

A COURT CASE ON LETTERS OF CREDIT & UCP600

Letter of Credit practitioners worldwide use ICC's rules for documentary credits, presently called UCP 500 and UCP 600 from 1st July 2007. The ICC rules have introduced a measure of uniformity into the field that was once fractured by individual country rules that rendered LC practice different from one region to another. But the UCP are contractual rules that do not have the force of law. Only when they are incorporated into credit do they become binding on the parties.

That is why court decisions on Letters of Credit are of considerable importance, not only Letter of Credit practitioners, but also to World Trade in general. While Letter of Credit practitioners may not always agree with court interpretations of the UCP, but they are compelled to respect them. In certain cases, ICC has been called upon to issue clarifications of its rules as a result of what the court decides, either by way of banking commission decisions or by adapting future

Issuing Bank	- Banque Paribas (Paribas)
Confirming Bank	- Banco Santander (Santander)
Beneficiary	- Bayferm Ltd (Bayferm)

The Court stated

“The Issuing Bank has requested the Confirming Bank to give its own undertaking to pay on 27 November 1998, in addition to that, the Issuing Bank has promised to reimburse the Confirming Bank when it pays on that deferred payment undertaking i.e. pay USD20.3 million on 27 November 1998. There is no request from Paribas that Santander should discount or give value for the documents prior to 27 November 1998 and albeit it may not be a breach of mandate for Santander to do so, it is upto Santander whether it does so or not. In my view the position is that Santander had no authority from Paribas to discount and did not seek it. It was something they were entitled to do on their own account. If they had not chosen to discount and waited until 27 November, they would have had a defence and it is in those circumstances not open them to claim reimbursement from Paribas”. Based purely on UCP500, the above appears to be a logical conclusion. Had Santander not effected payment until the maturity date, it would have had the same defence of Paribas against Bayferm i.e. no obligation to pay on the grounds of fraud.

Comments

US position:

Interestingly, if the LC was subject to US Law, the decision could have been totally different from the English Court's decision. The US Uniform Commercial Code provides for an exception to the fraud defence, and considers that the position of an assignee of a deferred payment credit is equivalent to that of a holder in due course of a negotiable instrument.

Korean case :

Industrial Bank of Korea Vs BNP Paribas 2003

The South Korean Supreme Court held a different view that when an Issuing Bank requests another Bank to confirm the LC, the Issuing Bank is authorising the Confirming Bank to negotiate the documents and to pre-pay the beneficiary against compliant documents presented under a deferred payment credit.

It appears that the crux of the problem concerning the availability of credit is that the UCP500 does not clearly set out whether financing under acceptance or deferred payment credit permitted. It was a widely accepted fact that UCP500 was unable to address with prepay or purchase under acceptance credit or deferred payment credit. On this issue we still are at the beginning of Trade i.e. the LC practice is different from one region to another. To arrest the situation, the International Chamber of Commerce (ICC) was compelled to review UCP500 for its completeness. The UCP600 is a brainchild of ICC and would be a remedy for grievances faced by LC practitioners.

Here is the Article No. 12(b) of UCP600 :

“By nominating a Bank to accept a Draft or incur a deferred payment undertaking, an Issuing Bank authorizes that nominated Bank to pre-pay or purchase a Draft accepted or a deferred payment undertaking incurred by that nominated Bank.”

Still there is a doubt that whether there could be a conflict with local laws of some countries with regard to who should be responsible for fraud.

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