing students to grapple with the problem.

Needless to say, students hate this approach. They simply want to write down the answer and move along to “learning” more “things” with as little

\(^{22}\) The author has spent more than 15 years writing summaries of international letter of credit cases in the Annual Survey of Letter of Credit Law & Practice (IIBLP) (1996–2009), the International Review of International Banking Law (2010–present), and as co-author of the American Bar Association’s Business Law Section’s Business Lawyer UCC Survey. This opinion of judicial decisions involving letters of credit derives from that experience and from working with bankers and lawyers around the world in annual sessions in the Americas, Europe, the Middle East, and Asia under the auspices of the Institute of International Banking Law & Practice. It should be noted, however, that under a well-drafted and explained statutory scheme, these estimates improve considerably, based on the experience of courts in the US before a statutory scheme (pre U.C.C. Article 5 – pre 1956), under a skeletal and premature scheme (Prior U.C.C. Article 5 – 1956 to 1998), and under a modern, sophisticated, systematic statute with commentary (Revised U.C.C. Article 5 – post 1998). See generally James E. Byrne, The Revision of U.C.C. Article 5: A Strategy for Success, 56 BROOK. L. REV. 13, 13 (1991).

\(^{23}\) See, e.g., JAMES E. BYRNE, INTRODUCTION TO DEMAND GUARANTEES & STANDBYS (2012).
intellectual strain or work as possible. This negative student reaction is a positive indication of the merits of the method, based on the reasons behind it. Another positive indicator is that more mature students tend not to react in this manner.

The problem remains as to where students can look for the resolution of the problems and issues. Subtle hints should be given. In addition, the ready availability of the texts of practice rules, statutory provisions, and model forms helps considerably. The library should also have ample resources. Above all, however, students must learn to find sources themselves, a skill that they will need to do in the real world so it is essential not to spoon-feed them.

E. What Are Letter of Credit Law and Letter of Credit Practice?

Since it has been asserted that LCs are not to be understood from the perspective of contracts or sales, it is necessary to consider what constitutes LC law and practice.

1. A Starting Place Is Classification

There has been considerable debate about how to classify LCs. This debate was undertaken at the beginning of the 20th Century and the best resolution was that it should be understood as sui generis, a manifestation of the lex mercatoria.24 That conclusion, in any event, coincides with my opinion.

Excluded from an LC course in most instances are the following related LC subjects: bank-to-bank reimbursements,25 collections,26 SWIFT,27 and


25. Bank-to-bank reimbursement is a mechanism by which an issuer can encourage a nominated bank to act on a nomination by indicating a bank to which it can turn for reimbursement. UCP600, supra note 4, art. 13 (Bank-to-Bank Reimbursement Arrangements) (providing basic rules for such reimbursements). The Uniform Rules for Bank-to-Bank Reimbursements Under Documentary Credits (URR725) provide comprehensive rules for bank-to-bank reimbursements. INT’L CHAMBER OF COMMERCE, PUBL’N NO. 725, ICC UNIFORM RULES FOR BANK-TO-BANK REIMBURSEMENTS (2008). URR725 Article 2(g) (Definitions) defines “reimbursement undertaking” as “a separate irrevocable undertaking of the reimbursing bank, issued upon the authorization or request of the issuing bank, to the claiming bank named in the reimbursement authorization, to honour that bank’s reimbursement claim, provided the terms and conditions of the reimbursement undertaking have been complied with.” Id. art. 2(g). Revised U.C.C. § 5-108(i)(1) and (2) set forth the rights of an issuer or confirmer to obtain reimbursement after honoring a complying presentation. Revised U.C.C. § 5-108(i)(1), (2) (1995). ISP98 Rule 8.04 (Bank-to-Bank Reimbursement) incorporates the current version of the URR by reference. Most often, these obligations
authentication. These topics are usually not addressed except in training professionals because they clutter discussions without adding light to basic

arise when the issuing or corresponding bank does not have a correspondent relationship with a bank that acts in accord to terms of the LC. ISP98, supra note 4, R. 8.04. Reimbursement undertakings are important to letter of credit practice because they provide the “necessary lubricant in correspondent banking relationships permitting banks which do not have an account relationship to act on behalf of other banks with the knowledge that they can claim reimbursement from a local bank with which they have a relationship.” BYRNE, supra note 20, at 289; see generally DAN TAYLOR, ICC GUIDE TO BANK TO BANK REIMBURSEMENTS UNDER DOCUMENTARY CREDITS (1997).

26. The 1995 revision of the Uniform Rules for Collections (“URC522”) is a revision of the URC322, published in 1978. INT’L CHAMBER OF COMMERCE, PUBL’N No. 522, ICC UNIFORM RULES FOR COLLECTIONS (1995); INT’L CHAMBER OF COMMERCE, PUBL’N No. 322, UNIFORM RULES FOR COLLECTIONS (1978). These rules guide the practice of handling of collections (sometimes referred to as “documentary collections” and “clean collections”), and they are completely different from handling of presentations under an LC, even when waiver of discrepancies is sought. Bank collections are handled under U.C.C. Article 4.

27. SWIFT/S.W.I.F.T. stands for “Society for Worldwide Interbank Financial Telecommunication.” After the completion of Revised U.C.C. Article 5, the periods between the letters were dropped and the name is now “SWIFT.” SWIFT is a financial industry owned, cooperative network that supplies secure, standardized messaging services and interface software, servicing more than 10,000 financial institutions in more than 212 countries. SWIFT, http://www.swift.com/about_swift/index (last visited Nov. 12, 2013). SWIFT’s worldwide community is made up of banks, broker/dealers, investment managers, and market infrastructures in payments, securities, treasury and trade. Id. at http://www.swift.com/about_swift/community/swift_user_categories. It is estimated that more than 90 percent of their commercial LCs by major LC banks are issued via SWIFT MT 700. Andr6 Casterman, ICC Survey 2012, Swift Trade Traffic-2011 Statistics, ICC BANKING COMMISSION 20 (Mar. 27, 2012), available at http://www.iccwbo.org/Data/Documents/Banking/SWIFT-Trade-Traffic-Stats_Andre-Casterman/. Information about SWIFT can be obtained at www.swift.com.

28. Authentication is the method by which a document may be signed, and also confirming the identities of an issuer, beneficiary or confirmer. The authentication must show who made the authentication and include that party’s signature or initials. If the authentication appears to have been made by a party other than the issuer of the document, the authentication must clearly show what capacity that party had to authenticate the correction or alteration. Under UCP600 Article 3 (Interpretations), it can be understood as an alternative to a “signed” document as long as it proves that the document is legitimately verified. See UCP600, supra note 4, art. 3. Under UCP600 Article 9(b), (c), & (f) (Advising of Credits and Amendments), in the process of advising a credit with respect to the sender and the integrity of the transmission, a certain level of formality is implicit. Id. art. 9(b), (c), (f). Revised U.C.C. § 5-104 requires that a credit or similar undertaking be “authenticated.” Revised U.C.C. § 5-104. While this term is not defined in U.C.C. Article 1, Official Comment 2 to Revised U.C.C. § 5-104 states that it refers to the “authentication only of the identity of the issuer, confirmer, or adviser.” Id. § 5-104 cmt. 2. “The statute indicates two means by which the record may be authenticated, namely: (1) signature or (2) ‘in accordance with the agreement of the parties or the standard practice referred to in Section 5-108.’” HAWKLAND, supra note 5, at 5-306. Where a signature is not authentic, the bank or person purportedly having signed it is not obligated but the person actually signing it
would be liable. The reference to standard LC practice is to the practice of "financial institutions that regularly issue letters of credit." Revised U.C.C. § 5-108(e). "In effect, this provision defers to the practices of bankers with respect to authentication, recognizing the high degree of sophistication that has evolved in providing secured means of authentication." HAWKLAND, supra note 5, at 5-306 to -307. It is important to note, however, that authentication is not used to determine whether the documents or signatures are indeed genuine. Issuers take the documents on their face value. See id.; INST. OF INT'L BANKING LAW & PRACTICE, 2007 ANNUAL SURVEY OF LETTER OF CREDIT LAW & PRACTICE 183–84 (James E. Byrne & Christopher S. Byrnes eds., 2007) (discussing Hilton Grp., PLC v. Branch Banking & Trust Co. of S.C., No. 2:05-937-DCN, 2007 WL 2022183 (D.S.C. July 11, 2007)), a rare case of an LC where the signature of the issuer is forged). In recent times, the systems of authentication are sufficiently effective that the problem of a forged LC rarely arises. The use of banks as advisers and the widespread use of the SWIFT system have effectively eliminated these issues. See UCP600 COMMENTARY, supra note 19, at 221–23, 1275, 1440.

29. LCs are not negotiable instruments. However, there are some credits under which negotiation, i.e. the transfer from one bank to another, occur. See James E. Byrne, Negotiation in Letter of Credit Practice and Law: The Evolution of the Doctrine, 42 TEX. INT'L L.J. 561 (2007).

30. Pre-advice is provided for in UCP600 Article 11 (Teletransmitted and Pre-Advised Credits and Amendments). UCP600, supra note 4, art. 11. The need for pre-advice arises in a commercial transaction where the beneficiary requires an LC for financing to produce the product but the details of transportation are not available. Were the credit issued without these details, the issuer would have to consent to any amendment; a pre-advice is an obligation of the issuer to issuer a similar credit which is not inconsistent, permitting omitted details to be inserted. UCP600 Article 11 (Teletransmitted and Pre-Advised Credits and Amendments) defines "pre-advice," which is a practice in commercial LCs where a bank will issue an advice, indicating that it will, under certain indicated terms, issue a credit on certain indicated terms. Id. While the definition of "credit" in UCP600 Article 2 does not expressly refer to a pre-advice, if read with Article 11, Article 2's definition certainly does encompass a pre-advice. Id. arts. 2, 11. Under the UCP, this advice is effectively equated to an LC because the issuer is irrevocably obligated to issue a credit under its specified terms without "delay." These types of undertakings are vulnerable to misuse. The definition of "credit" in Revised U.C.C. § 5-102(a)(10) raises a question about whether a pre-advice is truly an LC because the pre-advice is not the operative credit instrument. Revised U.C.C. § 5-102(a)(10). Nevertheless, this type of obligation is the functional equivalent of an LC and should be regarded as such. See HAWKLAND, supra note 5, at 5-204 to -205; UCP600 COMMENTARY, supra note 19, at 119; see also Bouzo v. Citibank, N.A., 96 F.3d 51 (2d Cir. 1996) (making summary judgment in favor of alleged issuer who promised in writing to "issue an unconditional, irrevocable bank pay order" reversed because terms were ambiguous; purported beneficiary had argued, inter alia, that the undertaking was a pre-advice although this theory was not mentioned in the appellate decision).

31. Occasionally, such topics can be addressed in required graded papers, assignments, or with each student reporting to the class on his or her assigned topic.
2. Deference of LC Law to LC Practice

The fundamental principle in the field of LC law is the deference of law to sound rules of practice. The corollary of this principle is that in order to understand LC law, it is necessary to understand LC practice. There are, of course, exceptions to this principle, but they are rather limited. There are also important policy questions in addition to the matters indicated above, namely the importance of insisting on the soundness and neutrality of the practices to which deference is given.

3. Encouraging Sound LC Practice

The primary mission of LC law is to encourage sound LC practice. On the whole, soundness is manifested in the neutrality of a given rule which does not favor any particular party and which is manifested in making the LC workable and not in multiplying excuses to payment. This rule often equates to contra proferentium, that is, construing ambiguity against the issuer/guarantor but which can also involve public policy issues where LC fraud, protected persons, perpetual undertakings, or similar issues are involved.

4. Letter of Credit Law

To the extent that there is a letter of credit law, it is either statutory or case-inspired law. There are chiefly three statutory schemes available, the United Nations Convention on Independent Guarantees and Standby Letters of Credit, Revised U.S. U.C.C. Article 5 (Letters of Credit), and

---

32. The exceptions include LC fraud or abuse (although there are practice issues grounded in the correspondent banking network that give rise to exceptions for protected persons or the equivalent of good-faith purchasers with qualifications), formality, and the power to issue LC-type undertakings. See, e.g., Consol. Aluminum Corp. v. Bank of Va., 704 F.2d 136 (4th Cir. 1983) (discussing the power to issue undertakings and issues regarding formality).

33. The UN LC Convention opened for signature in December 1995 by the U.N. General Assembly; it was adopted by resolution on 26 January 1996 at its fiftieth session; and it was signed by seven nations, including the United States, which signed on 11 December 1997. UN LC Convention, supra note 4. It went into effect on 1 January 2000 and has been adopted by Belarus, Ecuador, El Salvador, Gabon, Kuwait, Liberia, Panama, and Tunisia. The Convention has been signed but not ratified by the United States of America as of 1 January 2014. The UN LC Convention was drafted by the United Nations Commission on International Trade Law (UNCITRAL) in the six official languages of the UN. For the text of the UN LC Convention and a list of the countries which have ratified the Convention, see www.uncitral.org. The text and explanatory note are also reprinted in LC RULES & LAWS, supra note 3.

34. See Revised U.C.C. § 5; LC RULES & LAWS, supra note 3.
the Chinese Supreme Court rules regarding letters of credit. These statutes or rules were formulated in light of letter of credit practice and compliment it.

Apart from these rules, however, LC law consists of judge-made pronouncements, which are non-systematic at best. Although the common law recognized at an early point in time the importance of a statutory formulation for a subject as complex as commercial paper in the UK Bills of Exchange Act in 1882, many common law jurisdictions (including England) have failed to do so for a subject far more complex—namely, LCs. Even less understandably, the civil law jurisdictions have no statutes for LCs. The result is a series of decisions both in common and civil law jurisdictions, which are of mixed value at best. As indicated, even where the result is proper, the rationale explaining it may not be.

5. Letter of Credit Practice

What constitutes sound LC practice is a fairly complex question. There are, of course, articulated rules of practice; namely, the Uniform Customs and Practice for Documentary Credits (UCP600), the International


36. The current version of the UCP600 became effective 1 July 2007 and was promulgated by the Commission on Banking Technique & Practice of the International Chamber of Commerce (ICC Banking Commission). See generally UCP600, supra note 4. For studies of the UCP600, see UCP600 COMMENTARY, supra note 19; James Byrne, THE COMPARISON OF UCP600 & UCP500 (2007); COMMENTARY ON UCP600, supra note 9. Useful articles include James Byrne & Lee H. Davis, New Rules for Commercial Letters of Credit Under UCP600, 39 UCC L.J. 3 (2007); E.P. Ellinger, The UCP-500: Considering A New Revision, 2004 LLOYD’S MAR. & COM. L. Q. 30 (2004). Prior versions were issued in 1933 (UCP82), 1951 (UCP151), 1962 (UCP222), 1974 (UCP290), 1983 (UCP400), and 1993 (UCP500). The official text is the English text. UCP600, reprinted in LC RULES & LAWS, supra note 3, at 1. Although UCP600 has been or will be translated into virtually every language in which international commerce is conducted, the only official translation is French. Id. Therefore, care must be taken with translations of the official English version as they are only as good as the person or persons translating them and the review process instituted by the various ICC national committees. Id. For studies in the evolution of the UCP, see James E. Byrne, Ten Major Stages In The Evolution of Letter of Credit Practice, DOCUMENTARY CREDIT WORLD 28 (Nov./Dec. 2003); Dan Taylor, The History of the UCP, DOCUMENTARY CREDIT WORLD 11 (Dec. 1999). Mr. Taylor has usefully collected all prior versions of the UCP into one volume. DAN TAYLOR, THE COMPLETE UCP: UNIFORM CUSTOMS AND PRACTICE FOR DOCUMENTARY CREDITS: TEXTS, RULES
Standby Practices (ISP98), and the Uniform Rules for Demand Guarantees (URDG 758). In addition, there are a host of subsidiary articulations of practice including most notably the International Standard Banking Practices (ISBP 2013). These attempts to articulate standard international LC practice largely emanate from the Commission on Banking Technique and Practice of the International Chamber of Commerce. They are not written by lawyers or for lawyers and have


37. The International Standby Practices (ISP98) was completed in 1998. The text was endorsed by BAFT/IFSA (formerly the U.S. Council on International Banking), the United Nations Commission on International Trade Law, and by the International Chamber of Commerce in 1998, and became effective on 1 January 1999. ISP98 is published as ICC Publication No. 590 and is generally cited as ISP98 (ICC No. 590). ISP98, supra note 4. The rules are explained in THE OFFICIAL COMMENTARY ON THE INTERNATIONAL STANDBY PRACTICES, supra note 20. The ISP98 has been supplemented by the ISP98 Model Forms. The ISP98 Model Forms are attached as Appendix C. They may also be found online at www.iiblp.org/ISPForms. Additional information on the text of the ISP98 and educational tools may be obtained from the Institute of International Banking Law & Practice, Inc., P.O. Box 2235, Montgomery Village, MD 20886 or at http://www.iiblp.org. The full text of ISP98 has been reprinted in LC RULES & LAWS, supra note 3.

38. URDG 758, supra note 4; see generally DR. GEORGES AFFAKI & SIR ROY GOODE, GUIDE TO ICC RULES FOR DEMAND GUARANTEES URDG 758 (2011); “The URDG 758 Compared with ISP98 and UCP600: Part Three of the CSGP Training Program” (Institute of International Banking Law & Practice CD-ROM rel. 2013).

39. At its May 2000 meeting the Commission on Banking Technique and Practice of the International Chamber of Commerce (ICC Banking Commission) established a task force to document international standard banking practice for the examination of documents presented under documentary credits issued subject to the UCP. The ICC’s International Standard Banking Practice (ISBP) for the Examination of Documents under Documentary Credits complements the UCP500, filling in gaps and explaining the practices that underline UCP500. INTERNATIONAL CHAMBER OF COMMERCE, INTERNATIONAL STANDARD BANKING PRACTICE FOR THE EXAMINATION OF DOCUMENTS UNDER DOCUMENTARY CREDITS (2003); see Uniform Customs & Practice for Documentary Credits, Int’l Chamber of Comm., Publ’n No. 500 art. 2 (Jan 1, 1994) [hereinafter UCP500]. It is a statement of “standard banking practice” referenced in UCP500 Article 13(a) Sentence 2. The ISBP is based on ICC Banking Commission Opinions and Decisions, and its understanding of the practices reflected in them. To complete it, practices were compiled from some 39 ICC national committees and a substantial number of individual banks. It was an attempt to provide an international formulation to various national statements of practice, most notably the Standard Practice for the Examination of Documents promulgated by IFSA with the American Bankers Association. This ISBP was aligned with the UCP600 in 2007 (ISBP 2007) and extensively updated as ISBP 2013. See INTERNATIONAL CHAMBER OF COMMERCE, INTERNATIONAL STANDARD BANKING PRACTICE FOR THE EXAMINATION OF DOCUMENTS UNDER DOCUMENTARY CREDITS (2007), reprinted in LC RULES AND LAWS, supra note 3, at 161; INTERNATIONAL CHAMBER OF COMMERCE, INTERNATIONAL STANDARD BANKING PRACTICE FOR THE EXAMINATION OF DOCUMENTS UNDER UCP 600 (2013), reprinted in LC RULES AND LAWS, supra note 3, at 101.
occasioned considerable difficulty when courts have attempted to interpret them as statutes.40

F. Approach to Teaching

In the absence of a sophisticated conceptual model of teaching methodology for law schools, this paper distinguishes (i) a lecture-based approach, with or without tutorial session; (ii) a casebook approach; (iii) a litigation problem-oriented approach; and (iv) a transactional approach. For clarification purposes and understanding these following teaching approaches are understood and classified as:

Lecture-Based Approach. Lecture is understood to consist of a monoline presentation by the instructor with or without the possibility of questions that attempts to set forth a systematic exposition of the subject matter. It is my experience that pure lecture has very limited effect because it is difficult to determine the level of comprehension and is only effective as a means of summarizing material once it is apparent that the students have mastered it.

Casebook Approach. A casebook approach is understood to consist of using reported legal decisions as a platform on which to teach involving a series of oral questions designed to elicit an understanding of the decision and its theoretical underpinnings. It is my experience that this method is of limited value with non common law jurisdictions and that its focus for common law students is too narrow, in part because of the lack of a transactional appreciation of the underlying transactions.

Litigation Problem-Oriented Approach. A litigation problem-oriented approach is understood to consist of designed problems intended to systematically lead the students to resolve legal issues related to ligation through a series of situations that will require them to master the terminology and legal obligations involved and to apply them in a practical setting to resolve problems in a principled manner.

Transactional Approach. A transaction-oriented approach is understood to consist of problems related to resolving client needs by suggesting various solutions and drafting to implement them.

Both the litigation and transactional approaches require considerable instructional engineering and flexibility in execution depending on the

40. The ICC Banking Commission regularly issues opinions interpreting the UCP and addressing questions raised by its regional committees. They are collected regularly by ICC Publishing. See, e.g., INTERNATIONAL CHAMBER OF COMMERCE, ICC BANKING COMMISSION COLLECTED OPINIONS 1995–2001 (Gary Collyer & Ron Katz eds., 2002).
circumstances in the classroom. Typically, both approaches involve having students attempt to resolve the various problems, often in a context in which they must justify their position against those held by parties reflecting divergent interests.

II. METHODOLOGY FOR TEACHING LETTERS OF CREDIT: A TRANSACTIONAL APPROACH

Given that other more traditional studies of transactional law are inappropriate for the teaching of transactional law for the reasons discussed above, a better alternative is possible.

A. Preferred Approach

The preferred approach for teaching this material is a combination of the three forms identified here with primary emphasis on the problem-oriented approach. A modified version of what is described here as the casebook approach (based on thorough questioning) is used to assure student familiarity with essential definitions and terms of art (but, generally, not using assigned case reports). The problem-oriented approach is used for the bulk of the class sessions, ideally in settings in which students explain their positions, interact with opposing positions in a litigation setting or seek accommodation in a transactional setting with other parties. Lecture is used to summarize material at the conclusion of a session where it is apparent that the students have grasped the principles intended to be identified in order to reinforce the lesson. A modified version is interspersed throughout the class session where it is essential to redirect fruitless discussions or misdirection.

B. Discussions

Permitting students to discuss the issues among themselves during the class has proven helpful. Taking a break during a difficult point for the students to engage in side conversations can be useful for them to regroup and then raise more focused questions. This method is especially helpful where the students’ first language is not English. In this case, it can be helpful for the students to engage in discussions among themselves in their own language. The discussions can either clarify points that are not fully grasped or to enable one of the students whose English is better to formulate questions in English for those not able to do so. These comments would not exclude online discussions using vehicles such as TWEN but live interaction in a monitored setting has considerable advantages.
C. Two Cautionary Observations for Instructors

It is a challenge for instructors to refrain from intervening in problem solving exercises. However, if the students are to learn to apply their understanding to the resolution of problems, they must be allowed room to make mistakes and the freedom to conclude that they have made a mistake either by following their mistake to its ultimate consequence or with the assistance of classmates. Therefore, the instructor's best contribution to these exercises is not to speak or merely to ensure that the discussion flows evenly with all students involved.

There are times when silence can be golden. There is nothing wrong with silence in response to a question. Let the students work through the question. Many instructors fear silence and believe that they must fill any such void. Doing so, however, will teach the students that they need not think since the answer will be forthcoming if they only remain silent.

D. Assessment

The focus of the assessment of students used in these courses is not to determine whether basic terminology has been mastered or whether basic principles can be repeated. Mastery of these basics is assumed. What is intended to be tested is the understanding of these principles at a deeper level. This understanding is measured by testing the ability of the student to take basic principles and apply them to situations not discussed in class or the readings. All questions are in the context of a factual problem.

An example of such a question would be a factual setting in which the beneficiary has committed letter of credit fraud, but the transferable credit has been duly transferred to a transferee beneficiary who has drawn on the LC. The issue is whether the doctrine of independence applies to the due transfer of a transferable credit and whether the transferee is a protected person, thus constituting an exception to the LC fraud and abuse exception to the independence principle. Of course, the problem set forth in the examination would not be described in a conclusory manner as it was here but the various facts would have been explained, leaving the student to determine the issues, identify and express them, and to resolve them.

E. Forum and Governing Law

Careful thought must be given to the applicable law and forum for any problem. This decision will affect the significance of judge-made law in resolving the problem. Of course, a decision about judge-made law will be affected by the location where the course is being taught. However, students should be given the opportunity to explore at least one of the statutory schemes even where there is no applicable statutory scheme. The
UN LC Convention provides a useful platform for such an exercise.

III. SUGGESTED COURSE OUTLINES, METHODOLOGY, STRUCTURE, AND EXAMPLES

The principles discussed here would also apply to treatment of LCs in the context of other traditional commercial law courses such as sales or commercial paper/negotiable instruments, in one or two classes. In such a setting, the temptation is to focus on transmitting information to be recalled rather than on interiorization of principles necessary for problem solving due in large part to time limitations. This condensing manifests itself on two levels: by cramming facts and data in a written discourse in the text and by pure lecture in the classroom.

A. Prerequisites and Limited Coverage

The essential starting point for substantive areas of LC law is student understanding of the terms being used and an appreciation of the transactional or litigation context in which they unfold. Considerable work must be done to develop the contexts for these problems. Sample problems are explored further in following text.

While it is valuable for students to have some real world background in business, there are no essential prerequisite courses for this course, except that it is assumed that the course would not be offered to students in their initial year of legal or business studies. Contracts, or the law of volitional obligations, would be useful if the students understood third party debt obligations (suretyship or accessory undertakings), but this topic is rarely covered adequately in such courses. A course in the sale of goods may provide insights into the legal background for sales transactions, but it is my experience that any treatment of the payment obligation by means of letters of credit often causes more difficulties than benefits.

It also is assumed that no law school course will enable the student to obtain mastery of the entire field. The choice is between seeking a superficial mastery of large quantities of information and focusing on selected areas of concentration in which the student can be expected to gain some insight and understanding. The approach taken in this paper and the courses that it reflects is the latter choice. Therefore, it is necessary to identify discrete areas that can be grasped in the time available and that will yield significant insights into the subject. Even for these areas, however, it

41. These reflections assume that at least one semester hour (approximately 15 class hours) is devoted chiefly to letters of credit either as the only topic being taught or as a unit in a commercial transactional law course.
is necessary to select discrete problems that are typical and afford a useful insight.

B. Factors in Selecting the Areas Around Which the Problems Are Focused

The selected areas should be: (i) transaction—matters which involve the type of work that is done on a regular basis for clients with respect to drafting contracts, forms and other matters; (ii) litigation—issues that arise regularly and offer arguments from various perspectives; (iii) drafting of practice rules and related policy issues—issues that require in-depth appreciation of the various perspectives involved; and (iv) regulatory issues—questions of safety and soundness.

C. Materials

The most significant problem in creating a course is providing materials for the students. The problems include obtaining access to practice rules, statutes and similar materials, reported cases, and practical problems. I have developed materials for these courses. My students are required to have: (i) the texts of the practice rules and laws; (ii) a textbook containing problems, excerpts of texts of selected cases, and an outline of the course; and (iii) the ISP98 Model Forms. As indicated, it is not possible to understand LC law without thorough familiarity with the practice rules, meaning that the students must have their text. Because of the predatory copyright and pricing practices of the ICC, the Institute of International Banking Law & Practice (IIBLP) has collected the important texts into LC Rules & Laws: Critical Texts and made them currently available at USD 59.00, a price which is one quarter of what it would cost to purchase them individually, and more than half of the price of this book consists of royalties. The textbooks differ in that one is focused on LCs generally while the other focuses on standbys and demand guarantees. In addition, the students should have resources available to them in the school library.

D. Examples of Practice Problems

The following areas have been selected for development of practice problems: (1) independence principle versus dependent undertakings; (2)

---

42. The list is set forth in Appendix A.
43. IIBLP, which owns the copyright to ISP98, was forced to charge for its rules in order to obtain ICC endorsement but licenses the text to teachers without charge or provides pamphlets of ISP98 at cost.
44. An annotated bibliography of these materials is contained in Appendix A.
rules and laws; (3) obligations; (4) compliance with the terms and conditions of the undertaking; (5) drafting a clause in an independent undertaking; (6) counter-standby or counter-guarantee practice and issues which arise with respect to it; (7) LC fraud or abuse; and (8) an example of an assessment (test) based on the application of the material to public policy. The rationale behind the choice of each area is explained with respect to each area below.

The selected areas represent examples that have been used previously. They are changed in the courses from time to time, based on developments in the field. Whenever possible, I try to draw on current issues being debated in the evolution of doctrine in LC law and practice. For example, currently there is considerable interest in automatic extension of the expiry date of a LC-type undertaking and the automatic reduction of the amount available, which is reflected in two of the exercises below. Fifteen years ago, the issue would have been originality of documents and applicable rules and case law. That problem is now basically resolved and the issue is only of historical interest. An issue attracting attention and that is likely to be reflected in the next iteration of the course is how to handle the reinstatement of a LC that has expired, an issue on which there is no consensus.

**Example 1: Independent Undertakings.** Analysis of LC practice: the independence of an undertaking.

**The Assignment.** Classifying the text of an undertaking drawn from a reported case and redrafting it to ensure that it will be classified as an independent undertaking.

**Significance of the Topic.** Apart from the general importance of independence, a not insignificant number of cases are reported annually involving sophisticated parties and large sums in which it is not clear whether the undertaking is dependent or independent. Most of these cases relate to demand guarantees whose distinction from dependent (true) guarantees is often blurred. Considering these cases forces the student to decide what independence signifies, when it is present, and why.

**The Platform.** The materials contain the text of several undertakings from notable cases. The decisions are not linked to the texts, and some of the decisions appear later in the materials. Valid arguments can be made for concluding that the texts are either dependent or independent. There is no obviously correct answer based on the texts.

---

45. See James E. Byrne, The Original Documents Controversy: From Glencore to the ICC Decision 1–33 (Christopher S. Byrnes et al. eds., 1st ed. 1999).
Classroom Approach. Students are asked to determine whether or not a particular text is dependent or independent and justify their choice. They are then asked to compare their evaluation with that of the courts. They are then asked to revise the undertaking to make it unambiguously independent (or dependent) and, only after doing so, to compare the text with ISP98 Model Form 1 (Model Standby Incorporating Annexed Form of Payment Demand with Standby). The attempt to fix the text can alternatively be assigned before class.

Instructional Goals. It is hoped that the students will come to appreciate the importance of independence, the difference between it and suretyship, of drafting (good and bad and comparing the two), of classification, of using and relying on practice rules for independent undertakings, of presumptions in ambiguous situations, the problem of non documentary conditions, of clarity regarding the intention of a client, and of the elements of independence. They are also invited to consider whether independence is a question of drafting or status.

Appendices. Appendix B contains an undertaking from an English case, Marubeni Hong Kong and South China Ltd v. Government of Mongolia [2005] EWCA (Civ) 395, 2005 All E.R. 117, and Appendix C contains ISP98 Model Form 1.

Example 2: Law & Practice. Drafting a Practice Rule.

The Assignment. Formulating a practice rule for automatic extension clauses.

Significance of the Topic. Practice rules are critical to the understanding of letter of credit practice and letter of credit law. However, their quality is uneven. ISP98 represents the most tightly drafted set of practice rules and UCP600 the most porous. It is essential that students appreciate the difficulty of interpreting and applying practice rules.

The Platform. One of the areas not codified in detail in current practice rules is the automatic extension clause. Such clauses have considerable advantages in that they permit regular reevaluation of the credit decision for long-term undertakings, usually on an annual basis. There are, however, considerable challenges coupled with such clauses. Forcing students to attempt to draft a rule forces them to confront their own inadequacies as drafters. For convenience, I ask students to draft a new rule for ISP98 because it already deals with one preliminary issue—namely, that such a provision is not an “amendment” requiring the consent of the beneficiary—and so that they can concentrate on other more important doctrinal and technical issues.

A variation on this approach would be to start by asking the students to
draft a revision of The Official Commentary on the International Standby Practices on ISP98 Rule 2.06 (When an Amendment is Authorised and Binding), which contains the provisions explaining the effect of an automatic amendment, and to require them to draft a new rule in a second class.

An alternative approach would be to take a specific rule and require students to critique it. One obvious example is the inadequate definition of “Negotiation” in UCP600 Article 2 (Definitions), which incorrectly links the definition to the presentation being complying. This problem surfaced in a recent Hong Kong decision, China New Era Int’l Ltd. v. Bank of China (Hong Kong) Ltd., [2009] HKCU 2012 (C.F.I.). My approach has been to provide the facts of the case but not the decision and require the students to analyze the problem.

Classroom Approach. It is expected that students will circulate their clauses prior to class, and specific students are assigned to critique specific clauses.

Instructional Goals. The goal is to introduce an element of humility before the reality of LC practice and business needs. The students have no basis for drafting a practice rule without understanding the practice and the problems it entails. In my experience, they do not understand that practice rules must proceed from the comprehension of the practices being ordered. Only by taking what is typically a technically sound draft rule can this point be brought home to them forcefully.

Appendices. Appendix D contains a recent assignment reflecting a two part exercise that involves revising The Official Commentary on the International Standby Practices and then revising ISP98 itself.

Example 3: Obligations.

The Assignment. Students are given a problem drawn from LC practice with ramifications for the obligation of various players and asked to sort it out with a view to pending litigation.

Significance of the Topic. A necessary prerequisite to understanding LCs is understanding the undertakings made by various entities.

The Platform. Here, the platform is a problem based on practice. Depending on the focus of the course, the problem could be drawn from so-called silent confirmations, the obligation of negotiating banks that negotiate but seek to recover the proceeds from the beneficiary when the issuer refuses on the basis of alleged discrepancies, or the obligation of a confirming bank when the beneficiary bypasses the confirmer and presents documents directly to the issuer.

An alternative exercise could be based on the role of an advising bank to
which documents are presented on the expiration date and forwarded to the issuer or confirmer on that date but received after the expiration date.

**Classroom Approach.** Students are given the problem in advance and required to prepare and circulate brief memos to a senior partner assessing the problem and courses of action. They are given different clients, typically an applicant, issuer, nominated bank, and beneficiary. In class, they are required to discuss their positions.

**Instructional Goals.** The goal is to provide students with an appreciation of the obligations of the various players and their role in practice, the relative practice rules and their differences, and statutory provisions that might affect these obligations.

**Example 4: Compliance.**

**The Assignment.** Students are provided with the text of a letter of credit-type undertaking, documents presented under it, and a notice of refusal. They are given various persons as clients, namely an issuer, applicant, beneficiary, and possibly a nominated bank. The discrepancy is technical, that is: (i) omitting the number of the letter of credit or missing a number or letter in it; (ii) omitting or misstating some detail from the description of the goods that is not germane to the description of the goods and extraneous to the particular document (such as shipping information or addresses) and its role in the LC transaction; or (iii) omitting required information such as the LC number or inserting incorrect extraneous information on a document that has no bearing on its role in the LC. Applicable rules may have bearing on this problem and they will be indicated in the undertaking.

**Significance of the Topic.** A significant number of reported decisions deal with problems regarding the compliance of presented documents with the terms and conditions of the undertaking. Misunderstanding the notion of "strict compliance" (which is a legal term and not one contained in any of the practice rules), courts and attorneys often resort to the mindless notion of literal replication which neither reflects actual LC practice, the practice rules, or common sense.

**The Platform.** The problem and legal memos addressing it can proceed from the different perspectives of various clients. The problem could involve stages, starting with the course of action of the confirmer or negotiating bank (if there is one) and addressing the problems that arise when a notion of refusal is given for the issuer, the beneficiary, and the applicant. The notice of refusal is deliberately drafted inadequately but students’ attention is not drawn to this point until the classroom exercise is well underway.
Classroom Approach. Start with a discussion of the merits of the presentation, namely does it comply and why, and then to move on to the question of whether the notice of refusal is adequate and, if not, the consequences of its inadequacy.

Instructional Goals. One goal is to help students deal with problems caused by pending litigation or that arise transactionally. Also, the problem forces students to see a problem from the perspective of various parties. It forces the students to face the inadequacy of the so-called “strict compliance” approach and to take a more nuanced approach to the problems caused by minor typographical errors that are extraneous to the role of an otherwise complying document in a letter of credit transaction. The problem also forces students to appreciate the importance of provisions in an agreement between the issuer/guarantor and the applicant dealing with such issues.

Example 5: Drafting an Automatic Extension Clause.

The Assignment. Students are given a factual problem and asked to draft an automatic extension clause for a letter of credit which is to be circulated before class.

Significance of the Topic. The topic focuses on the significance of the processes involved in drafting and the need for interaction between the parties to reach a consensus. Automatic extension clauses are essential to modern letter of credit practice since it is neither safe nor sound for banks to make long term commitments without regular reassessment of the credit standing of the applicant. Such clauses are also highly problematic, however. To name only one issue, should a notice of non-extension be effective when sent to the beneficiary or received?

The Platform. Here, the platform is a factual problem in which a construction company requires a performance standby or demand guarantee for 10 years related to a USD 50 million hydroelectric project in another country for a government-controlled entity. The focus on the issue is whether the bank will or can issue such an undertaking for that length of time and the alternatives.

Classroom Approach. First, the students are invited to comment on the various draft clauses which are projected on a screen.

Second, students are required to take the role of the applicant, the beneficiary, and the applicant’s bank with respect to a transaction for a period of ten years. They are required to consider the various issues involved in such an undertaking and how it is that the relative risks can be mitigated. The optimal solution in such a context apparently is a limited duration of an expiration date with an automatic extension clause coupled
with notice of non-extension and the ability to draw in the event that notice is given. The students are forced to discuss, negotiate and consider the various alternatives as well as the issues involved in the formulation of such a clause such as to whom notice is given, addresses, whether it is to be sent or received, and similar issues.

**Instructional Goals.** This exercise should be linked with the exercises on drafting rule for automatic extension clauses but need not immediately follow it. The exercise should demonstrate the inadequacy of practice rules to solve certain problems. At some point, the students’ attention should be directed to ISP98 Model Form 2 (Model Standby Providing for Extension and Incorporating Annexed Form of Payment Demand with Alternative Non-Extension Statement) whose provisions and endnotes detail many of these issues. The dramatization forces students to identify with the various perspectives of their clients and to come to a resolution with which the various parties can live or to face the consequences of failure to do so. Any solution must provide adequate protection to the issuer/guarantor and to the beneficiary.

**Note:** Three of these exercises involve automatic extension clauses, namely (and in this order) drafting a comment in the official commentary on a practice rule, drafting a proposed revision of the rule, drafting a clause for a standby letter of credit, and negotiating the terms of the clause. These exercises are deliberately structured to be backwards. It is absurd to attempt to draft rules without understanding the issues that arise in practice and difficult to draft a clause for a standby without having a sense of what is possible. In addition, the exercises are designed to illustrate the limitations of rulemaking. Some things are better handled by drafting or model clauses than rules.

**Example 6: Counter Undertakings and related issues and problems.**

**The Assignment.** Students utilize the exercise involving drafting an automatic extension clause (Example 5), requiring issuance of a counter undertaking requesting issuance of a local bank undertaking in favor of the government agency ordering construction of the hydro-electric plant. The facts will be drawn from the problem in Exercise 5.

**Significance of the Topic.** Counter undertakings have assumed considerable importance in letter of credit practice.

**The Platform.** Students are requested to deal with the consequences of closure of the local bank on a business day which is also the expiration day of the local bank undertaking on the counter undertaking.

Alternatively, or in conjunction with this exercise, they can be asked to deal with forwarding documents presented under the local undertaking in
the context of an otherwise complying presentation under the counter undertaking.

Classroom Approach. Students are assigned roles in advance and asked (separately or together as a group) to draft a counter undertaking containing the text of the requested local undertaking or to draft a reply to the request on the part of the local bank. The class is used to discuss the issues.

Instructional Goals. To acquaint students with counter undertakings and the different problems and issues that arise under them.

Appendices. Appendix E contains a recent example of an assignment.

Example 7: Letter of Credit Fraud or Abuse.

The Assignment. Students are given a factual problem involving delivery of goods that had little or no economic value. The students are given various scenarios involving the beneficiary and involving nominated banks and a counter undertaking.

Significance of the Topic. An example is used in the context of counter-standbys or counter-guarantees coupled with several cases which speak to these issues. The focus of the exercise is the litigation postures of the various parties. Students are assigned to represent the local beneficiary, the local bank, the issuer of the counter-standby or counter-guarantee, and the applicant. They are required to indicate in a memo their approach to various issues including jurisdiction, law, and the substantive issues involved with respect to fraud and the role of protected persons. In the hypothetical that is set for them, it is likely that the local beneficiary has committed fraud and the question is whether or not a demand by the local bank which is the beneficiary of the counter-undertaking is to be honored where the local bank has honored its local obligation.

The Platform. The factual problem with various scenarios calling for memos on behalf of various clients.

Alternative: Use the problem from Example 6 and indicate a drawing without basis by the local beneficiary coupled with a complying drawing by the local bank on the counter standby. This problem would force the students to address whether the local undertaking was separately independent from the counter undertaking.

Classroom Approach. Require the students to submit to mediation on behalf of their clients and permit them to interact with each other's arguments.

Instructional Goals. Understanding the various degrees of conduct that constitute Letter of Credit Fraud or Abuse and exceptions in favor or protected persons.
Appendices. Appendix F contains a recent assignment.

Example 8: Assessment based on application of principles to a public policy question.

The Assignment. Students are given a take-home examination limited by a time deadline and the number of words permitted. The examination asks students to address the following question: “The Peoples’ Supreme Court is drafting rules [under Chinese organic law, legally binding on all Chinese courts] for standby letters of credit. Assume that you are asked for advice. What suggestions do you have?”

Significance of the Topic. Questions of public policy and statutory drafting. In a course to Chinese graduate students, they were required for the final examination to draft a memo directed to the People’s Supreme Court indicating issues to be considered in drafting rules for standby letters of credit. It should be noted that the People’s Supreme Court has drafted rules applicable to commercial letters of credit and is bogged down in theoretical and substantive questions with respect to demand guarantees which are confused with dependent guarantees for which there is legislation in China (as in many countries). The question is in the minds of the drafters whether standbys should be linked with commercial letters of credit or with demand guarantees which are (mistakenly) classified with dependent guarantees. The exercise tests the ability of the student to grasp substantive issues as well as to provide a sound resolution of the problem.

Basis for the Assessment. Whether the students able to provide a coherent and principled resolution to the various issues including classification.
APPENDIX A

Bibliography:

**Student Materials:**

JAMES E. BYRNE ed., *LC RULES & LAWS: CRITICAL TEXTS FOR INDEPENDENT UNDERTAKINGS* (6th ed. 2013) (377 pages/paperback) (IIBLP). ISBN 978-1-888870-63-3. [Contains the texts of all relevant practice rules, the UN LC Convention & Secretariat’s Explanatory Note, US Revised UCC Article 5, translations of the Chinese Peoples’ Supreme Court rules, the ISBP (2007), and other important resources. Ability to access these texts is essential for the study of letters of credit.]

*ISP98 Model Forms* (2012) (IIBLP). URL: www.iiblp.org/ISP98Forms. Also available in UBS with comments and index: [IIBLB]. [Eight forms developed for use with ISP98, including explanatory endnotes containing alternative clauses intended as a starting point for applicants and beneficiaries to draft ISP98 standbys.]


**Resources that Should be Available to Students in an Academic Library:**

1. Commercial LCs & UCP:

distorted UCP provisions regarding original, detailing the response of the letter of credit community and its effect on courts.]

JAMES E. BYRNE ET AL., UCP600: AN ANALYTICAL COMMENTARY (2010) (1462 pages/hardback) (IIBLP). ISBN 978-1-888870-47-3 [Definitive analysis of the UCP, organized on an article by article basis but tracing the genesis of each article to the original UCP82 (1933), referencing all relevant ICC Banking Commission opinions, the ISBP, and relevant judicial decisions. Essential for any serious study of the UCP and commercial letter of credit practice.]


DAN TAYLOR, THE COMPLETE UCP (2008) (249 pages/paperback) (ICC). ISBN 978-92-842-0032-0 [Contains the text of all versions of the Uniform Customs and Practice for Documentary Credits, including versions prior to its adoption by the ICC.]

2. Standby Letters of Credit Practice:


3. Demand Guarantee Problem:


4. LC Law:

summaries of all reported cases and texts of non-reported or translated cases, practice and other developments. Cumulatively indexed.]

JAMES E. BYRNE, HAWKLAND UNIFORM COMMERCIAL CODE SERIES, VOLUME 6B, [REV.] ARTICLE 5 LETTERS OF CREDIT (Frederick H. Miller ed.) (unit of multi-volume treatise on Uniform Commercial Code/750 pages/hardback) (West Group Pub. 2009) [Article by article analysis of US Revised UCC Article 5 (Letters of Credit) containing the text of the statute, prior statutory versions, an analysis of the issues inherent in each section drawing on all case law and select case law under prior version, and comparing UN LC Convention, Chinese LC Rules, and relevant practice rules.]


APPENDIX B

Marubeni Hong Kong and South China Ltd v Government of Mongolia
Abstracted by James G. BARNES 46

Topics: Guaranty; Independent Guarantee; Surety; Independent, Dependent;

Type of Lawsuit: Beneficiary sued issuing bank for wrongful dishonor

Parties: Claimant/Beneficiary/Seller– Marubeni Hong Kong and South China Ltd
Applicant/Buyer– Buyan Holding Co Ltd
Defendant/Issuer– Mongolian Government

Underlying Transaction: Purchase of equipment for cashmere processing plant.

Undertaking: The text of the undertaking issued by the Finance Ministry of Mongolia is reproduced below.

Decision: The Court of Appeals (Civil Division), Waler, Carnwath, LJJ, and Sir Martin Nourse, J.J., dismissed an appeal and approved the decision of Creswell, J., that an undertaking issued by the Finance Ministry of Mongolia was binding on the issuer as a secondary obligation and not as an independent obligation

Rationale: An undertaking issued by a non-bank is presumed not to be independent.

Factual Summary: The beneficiary sold equipment and materials for a cashmere processing plant in Mongolia under a deferred payment contract for US$18,511,670. Disputes between the seller and buyer resulted in several reschedulings of the payment obligations of the buyer. Following non payment of most of the rescheduled amounts, seller demanded

GOING BEYOND THE FOUR CORNERS

payment of US$13,796,556 plus interest under the undertaking issued by the Finance Ministry of Mongolia, reproduced below. The defendant issuer refused to pay on the grounds that the reschedulings materially changed the underlying obligation with the effect of discharging its obligations under its undertaking. The claimant beneficiary sought to eliminate that defense by characterizing the undertaking as "independent".

**Legal Analysis:** The English Court of Appeal held that the undertaking issued by the Finance Ministry of Mongolia, reproduced below, was not an independent undertaking. The court emphasized that the issuer was not a bank and held that only bank undertakings to pay on demand enjoy a presumption of independence, such that they are enforceable as first demand guarantees or performance bonds that are analogous to letters of credit. The court then determined that neither the text of the undertaking nor any other factor overcame the presumption of non-independence of the non-bank undertaking in this case.

For procedural reasons the court did not consider any other grounds for treating the undertaking as unaffected by reschedulings of the underlying payment obligations.

**Comment by James G. BARNES:**

1. Determining which undertakings qualify as independent and which do not can be difficult, particularly if there is no clear statutory or case law definition of independence.

2. US law provides a clear framework for identifying undertakings that qualify as independent. The Restatement Third, Suretyship and Guaranty, broadly defines guarantee and suretyship relationships and expressly excludes letters of credit from the definition. The Uniform Commercial Code defines letters of credit, essentially as undertakings to pay against the presentation of documents, so as to exclude from suretyship law commercial letters of credit, standby letters of credit, and independent guarantees, not (though undertakings issued subject to UCP500, ISP98, and URDG, as well as Article 5 of the UCC itself. A feature of the law and practice applicable to such undertakings is that nondocumentary conditions, if any are included in the undertaking, must be disregarded. A consequence of this interpretive rule, as well as the statutory definition of "letter of credit", is that an undertaking containing nondocumentary
conditions that are essential to the undertaking may not qualify as a letter of credit, in which case they would not be excluded from the definition of suretyship. Fortunately, the divide between independent and non-independent undertakings is not frequently tested in the US, and US case law applying UCC Article 5 in this regard is generally good.

3. Outside the US there is much more testing of the divide between independent and non-independent undertakings both in practice and in the courts. There is more inclination to draft undertakings that are intended to be independent and then to add recitals and waivers appropriate for suretyship undertakings but not for independent undertakings. There is an understandable desire on the part of courts, and the banking industry generally, to enforce bank undertakings to pay without regard to the facts of performance or default in the underlying transaction. Accordingly, there is considerable case law outside the US treating bank undertakings as independent that are riddled with nondocumentary conditions and otherwise in a form that would not be issued by a US bank. In this case, the English court rather struggled to decide that the undertaking before it was not independent, because, had it been issued by a bank, it might have qualified under English case law precedent as independent, even though it is indefinite as to the form and substance of the demand required to be presented, its duration and amount are expressed only in terms of a defaulted underlying obligation, and it does not incorporate rules that might signify its independence and provide for disregard of nondocumentary conditions.

4. US law recognizes that ordinary guarantors may effectively waive defenses otherwise available to a secondary obligor, notably by providing in the guarantee that the beneficiary may change the underlying obligation, or release collateral, or otherwise agree to pay as if a primary obligor. It appears that English law is similar, but for procedural reasons the Court of Appeal did not address the possibility that this particular undertaking should be unaffected by a rescheduling of the underlying debt even though it did not qualify as independent.
TEXTUAL APPENDIX

The following text appeared in the report of the decision:

“To: Marubeni Hong Kong Ltd

“In consideration of your entering into the deferred payment sales contract No 258500 (hereinafter called the ‘agreement’) with Buyan Holding Co Ltd, a corporation duly organised and existing under the laws of Mongolia, with its principal office at I-40000-68-4 Ulaanbaatar, Mongolia (hereinafter called the ‘buyer’) for sales and purchase of a textile plant the contract price of which is United States dollars eighteen million eight hundred eleven thousand six hundred seventy (US$18,811,670), the undersigned Ministry of Finance of Mongolia unconditionally pledges to pay to you upon your simple demand all amounts payable under the agreement if not paid when the same becomes due (whether at stated maturity, by acceleration or otherwise) and further pledges the full and timely performance and observance by the buyer of all the terms and conditions of the agreement. Further Ministry of Finance undertakes to hold indemnify and hold you harmless from and against any cost and damage which may be incurred by or asserted against you in connection with any obligations of the buyer to pay any amount under the agreement when the same becomes due and payable (whether at stated maturity, by acceleration or otherwise) or to perform or observe any term or condition of the agreement, or in connection with any invalidity or unenforceability of or impossibility of performance of any such obligations of the buyer.

“This covenant shall come to force from the date of implementation of this agreement and remain in full force and effect until all amounts due to you by the buyer under the agreement have been paid in full and all the terms and conditions of the agreement have been fully performed and observed by the buyer.

“The Ministry of Finance hereby waives any right to require you to proceed against the buyer or against any security received from the buyer or any third party or to pursue any other remedy available to you.”

The letter also provided that: “All disputes related to this pledge shall correlate in accordance with the jurisdiction courts of England.”
APPENDIX C

ISP98 Form 1

Model Standby Incorporating Annexed Form of Payment Demand with Statement*

[name and address of beneficiary] [date of issuance]

Issuance. At the request and for the account of [name and address of applicant] ("Applicant"), we [name and address of issuer at place of issuance] ("Issuer") issue2 this irrevocable3 standby letter of credit number [reference number] ("Standby")4 in favour of [name and address of beneficiary] ("Beneficiary")5 in the maximum aggregate amount6 of [currency/amount].

Undertaking. Issuer undertakes to Beneficiary7 to pay8 Beneficiary’s demand for payment in the currency and for an amount available under this Standby9 and in the form of the Annexed Payment Demand completed as indicated10 and presented11 to Issuer at the following place for presentation: [address of place for presentation],12 on or before the expiration date.13

Expiration. The expiration date of this Standby is [date].14

[Payment. Payment against a complying presentation shall be made within 3 business days15 after presentation at the place for presentation or by wire transfer to a duly requested account of Beneficiary. An advice of such payment shall be sent to Beneficiary’s above-stated address.]16

[Drawing. Partial and multiple drawings are permitted.]17

[Reduction. Any payment made under this Standby shall reduce the amount available under it.]18

ISP98. This Standby is issued subject to the International Standby Practices 1998 (ISP98) (International Chamber of Commerce Publication No. 590).19

[Communications. Communications other than demands may be made to
Issuer by telephone, telefax, or SWIFT message, to the following: [numbers/addresses]. Beneficiary requests for amendment of this Standby, including amendment to reflect a change in Beneficiary's address, should be made to Applicant, who may then request Issuer to issue the desired amendment.\textsuperscript{20}

[Issuer's name]

[signature]

Authorized Signature

Annexed Payment Demand

[INSERT DATE]\textsuperscript{21}

[name and address of Issuer or other addressee at place of presentation as stated in standby]\textsuperscript{22}

Re: Standby Letter of Credit No. [reference number], dated [date], issued by [Issuer's name] ("Standby")\textsuperscript{23}

The undersigned Beneficiary demands payment of [INSERT CURRENCY/AMOUNT] under the Standby.\textsuperscript{24}

Beneficiary states\textsuperscript{25} that Applicant\textsuperscript{26} is obligated\textsuperscript{27} to pay to Beneficiary the amount demanded\textsuperscript{28}, which amount is due and unpaid\textsuperscript{29} under [or in connection with] the agreement\textsuperscript{30} between Beneficiary and Applicant\textsuperscript{31} titled [agreement title] and dated [date].

[Beneficiary further states that the proceeds\textsuperscript{32} from this demand will be used to satisfy\textsuperscript{33} the above-identified obligations and that Beneficiary will account to Applicant\textsuperscript{34} for any proceeds that are not so used.]

Beneficiary requests that payment be made by wire transfer to an account of Beneficiary as follows: [INSERT NAME, ADDRESS, AND ROUTING NUMBER OF BENEFICIARY'S BANK, AND NAME AND NUMBER OF BENEFICIARY'S ACCOUNT].\textsuperscript{35}
[Beneficiary’s name and address]35

By its authorized officer:

[INSERT ORIGINAL SIGNATURE]36
[INSERT TYPED/PRINTED NAME AND TITLE]

[Before the standby is issued, all text in [bold] should be completed, and optional text in [italics] should be included or deleted (or redrafted). Text in the annexed demand form preceded by “INSERT” (or other ALL CAPITALS guidance) and in [ALL CAPITALS UNDERLINED] is to be completed as indicated when the beneficiary prepares and presents a demand.]

****************************************************

* Copyright © 2012 by the Institute of International Banking Law & Practice, Inc., www.iiblp.org (“IIBLP”). Unlimited permission is hereby granted to copy and use this ISP98 form, including endnotes, for all purposes except publication for a charge to a purchaser or subscriber.

This ISP98 Form 1 model standby includes terms that ISP98 indicates should be included in a standby. It includes terms that restate other ISP98 rules for the avoidance of doubt, e.g., that the standby is irrevocable and permits partial demands. It uses words, phrases, and spellings that are used in ISP98. It also includes optional terms that are specific about when and how payment will be made.

This ISP98 Form 1 incorporates an annexed model form of payment demand that includes terms that ISP98 indicates should be included when making a presentation. This demand form also includes beneficiary statements of a type the applicant or beneficiary may desire in order to identify the underlying obligation(s) to be supported by the standby (and to be satisfied upon honour of the standby).

The annexed demand form may also be used as a precedent by a beneficiary preparing a demand to be presented under an ISP98 standby that does not specify the entire form of demand to be presented. See ISP98 Form 5 (Simplified Demand Only Standby).

This ISP98 Form 1 is intended to be self-contained and, absent special
circumstances, useable without extended reference to the text of ISP98.

The endnotes to this form include alternative and other optional terms, as well as references to relevant ISP98 rules. Other ISP98 model standby forms vary this form, e.g., by adding text and annexes (with relevant endnotes) that focus on expiration, reduction, transfer, confirmation, and counter standby support.

This form is published for educational purposes and not as legal or professional advice. Potential users should consult with their own advisers in the drafting or use of a standby letter of credit. ISP98 and letter of credit educational and training materials, including *The Official Commentary on the International Standby Practices* containing official interpretations of ISP98, are available from IIBLP at www.iiblp.org.

**Endnotes**

1. **Applicant.** As noted in ISP98 Rule 1.09(a) (Definitions), the “applicant” is the person who applies for issuance or for whose account the standby is issued. Typically, the applicant stated in the standby is the person whose underlying obligation is supported by the standby. The standby’s terms should be appropriate to support those underlying obligations, and the underlying documentation should appropriately provide for the standby and for the use of funds paid under the standby.

Where a standby is issued on the application of a correspondent bank from whom the issuer expects reimbursement, consideration should be given to an alternative clause: “At the request and for the account of [name of correspondent bank], (“Applicant”) acting at the request and for the account of its customer, [XYZ]...”. Similarly, where a standby is issued on the application of a parent company, consideration should be given to an alternative clause: “At the request and for the account of [Parent] (‘Applicant’) acting at the request and for the account of its subsidiary [name]...”.

This standby form adds “(‘Applicant’)” after the name of the applicant, and that defined term is used in the annexed model demand form. If this parenthetical definition (or the parenthetical definition for the issuer or the beneficiary) is not wanted, appropriate adjustments should be made in the standby, including in any statement required to be included with any beneficiary demand. If an adjustment is made because the applicant is not also the underlying obligor (or the beneficiary is not also the underlying obligee), then the adjustments should be made in the standby and also in
the documentation underlying the standby. See endnote 30.

Except for endnotes 1 and 30, these endnotes do not address issues that may arise where the applicant is not the underlying obligor or where there are multiple applicants.

2. Issuance. The name of the issuer and the place(s) of issuance and presentation should be indicated in the standby. The indicated place of issuance is significant in determining what law governs the issuer’s obligations. Absent an indication of the place of issuance in the standby, it may prove difficult to determine a single place of issuance, even with full knowledge of the process resulting in sending the standby to the beneficiary. This form, including endnotes, does not address the possibility, briefly addressed in ISP98 Rule 10 (Syndication/Participation), of multiple issuers or of participating interests in a single issuer’s standby facility.

Rule 2.03 (Conditions to Issuance) provides generally that a standby is issued when it leaves the issuer’s control, and Rule 3.05 (When Timely Presentation Made) allows presentation any time after issuance (and before expiry) It is customary for a standby to recite the issuance date either at the top of the undertaking or in the first paragraph of the text (or both).

3. Irrevocability. It is unnecessary to state that an ISP98 standby is irrevocable. See ISP98 Rule 1.06(a) and (b) (Nature of Standbys). However, because of the contrary rule in UCP82 (1933) until UCP500 (1993), some letter of credit users expect or require inclusion of the word “irrevocable”.

4. Name of undertaking. While this form of undertaking is named a “standby letter of credit”, the name is not determinative of its character as an undertaking within the scope of ISP98 or as an independent undertaking under applicable law. As provided in ISP98 Rule 1.01(b) (Scope and Application), it could be called an independent guarantee, bank guarantee, bond, or any other name.

5. Beneficiary. The beneficiary named in a standby is the person to whom the issuer’s obligation is owed. Typically, there is one named beneficiary of the issuer’s undertaking, who is also the obligee of the applicant’s obligation that is supported by the standby. This standby form, including endnotes, does not address issues that may arise where the named
beneficiary is not the underlying obligee or where there are multiple beneficiaries.

6. **Amount available.** A standby should expressly state the amount available under the standby. Standbys commonly add that the stated amount of a standby is the “maximum” (or “full” or “not to exceed”) “aggregate” amount. These are unnecessary additions because ISP98 Rule 3.08 (Partial Drawings & Multiple Presentations; Amount of Drawings) permits presentations for less, but not more, than the amount available under a standby.

Under ISP98 Rule 3.08(e) (Partial Drawings & Multiple Presentations; Amount of Drawings), a drawing that exceeds the amount available under the standby is discrepant. To override that rule and require the issuer to pay the full amount available under the standby against a presentation that would comply but for the “credit overdrawn” discrepancy, the following clause may be added: “If a demand exceeds the amount available, but the presentation otherwise complies, Issuer undertakes to pay the amount available.”

7. **Undertaking to the beneficiary only.** It is unnecessary to state that an issuer’s payment obligation is made “to Beneficiary”. Except as otherwise stated in the standby or mandated by applicable law, a standby that names a beneficiary and does not identify any other person as having rights under the standby obligates the issuer solely to the named beneficiary. ISP98 Rule 2.04 (Nomination) provides for the possibility that a standby nominates another person to confirm the issuer’s undertaking or otherwise to give value against the named beneficiary’s complying demand. ISP98 Rule 6 (Transfer, Assignment, and Transfer by Operation of Law) provides for the possibility that an issuer is requested to acknowledge a person claiming to be a transferee beneficiary or an assignee of standby proceeds or a successor beneficiary. ISP98 Form 4 (Model Standby Providing for Transfer and Incorporating Annexed Form of Transfer Demand) focuses on transfer of drawing rights by beneficiary demand and other standby terms affecting a claimed transferee beneficiary, assignee of standby proceeds, or successor beneficiary.

8. **Honour by payment.** An issuer may undertake to honour a letter of credit other than by sight payment. Under ISP98 Rule 2.01 (Undertaking to Honour by Issuer and Any Confirmer to Beneficiary) an issuer may undertake to honour by non-recourse negotiation (purchase) of the
documents presented or by acceptance of a time draft or incurrence of a deferred payment undertaking, followed by payment at maturity. Also, an issuer may undertake to honour by the delivery of an item of value, such as gold, in which case the issuer must be able to deliver the specified item. These other forms of honour are not covered in this form because they are much less common for standbys than honour by sight payment.

9. Presentation of standby. An issuer’s obligation is not dependent on the beneficiary’s holding or presenting the standby, unless the standby so provides. See ISP98 Rule 2.03 (Conditions to Issuance). This form, like most standbys, does not require presentation of the standby with a payment demand. Any such requirement exposes the beneficiary to the risk that a demand may be rightfully refused if the standby is lost or otherwise cannot be timely presented. It also exposes the issuer to disputes over the issuer’s receipt, handling, or return of the standby. There are other ways to avoid payment against a forged demand, e.g., by providing in the standby that payment must be made to a specified beneficiary account.

Under ISP98 Rule 3.12 (Original Standby Lost, Stolen, Mutilated, or Destroyed), an issuer is entitled to enforce a requirement that the standby be presented with a demand. However, the rule also gives an issuer considerable discretion to excuse or remedy a beneficiary’s failure to present the standby. If greater certainty is desired, then the standby could add the following or a variation: “Issuer undertakes to exercise its discretion under ISP98 Rule 3.12 to waive the requirement to present this Standby (or to replace it) against Beneficiary’s representations and indemnities (including third party indemnities deemed appropriate by Issuer) in favor of Issuer and Applicant that are reasonably satisfactory to Issuer.” The representations and indemnities should run to the applicant as well as the issuer. Although the issuer would determine what is reasonable at the time of taking any representations or indemnities, the applicant would bear the ultimate risk of payment against a forged demand.

The term “this Standby” in this ISP98 Form 1, like the term “original standby” in ISP98 Rule 3.12 (and Rule 6.03 (Conditions to Transfer)), refers to the originally signed/authenticated undertaking that evidences the issuer’s obligation. Unless the issuer sends a signed/authenticated undertaking directly to the beneficiary, it may be desirable to clarify in the standby what must or may be presented as, or in lieu of, the issuer’s undertaking in the form it left the issuer’s control. If the standby was sent by an authenticated SWIFT message from an issuing bank to an advisor,
the document to be presented would be the advisor’s signed/authenticated message to the beneficiary annexing, or reproducing the text of, the SWIFT message sent by the issuer. There may be no unique undertaking for the beneficiary to present. If, for example, a standby was sent to a beneficiary in an electronic medium, its presentation to the issuer in an electronic medium or as a paper printout would serve merely to identify the standby to be transferred.

The terms “this standby” and “original standby” do not necessarily refer also to amendments. Some standbys state that all amendments must also be presented, and some also require a statement from the beneficiary as to whether it has consented (or not) to each amendment issued by the issuer. Neither should be necessary. An issuer should be able to determine from its own records whether amendments are binding on the issuer and the beneficiary, but it may nonetheless be desirable to address the status of amendments in any standby term requiring presentation of the standby.

10. Form of payment demand. This ISP98 Form 1 standby incorporates an annexed model form of payment demand to be completed and presented by the beneficiary. Annexing the desired form of payment demand (with any desired beneficiary statement) to a standby is unnecessary but promotes the efficient use of standbys. Requiring a “draft” (or bill of exchange) drawn at sight by the beneficiary on the issuer is neither necessary nor efficient under a standby that undertakes to pay at sight.

A standby that specifies wording in an annexed form of demand is subject to ISP98 Rule 4.09(b) (Identical Wording and Quotation Marks). That subsection requires or permits the beneficiary to complete blank lines or spaces and to correct apparent typographical errors and the like. It is intended to cover practically all circumstances in which a form of beneficiary demand and statement is annexed to the standby.

If more flexibility is desired, Rule 4.09(a) should be consulted, but flexibility is better introduced by adding alternative wording to the annexed form of demand or otherwise indicating in the annexed form of demand how blank spaces may be completed. If no flexibility whatsoever is desired (e.g., because the demand or statement must be delivered to a third person in a precisely specified form), then Rule 4.09(c) should be consulted, with the understanding that it should be invoked rarely, that it requires use of the word “exact” or “identical” in the standby, and that its use may lead to unintended consequences for the issuer, applicant, or beneficiary.
The phrase "completed as indicated" assumes that the annexed form of demand adequately indicates how it is to be completed (e.g., by the inclusion of instructions and blank lines) and that it is to be dated and signed by the beneficiary. It does not add that the demand be "apparently" signed by the beneficiary or the beneficiary's "purported" representative, because such additions are more likely to confuse than clarify the allocation of risks under ISP98 and applicable law of payment or non-payment of a forged demand.

ISP98 Rule 4.08 (Demand Document Implied) requires presentation of a documentary demand for payment. ISP98 itself does not require the named beneficiary to present any beneficiary statement.

Some standbys state that they are available by "one or more demands" or by "demand(s)", rather than by "demand" in the singular. This is unnecessary for the reasons indicated in endnote 17.

11. Manner of presentation. This standby form is based on the usual practice of sending original documents, sometimes including the original standby, in a package by courier to the issuer's indicated place of presentation. Presentations by telefax and the like are prohibited unless expressly permitted in the standby or unless the beneficiary is a SWIFT participant or bank sending a demand using SWIFT or other similar authenticated means. See ISP98 Rule 3.06 (Complying Medium of Presentation). ISP98 Rule 1.09(c) (Electronic Presentations) includes defined terms that may be used in a standby that permits electronic presentation.

12. Place of Presentation. ISP98 Rule 3.01 (Complying Presentation under a Standby) provides that a standby should indicate the place, the location within that place, and the person to whom presentation should be made. ISP98 Rule 3.04 (Where and to Whom Complying Presentation Made) provides default rules. The indicated place of presentation is significant in determining whether a complying demand is timely presented.

Standbys frequently include a requirement that the presentation be addressed to the attention of the Standby Letter of Credit Department or the like, which may prove critical on a last minute presentation. Some standbys also include in the address for presentation a specific floor or
office, which, if it is not accessible to the beneficiary, may prove contentious in the case of a last minute presentation. Beneficiaries and issuers both should avoid testing the limits of such requirements.

A standby may require presentation to the issuer to be made at a place that is not the place of issuance, e.g., to and at the address of a processing agent for the issuer (which could be an affiliate or another bank). A standby may also nominate another branch or bank to receive a presentation and act on that nomination. This standby form does not include any nomination or address issues which arise from a nomination. See ISP98 Rule 2.04 (Nomination).

13. **Time of presentation.** ISP98 Rule 3.05 (When Timely Presentation Made) provides that presentation must be made before expiry on the expiration date and that a presentation after business hours is treated as made the next business day. Rule 9.04 (Time of Day of Expiration) provides that expiry occurs at the close of business at the place of presentation.

14. **Expiration.** Standbys must contain an expiration date under ISP98 Rule 9.01 (Duration of Standby) and likely also under applicable commercial law and banking regulations. This standby form is based on the common practice of stating a specific calendar date. The stated date should be set sufficiently after the underlying obligation becomes due to allow for drawing after refusal of an initial drawing. If payment of the underlying obligation may be made outside of the standby, the stated date should be set to allow also for drawing after any possible rescission of an outside payment made by an insolvent payor.

Many issuers are subject to laws, regulations, or internal policies that limit their incurrence of obligations that are indefinite or long term. A common response is to set a one year expiration date and allow for automatic annual extensions unless the issuer sends or the beneficiary receives advance notice of non-extension. ISP98 Rule 2.06(a) (When an Amendment is Authorized and Binding) makes “automatic amendments”, including extensions of the expiration date, effective without further notification or consent, if the automatic amendment is expressly stated in a standby. ISP98 Form 2 (Model Standby Providing for Extension) focuses on annual automatic extension and other alternatives to a single fixed expiration date.

The expiration date stated in a standby is not necessarily the last day on
which a complying presentation may be made under the standby. ISP98 Rules 3.13 (Expiration Date on a Non-Business Day) and 3.14 (Closure on a Business Day and Authorization of Another Reasonable Place for Presentation) extend the expiration date where it falls on a non-business day or on a day the bank is closed for any other reason.

15. **Three days to examine and pay a presentation.** ISP98 Rules 2.01(c) (Undertaking to Honour by Issuer and Any Confirmer to Beneficiary) and 5.01 (Timely Notice of Dishonour) provide for the time an issuer has to honour or dishonour and include a safe-harbor of three business days after presentation. The three day period begins on the business day following the business day of presentation. This optional standby text converts that 3-day safe harbor period in ISP98 into a timing requirement for payment of a complying presentation.

Many so-called financial standbys state a shorter period within which a complying presentation must be paid, and some also state that the shortened period also applies to the time allowed for the issuer to avoid preclusion by giving a notice of dishonour. For example, a standby payable against a simple demand to be presented by a bank beneficiary might state: “Payment of a complying presentation shall be made[, or in the case of a non-complying presentation a notice of dishonour shall be given,] on the first banking day following the banking day on which Issuer receives a presentation from Beneficiary[, if received before noon,][by SWIFT/telefax message at Issuer’s following SWIFT address/telefax number]. . .”

Some standbys permit a longer period for payment, e.g., 30 days after presentation or 10 days after a presentation is determined to comply. Lengthening the time for honour would not, without more, lengthen the timing requirements of ISP98 Rule 5.01 (Timely Notice of Dishonour) for giving a notice of dishonour or for precluding defenses under ISP98 Rule 5.03 (Failure to Give Timely Notice of Dishonour).

16. **Place and method of payment.** If a standby, including an annexed form of demand, does not state the method of payment, then an issuer may voluntarily follow the presenter’s request. ISP98 Rule 5.08 (Cover Instructions/Transmittal Letter) permits an issuer to deal with the presenter and to follow instructions accompanying a presentation. Similarly, ISP98 Rule 6.10 (Reimbursement for Payment Based on an Assignment) protects an issuer’s reimbursement rights in cases of payment to an acknowledged
assignee of standby proceeds. ISP98 Rule 2.01(e) (Undertaking to Honour by Issuer and Any Confirmer to Beneficiary) provides that honour by payment is to be made in immediately available funds. This optional standby text facilitates payment by wire transfer in response to a request duly made by the beneficiary.

Unless the standby otherwise states, an issuer is not required to pay anyone other than a beneficiary, a nominated person, or an acknowledged assignee of standby proceeds and is not required to pay anywhere other than at the place of presentation. See ISP98 Rule 6 (Transfer, Assignment, and Transfer by Operation of Law). Payment may be made at the place of presentation by sending a bank check to the order of the beneficiary or by initiating a wire transfer.

If payment by check is the sole desired method of honour, the following may be substituted: “Payment shall be made by Issuer’s check payable to Beneficiary sent to Beneficiary’s above-stated address by registered mail or [inter]nationally recognized courier or other means of receipted delivery to Beneficiary.”

If payment by wire transfer is the sole desired method of honour, the following standby text may be substituted: “Payment shall be made by wire transfer to an account of Beneficiary as follows: [name, address, and routing number of Beneficiary’s bank, and name and number of Beneficiary’s account] or to such other bank account of Beneficiary as Beneficiary may duly request of Issuer”. An issuer’s response to a beneficiary request may be affected by regulatory requirements limiting payment to a permissible account at a permissible financial institution located in a permissible country. The annexed form of demand and statement incorporated into this ISP98 Form 1 standby contains model wording for a beneficiary’s request for payment by wire transfer. Including a detailed method of payment in a standby may deter forged beneficiary demands, as well as avoid delays resulting from the issuer’s receipt of an inadequate request as to the method of payment.

No matter what a standby, demand form, or separate request for routing payment may state, applicable law, e.g., a court or government agency order, may block payment. Applicable law may also allocate the risks of loss in case of payment to the wrong person.

17. More than one drawing. It is unnecessary to state that a beneficiary
may make multiple drawings or drawings for less than the full amount available. A standby that undertakes to honour “a demand” (in the singular) does not affect the beneficiary’s right to present more than one demand under standard practice applicable to standby (and commercial) letters of credit. ISP98 Rule 3.08 (Partial Drawings & Multiple Presentations; Amount of Drawings) permits both partial and multiple drawings unless prohibited in the standby. If a standby is to be honoured once only, then the standby should state that affirmatively or, as indicated in ISP98 Rule 3.08(d), state “multiple drawings prohibited”.

18. Reduction by honour. It is unnecessary to state that the amount available under a standby is reduced by the amount of any drawing that is honoured. This is because honour discharges (rather than amends or cancels) the issuer’s obligations and because ISP98 Rule 1.10(c)(ii) (Redundant or Otherwise Undesirable Terms) presumes that reinstatement is not intended. ISP98 Form 3 (Model Standby Providing for Reduction and Incorporating Annexed Form of Reduction Demand) focuses on reduction, including reduction to zero, by beneficiary demand and by other optional terms permitting or requiring reductions in the amount available under a standby.

19. Incorporation of ISP98; law, court, arbitration, and sanctions. Incorporation of ISP98 into an undertaking that is payable against the presentation of documents should qualify the undertaking as independent under applicable law. ISP98 invokes letter of credit law by emphasizing the letter of credit aspects of a standby and its independence in ISP98 Rules 1.06(c) (Nature of Standbys) and 1.07 (Independence of the Issuer-Beneficiary Relationship). See Team Telecom Int’l v. Hutchison 3G UK Ltd, 2003 EWHC 762 (Q.B. Div’l Ct.) [England], abstracted at 2004 Annual Survey of Letter of Credit Law & Practice 335 (bond subject to ISP98 is an independent undertaking).

It is unnecessary for a standby to recite that it is independent or that it is enforceable without regard to the validity of any claim of performance or non-performance in the underlying transaction. It is unnecessary for a standby to add a recital (including an “integration” or “merger” clause) that would deny or limit the effect of any document or other matter mentioned in the standby or of any negotiations leading up to or following standby issuance. Such clauses and recitals risk limiting the various ISP98 rules that provide for the standby’s independence.
Where a choice-of-law clause is included in a standby, most courts will give effect to it. Otherwise, a court will likely apply its own conflict-of-laws' rules. Conflict-of-laws' rules affect the legal standards for compliance of any presentation, for the scope of any fraud/abuse exception, for the availability of any excuse based on government sanctions, etc. Under many legal systems, the conflict-of-laws' rules provide that the law at the place of issuance of the standby (or confirmation) should govern the issuer's (or confirmer's) obligations. See, e.g., the UN Convention on Independent Guarantees and Standby Letters of Credit, Articles 21 (Choice of applicable law) and 22 (Determination of applicable law). However, courts may hear a wrongful dishonour claim filed other than where the issuer (or confirmer) is located, may apply different conflict-of-laws' rules, and may determine, e.g., that the law of the place where the beneficiary is located should govern.

As indicated, most courts will respect a choice-of-law clause and a choice-of-exclusive-forum clause in a standby (or confirmation of a standby). Including a choice of law clause or an exclusive forum clause or both fosters certainty. E.g.: “Issuer’s obligations under this Standby are governed by the laws of [State]. The courts located in [State] shall have exclusive jurisdiction over any action to enforce Issuer’s obligations under this Standby.”

The Preface to ISP98 includes a suggested arbitration clause: “This Standby [undertaking] is issued subject to ISP98, and all disputes arising out of it or related to it are subject to arbitration under ICLOCA Rules (1996).” (The ICLOCA Rules, which are based on the UNCITRAL Rules of Arbitration, are available at www.icloca.org. The International Center for Letter of Credit Arbitration is located in metropolitan Washington, D.C., at 20405 Ryecroft Court, Montgomery Village, MD 20886 USA.)

Particularly if the standby does not choose applicable law, the issuer may wish to consider including a “sanctions” clause covering sovereign compulsion excusing the issuer, e.g.: “Issuer disclaims liability for delay, non-return of documents, non-payment, or other action or inaction compelled by a judicial order or government regulation applicable to Issuer.”

A standby consists of obligations of the issuer limited by its terms and conditions. Accordingly, a choice of law or forum or both in a standby
applies to those issuer obligations and not to the obligations of any
confirmor or other person. There is no problem under a straight standby
that states that "this standby is governed" by the chosen law or that any
litigation under it is limited to the chosen court, but this same wording
might prove confusing when included in a standby that nominates another
person to advise, confirm, or otherwise act on the standby.

20. Communications. This optional clause or a variation of it is
particularly apt for a standby that is long term or that provides for
communications from or to the beneficiary (apart from payment demands).
If a beneficiary requires greater certainty that its request to amend its
address will be given effect, then the standby should expressly provide for
automatic amendment against presentation of a complying beneficiary
demand for an address change. Standby language with a demand form for
this purpose may be adapted from ISP98 Forms 3 and 4 providing for
reduction and transfer on demand by the beneficiary.

21. Demand Date. ISP98 Rule 4.16(b)(ii) (Demand for Payment) provides
that a demand must contain an issuance date, and ISP98 Rule 4.06 (Date of
Documents) provides that its issuance date may not be later than the date of
its presentation. To override that rule, e.g., to permit post-dated
documents, the following clause may be added to the Standby text: "The
issuance date or any other date on any document, including the required
demand, may be a date on, before, or after the date the document is
presented under this Standby."

22. Addressee. The information in the text of the standby indicating where,
how, and to whom a presentation is to be made under the standby should be
repeated in the demand form. See ISP98 Rules 3.01 (Complying
Presentation under a Standby), 3.04 (Where and to Whom Complying
Presentation Made), and 3.06 (Complying Medium of Presentation).
Particular attention should be given to the possibility that a standby may
require presentation at an address that differs from the issuer’s letterhead
address.

23. Standby identification. A demand form should identify the standby by
including the information in the standby text that identifies it, particularly
the issuer’s reference number. See ISP98 Rules 3.01 (Complying
Presentation under a Standby) and 3.03 (Identification of Standby)

24. Demand. This model form of annexed demand should satisfy the
requirements of ISP98 Rules 4.16 (Demand for Payment) and 4.17 (Statement of Default or other Drawing Event), so that, when the beneficiary completes it as indicated, it will include a demand for payment of a stated amount, be dated and signed, and contain any required beneficiary statements.

25. **Beneficiary statements.** Standbys commonly require presentation of beneficiary statements and commonly combine them with the required form of demand for payment. Words other than “states”, such as “certifies”, “represents”, “warrants”, “promises”, or a combination of those words, are also used and may be preferable in the context of the underlying transaction. Any such word of assurance, when required to be included in a document presented under a standby, may give rise to a claim against the beneficiary who obtains payment under the standby. The nature and sufficiency of such claim may depend on the precise wording included in the demand, the identity of the claimant, and the status of any related claims based on the obligations intended to be supported by the standby.

The applicant or issuer or both may prefer a combination of specific representations and undertakings from the beneficiary. The beneficiary may prefer no such wording or only conclusory wording qualified by the beneficiary’s reference to “good faith” belief or the like. The applicant or issuer or both may prefer that the beneficiary make its statements expressly to the applicant or issuer or both.

ISP98 Rule 4.12 (Formality of Statements in Documents) provides guidance on standby requirements for statements that are to be “sworn to”, “witnessed”, “legalized”, or the like.

It should be unnecessary to include in a demand form that the amount demanded is available under the standby, because that amount should be determinable without dependence on any such statement.

26. **“Applicant” as underlying obligor.** This demand form uses “Applicant”, which is a defined term in the text of the standby, and assumes that the applicant and beneficiary are parties to an underlying agreement that establishes the obligations to be supported by the standby. See endnotes 1 and 30.

27. **Obligated/in default.** This statement indicates that the applicant is “obligated to pay” the amount demanded, not that there is a “default”. A
default statement is inapt where the amount demanded is payable on the date demanded without regard to the occurrence or continuance of a default or where “default” is not adequately defined in the documentation for the underlying obligations or where “default” may require that an action be taken that may be prohibited under laws triggered by the insolvency of the applicant or other party.

28. **Unpaid.** The term “unpaid” in the optional “due and unpaid” recital may raise a question where the applicant has made a direct payment to the beneficiary but the funds paid are subject to recapture by an insolvency representative of the applicant. It should be possible for a beneficiary in that context to state, without running afoul of a fraud or abuse exception under applicable letter of credit law, that the underlying obligation remains unpaid where a direct payment has been received subject to a credible claim that the direct payment is voidable and must be returned.

29. **Underlying obligation.** Although some standbys are payable on simple demand, the applicant, beneficiary, or issuer may insist that a demand under a standby identify the underlying obligation, obligor, and obligee, particularly where there may be no single underlying agreement between the applicant and beneficiary that establishes the underlying obligations and provides that those obligations be supported by a standby.

30. **Applicant-beneficiary relationship.** This model form of annexed demand assumes that the standby supports one or more obligations of the applicant to the beneficiary. Under commercial and regulatory laws, the issuer, any nominated bank, the applicant and beneficiary, and, where different, the underlying obligor and obligee may need to identify the underlying obligations intended to be supported by the standby and to be satisfied or secured by the proceeds of a drawing under the standby. Accordingly, this form of demand should be redrafted if, e.g., the applicant is a surety for the underlying obligor or the beneficiary is a creditor of the underlying obligee. Additionally, the underlying documentation should be drafted to provide for the pre- and post-honour obligations of the applicant and beneficiary (and, where different, of the underlying obligor and obligee) to each other, particularly if the named applicant has or intends to claim the rights of an ordinary guarantor or surety. In this regard, it may be desirable for the beneficiary’s statement to refer expressly to the underlying obligations, as they may be amended by the obligor and obligee, without (or with) the further consent of the applicant.
31. **Use of proceeds.** This optional beneficiary statement is unnecessary if the underlying agreement adequately provides for the use of all proceeds from a drawing under the standby and if the applicant reimburses the issuer. Otherwise, some mention in the form of demand of the relationship of any standby proceeds to the underlying obligation is helpful in answering post-honour questions about the disposition of any excess standby proceeds. Absent such a provision, the "independence" of the standby obligation may hinder appropriate post-honour accounting for the use of funds received under a standby.

32. **Proceeds as cash collateral.** Where the proceeds cannot or might not be used to "satisfy" the applicant’s obligations, the demand form should indicate that the proceeds will be used to "secure" them. This consideration is important under standbys that are intended to be used, at least in some circumstances, to fund the applicant’s underlying obligation to provide cash collateral. The most common circumstance involves standbys that may expire before the underlying obligations become fully due and payable.

33. **Accounting to issuer for unused proceeds.** The issuer may want to take a security interest in the applicant’s rights to unused proceeds and/or require the beneficiary to state, e.g., "...and that Beneficiary will account to Issuer or Applicant, as their interests may appear, for any proceeds that are not so used."

34. **Request for wire transfer to beneficiary’s account.** This term in the demand form is unnecessary if the text of the standby includes satisfactory wire transfer information for payment to the beneficiary. See endnote 16.

Issuers are not required to pay wherever, however, or whomever the beneficiary requests, unless the standby so states. Under ISP98 Rule 5.08 (Cover Instructions/Transmittal Letter), issuers are permitted to follow a request to pay by wire transfer to the beneficiary’s account, subject to timely receipt of customary account information and deduction of customary wire transfer charges and due consideration of any regulations or bank policies affecting wire transfer of funds to the requested country, bank, and account.

A request to pay to another’s account is a request for acknowledgement of an assignment of proceeds, which is subject to the special rules in ISP98
Rules 6.06-6.10 (Acknowledgement of Assignment of Proceeds), as well as laws protecting issuers and applicants and other laws regulating money laundering, etc.

To deter forged demands, and to address anti-money-laundering concerns, this model form of request for payment by wire transfer states that payment is to be made to the named beneficiary at a specified beneficiary account at a specified bank location.

35. **Signer authentication.** This demand form requires the signer to indicate in the signature line that the demand and statement are made by the named beneficiary located at the address stated in the standby. Accordingly, the beneficiary’s name and address should be stated in this demand form when the standby incorporating it is issued.

36. **Original signature.** What is an original signature depends on the mode of communication. See ISP98 Rules 1.09(a) (Defined Terms) (“Signature”) and 3.06(d) (Complying Medium of Presentation)[IIBLP as of 10 May 2012]
Assignments for Monday 24 September and 1 October 2012

The readings focus on automatic extension and reduction clauses. There are no rules, as such, that address automatic extension with the minor exception of ISP98 Rule 2.06(a).

The assignment for Monday 24 September is to revise the portion of *The Official Commentary on the International Standby Practices* for ISP98 Rule 2.06 that deals with automatic extension clauses. A PDF of that chapter accompanies this message. Email your revision to the entire class via the TWEN email list before the beginning of class. Include a brief explanatory paragraph describing your methodology.

The assignment for the class on Monday 1 October is to draft a revision of Rule 2.06’s treatment of automatic extension, explaining in endnotes the provisions. The new rule should be entitled Rule 2.06B Automatic Extension Clauses address automatic extension clauses exclusively, leaving to Rule 2.06A the treatment of amendments. Its content will be current ISP98 Rule 2.06(b), (c), and (d). Email your revision to the entire class by 9:00 PM on Sunday 30 September via the TWEN email list.

You should understand the effect of Revised UCC Article 5 on amendments, the rules and practices regarding amendment, the reasons for automatic extension provisions, how they operate (read ISP98 Form 2), and the problems inherent in them (see the cases and notes in the text).

The purpose of this exercise is to enable you to understand the role and process of rulemaking in commercial law.
APPENDIX E
International Commercial Transactions Fall 2012

Assignment for 15 October 2012

1. Read Chapter 4 Confirmation, Counter Standbys, and Counter Guarantees.
2. Prepare the following exercise and submit by Friday 12 October via TWEN drafts for discussion in class.
3. Exercise: The sovereign principality of Bifurcated wishes to purchase jet fighter parts from Atlas Air Corp. for US$ 500 million. It is prepared to pay via commercial letter of credit. It requires, however, assurance of performance and warranty amounting to 10% of the contract amount. It will accept cash to be held in escrow or a demand guarantee in its favor. Its regulations require that the obligation be from a local bank. Atlas Air does not have accounts with any banks in Bifurcated; its bank is Global International Bank. Global International has a correspondent banking relationship with Commercial Bank of Bifurcated (CBB).

a. Student A will arrange a drawing in class on 1 October to determine who will represent whom. There will be two representatives of the banks and one each of the buyer and seller. The bankers will be further divided in that one will propose a counter guarantee/local bank undertaking relationship and the other will propose an issuance/confirmation relationship.

b. Each party will draw up and submit to one another proposals for terms of the undertakings to be issued by the banks (on the part of buyer and seller) or what the banks are prepared to do (on the part of the banks). In addition to proposing the terms, the bankers should prepare a draft undertaking using the ISP98 Model Forms. The buyer and seller should be prepared to react to these proposed forms in class.

c. The class on 22 October will be devoted to negotiations between the parties regarding what their clients are prepared to accept. Note: everyone wants this deal to work.

[30 September 2012]
Problem A:

Antoine Ltd, a producer of USB drives located in Bulgaria, agreed to sell 10 million USB drives to Sampson, Inc., located in Virginia, for USD 4 million. The contract provided for commercially usable USB drives. Payment was to be by commercial letter of credit issued by Sampson’s bank, Virginia Credit Bank, and, pursuant to the agreement, confirmed by Antoine’s bank, ABC, also located in Bulgaria. Required documents included a certificate of inspection issued by SGS stating that the drives meet the contract specifications. The commercial LC was payable 60 days after presentation of the required documents.

On 1 March 2012, Antoine presented complying documents to ABC which forwarded them to Virginia Credit. Neither bank sent a notice of refusal. Thirty days later, the goods arrived and were not compatible with any computers except those produced in the former Soviet Union, utilizing a technology that was so outdated and unique as to make them unusable for most computers in the world.

Assignment Part A1: Prepare a 2 page Memo outlining whether Buyer should seek to enjoin payment on the LC and against whom the suit should be brought in what jurisdiction and under what law.

Assignment Part A2: Prepare a 2 page Memo outlining options available to Seller in opposition to an action for an injunction.

Assignment Part A3: Prepare a 2 page Memo on behalf of the Confirmer.

Assignment Part A4: Prepare a 2 page Memo on behalf of the Issuer.

Problem B:

To support its warranty obligations under the contract, Antoine caused its bank, ABC, to issue a counter standby in favor of Sampson’s bank, Virginia Credit, asking Virginia Credit to issue its local bank undertaking in favor of Sampson. When the USB drives would not work because they
were not compatible, Sampson drew on the local undertaking whereupon Virginia Credit drew on the ABC Counter Standby.

Contending that it shipped good goods to Sampson, Antoine objects and threatens to sue for an injunction. Prepare a 2 page Memo on behalf of

Assignment B1: Antoine

Assignment B2: Virginia Credit.

Assignment B3: ABC.

Assignment B4: Sampson.

The Memos.

The Memos should be directed to your Senior Partner and indicate possible strategies, risks, and make a recommendation. They should also note any factual questions, which must be clarified.

The Memos should be sent to everyone in the class on the TWEN email list by the end of the day on Friday 26 October 2012.