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REPORT OF THE WORKING GROUP ON INTERNATIONAL CONTRACT PRACTICES ON THE WORK OF ITS TWENTY-FIRST SESSION

(New York, 14-25 February 1994)

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I. INTRODUCTION

1. Pursuant to a decision taken by the Commission at its twenty-first session, 1/ the Working Group on International Contract Practices began its work on independent guarantees and stand-by letters of credit by devoting its twelfth session to a review of the draft Uniform Rules on Guarantees being prepared by the International Chamber of Commerce (ICC) and to an examination of the desirability and feasibility of any future work relating to greater uniformity at the statutory law level in respect of guarantees and stand-by letters of credit (A/CN.9/316). The Working Group recommended that work be initiated on the preparation of a uniform law, whether in the form of a model law or in the form of a convention. The Commission, at its twenty-second session, accepted the recommendation of the Working Group that work on a uniform law should be undertaken and entrusted this task to the Working Group. 2/

2. At its thirteenth session (A/CN.9/330), the Working Group commenced its work by considering possible issues of a uniform law as discussed in a note by the Secretariat (A/CN.9/WG.II/WP.65). Those issues related to the substantive scope of the uniform law, party autonomy and its limits, and possible rules of interpretation. The Working Group also engaged in a preliminary exchange of views on issues relating to the form and time of establishment of the guarantee or stand-by letter of credit.

3. At its fourteenth session (A/CN.9/342), the Working Group examined draft articles 1 to 7 of the uniform law prepared by the Secretariat (A/CN.9/WG.II/WP.67). The Working Group also considered the issues discussed in a note by the Secretariat relating to amendment, transfer, expiry and obligations of the guarantor (A/CN.9/WG.II/WP.68).

4. At its fifteenth session (A/CN.9/345), the Working Group considered certain issues concerning the obligations of the guarantor, presented in the note by the Secretariat relating to amendment, transfer, expiry and obligations of the guarantor (A/CN.9/WG.II/WP.68). The Working Group then considered the issues discussed in a note by the Secretariat relating to fraud and other objections to payment, injunctions and other court measures (A/CN.9/WG.II/WP.70) and issues discussed in a note by the Secretariat relating to conflict of laws and jurisdiction (A/CN.9/WG.II/WP.71).

5. At its sixteenth session (A/CN.9/358), the Working Group examined draft articles 1 to 13, and, at its seventeenth session (A/CN.9/361), draft articles 14 to 27 of the uniform law prepared by the Secretariat (A/CN.9/WG.II/WP.73 and Add.1). At the eighteenth, nineteenth and twentieth sessions (A/CN.9/372, 374 and 388), the Working Group considered further revisions of the draft articles (contained in A/CN.9/WG.II/WP.76 and Add.1 and

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

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

A/CN.9/WG.II/WP.80), which, at the sixteenth session, the Working Group provisionally decided should be presented in the form of a draft Convention (A/CN.9/361, para. 147).

6. The Working Group, which was composed of all States members of the Commission, held its twenty-first session in New York, from 14 to 25 February 1994. The session was attended by representatives of the following States members of the Working Group: Argentina, Austria, Bulgaria, Canada, China, Ecuador, France, Germany, India, Iran (Islamic Republic of), Italy, Japan, Morocco, Nigeria, Poland, Russian Federation, Saudi Arabia, Thailand, Togo, United Kingdom of Great Britain and Northern Ireland, United Republic of Tanzania and United States of America.

7. The session was attended by observers from the following States: Algeria, Australia, Bahrain, Cyprus, Czech Republic, Democratic People's Republic of Korea, Finland, Hungary, Jordan, Mongolia, Philippines, Sweden, Switzerland, Turkey and Ukraine.

8. The session was attended by observers from the following international organizations: Banking Federation of the European Community; International Chamber of Commerce.

9. The Working Group elected the following officers:

Chairman: Mr. J. Gauthier (Canada)

Rapporteur: Mr. V. Tuvayanond (Thailand).

10. The Working Group had before it the following documents: provisional agenda (A/CN.9/WG.II/WP.81); a note by the Secretariat containing a further revision of draft articles 1 to 17 (A/CN.9/WG.II/WP.80), prepared by the Secretariat following the nineteenth session.

11. The Working Group adopted the following agenda:

1. Election of officers;

2. Adoption of the agenda;

3. Preparation of a draft Convention on independent guarantees and stand-by letters of credit;

4. Other business;

5. Adoption of the report.

II. DELIBERATIONS AND DECISIONS

12. The Working Group discussed draft articles 2 (2) to 17 (2) as set forth in A/CN.9/WG.II/WP.80.

13. The deliberations and conclusions of the Working Group relating to draft articles 2 (2) to 17 (2) are set forth below in chapter II. The Secretariat was requested to prepare, on the basis of those conclusions, a revised draft of articles 2 (2) to 17 (2), as well as the other articles of the draft Convention, to implement the decisions and conclusions of the Working Group.

III. CONSIDERATION OF ARTICLES OF A DRAFT CONVENTION ON INDEPENDENT GUARANTEES AND STAND-BY LETTERS OF CREDIT

CHAPTER I. SCOPE OF APPLICATION

Article 2. Guaranty letter (continued)

General remark

14. In the context of the discussion of article 2, the Working Group reaffirmed the decision made at its previous session that, instead of promoting a new term such as "guaranty letter" as an attempt to describe both bank-guarantee and stand-by-letter-of-credit practice, the draft Convention should rely on a neutral term such as "undertaking" to refer to both types of instruments being covered by the draft Convention (A/CN.9/388, para. 97). The Secretariat was requested to reflect that decision in the next draft.

Paragraph (2)

15. The Working Group, recalling its consideration of the matter at its eighteenth session (A/CN.9/372, paras. 54-55), approved the substance of paragraph (2).

Paragraph (3)

16. The view was expressed that some among the forms of payment listed in subparagraphs (a) to (d) were not commonly used, at least in bank-guarantee practice. It was suggested that paragraph (3) should be limited to the general statement of principle contained in its opening words, establishing that payment could be made in any form stipulated in the undertaking. Other suggestions were to delete, variously, subparagraphs (a), (b), (c) and (d).

17. The prevailing view was that, while a listing of possible forms of payment might be superfluous with respect to bank guarantees, it might help to delimit appropriately the scope of the draft Convention with respect to stand-by letters of credit. After deliberation, the Working Group found the substance of paragraph (3) to be generally acceptable. It was suggested that the term "draft" might be added in brackets to the term "bill of exchange" for consistency with the terminology used in the Uniform Customs and Practice for

Documentary Credits adopted by the International Chamber of Commerce ("UCP 500").

Paragraph (4)

18. The Working Group reaffirmed the decision made at its eighteenth session (ibid., paras. 42-43) that the draft Convention should accommodate the practice under which an undertaking could validly stipulate that the guarantor or issuer itself was the beneficiary when acting as a fiduciary or trustee in favour of another person.

19. A question was raised as to whether the draft Convention satisfactorily dealt with the cases where the undertaking might stipulate that the beneficiary was a "branch" of the issuer. It was generally agreed that the draft Convention would readily apply to such an undertaking in those situations where the "branch" as a legal entity was distinct from the issuer.

20. Various views were expressed with respect to those situations where a "branch" issued a guaranty undertaking to another branch of the same legal entity, a practice which was reported to exist with respect to both bank guarantees and stand-by letters of credit. One view was that the text of paragraph (4) needed to be redrafted to make it clear that the draft Convention applied to such undertakings. To that effect, it was suggested that the draft Convention should include a provision, along the lines of both article 1 (3) of the UNCITRAL Model Law on International Credit Transfers and article 2 of UCP 500, stating that, for the purposes of the draft Convention, branches and separate offices of a bank in different States were separate banks. A contrary view was that such undertakings should not be brought within the scope of the draft Convention since it was difficult to conceive how the draft Convention would apply in case of a dispute between branches of the same legal entity. It was suggested that, should such a dispute arise, it would in all likelihood be settled by internal procedures that were outside the scope of the draft Convention. The prevailing view was that the draft Convention should not attempt to regulate those situations involving issues of company law. However, it was also agreed that it was not intended to disallow such practice or to invalidate an undertaking whose issuer and beneficiary were branches of the same legal entity. It was also agreed that parties should be free to make the draft Convention applicable to such situations by expressly so stipulating in the undertaking.

21. After deliberation, the Working Group requested the Secretariat to prepare a new draft of article 2 reflecting the above decisions.

Article 3. Independence of undertaking

22. Before entering into the discussion of the substance of article 3, the Working Group expressed a preference for the expression "the guarantor's or issuer's obligation" over the expression "the guarantor's or issuer's performance". A suggestion to refer, in addition to the existence or validity of the underlying transaction, to the "legal effects" or "type" of transaction did not receive support. The Working Group also noted a concern that the

current version of article 3 no longer contained a statement to the effect that counter-guarantees under the draft Convention were independent from the underlying guarantee to which they related, a point that could usefully be stated expressly, as had been done in paragraph (3) of the previous version of article 3 (A/CN.9/WG.II/WP.76).

23. As to the substance of article 3, it was generally felt that the provision was not sufficiently clear as to the rule that it attempted to lay down on the effect and fate of non-documentary conditions found in the undertaking. There was uncertainty in particular with regard to the phrase appearing within square brackets, "even if stipulated as a condition of payment in the guaranty letter". It was noted that the article was intended to reflect the decision at the eighteenth session to exclude undertakings containing non-documentary conditions from the scope of application of the draft Convention, by linking the definition of independence to the documentary character of the undertaking. An alternative approach would have been to include such undertakings in the scope, by providing a "safe-haven" rule under which undertakings denominated in a prescribed manner could be deemed independent irrespective of the presence of non-documentary conditions. Linked to that approach was a "conversion" rule providing for the transformation of non-documentary conditions into documentary ones (article 3 (1) (b) and (2), in A/CN.9/WG.II/WP.76).

24. Considerable interest was expressed by the Working Group in possibly modifying the above decision as reflected in the current formulation of article 3. Grounds cited for considering further the earlier decision with regard to article 3 included the realization that the strict rule in article 3 would exclude from the scope of the draft Convention a large number of undertakings, of both the bank guarantee and stand-by letter of credit variety, undertakings intended by the parties to be independent despite the presence of non-documentary conditions. The concern was expressed that the exclusion from the scope of a significant number of undertakings would contribute to a diversification of legal regimes and greater uncertainty, rather than to the goal of unification. To that end the Working Group considered a variety of approaches that differed in the extent to which they would permit the draft Convention to take into account non-documentary conditions.

25. There was broad agreement in the Working Group that, as one possible, relatively minimal approach, article 3 could be modified to take cognizance of conditions that, though non-documentary, could be verified within the operational purview of the guarantor or issuer (variant A, under para. 28 below). An example cited in this vein was the advance payment guarantee in which receipt of the advance payment by the guarantor, as a requirement for the effectiveness of the guarantee, could be verified by the guarantor’s checking its own bank records. It was suggested that such "conditions of effectiveness" were relevant to the current discussion and could be distinguished from "conditions for issuance", for example, a seller’s request for issuance of a letter of credit as a condition for the issuance of a performance guarantee.

26. Several possible approaches were considered with respect to the other category of non-documentary conditions, those that fell outside the operational purview of the guarantor or issuer. A number of interventions were directed at the reinstitution of the "safe haven" and conversion rules contained in the

earlier draft (and described above, para. 23). While support was expressed for such an approach, objections were raised based on a concern that it would subvert party autonomy by bringing into the scope of the draft Convention undertakings not intended to be independent. Similar concerns were raised with respect to using an approach similar to that found in article 13 (c) of UCP 500, which provided for ignoring non-documentary conditions. A number of suggestions were made aimed at injecting more flexibility in determining which type of non-documentary conditions would not cripple independence. They included: assessment of the entire face of the undertaking in order to determine independence; whether conditions could be verified "easily" or "without doubt"; whether the condition was unrelated to the underlying transaction.

27. Two other approaches were proposed, inspired in part by the suggestion that reference could be made to uniform rules of practice in defining independence for the purposes of the scope of application of the draft Convention. Under the first approach (variant B, under para. 28), an undertaking would not be deprived of independence by the presence of a non-documentary condition either if the condition was within the purview of the guarantor or issuer or if the undertaking was subject to rules of practice that provided for ignoring the condition or converting it into a documentary condition. It was noted that, under this approach, bank guarantees containing non-documentary conditions would be excluded from the scope of the draft Convention, since the uniform rules in question (URDG) did not contain a rule for disposing of non-documentary conditions. Under the second, broader approach (variant C, under para. 28), which would include bank guarantees containing non-documentary conditions, an operational rule would be included for the case of an undertaking not subject to rules of practice that contained a solution to the question of non-documentary conditions. In such cases, the guarantor or issuer would not be obliged to pay unless it was shown prima facie evidence that the non-documentary condition had been met. It was suggested that such an approach would reflect a practice followed by most guarantors in such cases. The concern was expressed generally that the reliance on rules of practice for determining the scope of application of a convention was not appropriate.

28. Having engaged in the above survey of possible approaches, the Working Group then considered which of the main approaches that had been identified and that are presented below in textual form would be preferable:

Variant A:

> For the purposes of this Convention, an undertaking is independent where the guarantor’s or issuer’s obligation to the beneficiary is not subject to the existence or validity of an underlying transaction, [or to any other undertaking,] or to any term or condition not appearing in the undertaking, or to any future, uncertain act or event other than presentation of stipulated documents or another act or event [whose occurrence lies] within the operational purview of the guarantor or issuer. [A counter-guarantee is separate also from the guarantee to which it relates.] [This rule applies to counter-guarantees also in respect of the guarantees to which they relate.]

Variant B:

(1) For the purposes of this Convention, an undertaking is independent where the guarantor's or issuer's obligation to the beneficiary is not subject to the existence or validity of an underlying transaction or to any term or condition not appearing in the undertaking.

(2) An undertaking which provides that the guarantor's or issuer's obligation to the beneficiary is subject to a future, uncertain act or event other than presentation of stipulated documents is independent only if:

(a) the occurrence of that act or event [lies] [can be verified] within the guarantor's or issuer's operational purview, or

(b) that condition is, by virtue of applicable [uniform rules] [rules of practice] or otherwise, to be disregarded or to be converted into a documentary one.

Variant C:

(1) For the purposes of this Convention, an undertaking is independent where the guarantor's or issuer's obligation to the beneficiary is not subject to the existence or validity of an underlying transaction or to any term or condition not appearing in the undertaking.

(2) Where an [independent] undertaking subjects the guarantor's or issuer's obligation to a future, uncertain act or event and that condition is neither to be disregarded nor to be converted into a documentary one [by virtue of applicable uniform rules or otherwise], the guarantor or issuer is not obliged to pay unless it is [satisfied] [shown prima facie evidence] that the act or event has occurred.

29. As a first step in its review of the above variants, the Working Group considered which of the three approaches should be followed. Broad support was expressed for variant A on the grounds of its simplicity, which made it more apparent how the article would operate. Part of the support for variant A derived from uncertainty concerning the formulation and effect of variant C, the other of the variants to attract significant interest. It was also suggested, and widely supported, that variant A could be interpreted as permitting application of the Convention when non-documentary conditions were "taken out of play" by the ignoring rule in article 13 (c) of UCP 500, a result expressly provided for in variant B. The view was expressed that for that reason variant B would be preferable, though variant B raised objections, as noted above, that it would be inappropriate for the draft Convention to rely for its application on rules of practice.

30. Interest in variant C was motivated by the benefit that it would bring of expanding the scope of the Convention to cover a significant additional portion of the market, in particular bank guarantees intended to be independent but containing non-documentary conditions beyond the guarantor's operational purview. It was noted that the wording was intended to be broad enough to

encompass the purview notion. However, hesitation was expressed about variant C, in particular because of a view that paragraph (1) of variant C would entangle in the scope of application of the draft Convention a host of independent undertakings not intended to be dealt with, for example, insurance undertakings and bills of exchange. It was pointed out, in response, that paragraph (1) was intended merely to define independence of the undertaking, and that the range of undertakings covered by the draft Convention was subject to limitation by articles 1 and 2. It was also recalled to the Working Group that the formulation used in paragraph (1) to filter out accessory guarantees, in particular the words "not subject to the existence or validity of an underlying transaction", was identical to the formulation used in variant A for the same purpose, and that accessory undertakings would therefore be excluded.

31. The Working Group noted that paragraph (2) of variant C was not intended to be a scope rule, but was currently being considered because of its relevance, as an operational rule for dealing with non-documentary conditions, to the decision to be taken on scope by the Working Group. Hesitation about the operational rule in paragraph (2) was expressed because of uncertainty as to its effect and a concern for protecting party autonomy. A proposal to replace the prima-facie-evidence procedure by a statement from the beneficiary concerning the occurrence of the condition, a procedure reflecting case-law in some jurisdictions, was unable to overcome those concerns.

32. Drafting suggestions aimed at clarifying variant C included: taking into account that a condition could be predicated on a future uncertain event not occurring; referring to "readily available evidence" rather than to "prima facie evidence"; and referring to "fundamental" future, uncertain acts or events.

33. After deliberation, the Working Group decided that, in accordance with the prevailing view, variant A should be retained. The view was expressed, however, that the matter was likely to be subject to further consideration. As to the precise formulation of variant A, the Working Group decided to retain the words "or to any other undertaking" as a reference to the independence of a counter-guarantee from the other guarantee to which it related. It was felt that such a formulation was preferable to either of the two contained in square brackets at the end of variant A, both of which were therefore deleted. It was also decided to delete the words "whose occurrence lies". Drafting suggestions included: to remove the reference to the operational purview of the guarantor or issuer; to refer to a "fundamental" term and to try to avoid using the expression "uncertain act or event" in a scope context; and to follow the drafting style of variant B, by using paragraphs (1) and (2) (a), the content of which paralleled that of variant A. Only the latter suggestion was accepted by the Working Group.

Article 4. Internationality of guaranty letter

34. The Working Group, recalling the decision made at its eighteenth session (A/CN.9/372, para. 70), found the objective criteria provided in article 4 for determining the internationality of an undertaking to be generally acceptable. A question was raised as to whether, under the current draft, the parties retained the freedom of meeting the internationality requirement merely by

calling the undertaking international, through what was referred to as an "opting-in provision". In response, it was recalled that the Working Group at its eighteenth session had decided that the draft Convention should contain a straightforward opting-in provision in article 1 rather than somewhat artificially extend the test of internationality (ibid., paras. 71-72).

35. A concern was expressed that a party in a contracting State should not be allowed to impose the application of the draft Convention on a party in a non-contracting State. It was suggested that the draft Convention should make it clear that "different States" mentioned in article 4 should all be contracting States. In response, it was recalled that the issue had been considered by the Working Group at its previous session in the context of the discussion of draft article 1. It had then been decided that the draft Convention should apply to undertakings issued in a contracting State and when the rules of private international law lead to the application of the law of a contracting State (A/CN.9/388, paras. 98-100).

36. As regards the drafting of article 4, it was noted that the term "place" had been substituted for the expression "place of business" as a result of a decision made by the Working Group at its eighteenth session (A/CN.9/372, para. 76). However, there was general agreement that the mere reference to the "place" of a given party was insufficiently clear and that the text should instead use the notion of "place of business". As a consequence, the Working Group decided that the text of article 4 should contain provisions along the lines of paragraph (2) (a) and (b) of draft article 4 as discussed by the Working Group at its eighteenth session (ibid., para. 67). The effect of such provisions would be to establish that, where the undertaking listed more than one place of business, the relevant place of business was that which had the closest relationship to the undertaking and that, where the undertaking did not specify a place of business for a given party but specified its habitual residence, that residence was relevant for determining the international character of the undertaking. As regards the use of the word "person" between square brackets, it was generally agreed that the term should be retained.

37. With respect to the reference to the place of business of the adviser as a possible criterion for determining the international character of the undertaking, it was generally felt that, although an adviser might perform important functions, it would typically act as an agent and that the performance of its functions could not be regarded as characteristic of the stand-by letter of credit or guarantee relationship. It was thus decided that the reference to the place of business of the adviser should be deleted.

38. After deliberation, the Working Group requested the Secretariat to prepare a new draft of article 4 reflecting the above decisions.

CHAPTER II. INTERPRETATION

Article 5. Principles of interpretation

39. The Working Group found the substance of article 5 to be generally acceptable.

Article 6. Rules of interpretation and definitions

40. The view was expressed that the reference in the title to rules of interpretation should be deleted. The Working Group noted that observation and decided that the exact formulation of the title would be better assessed after a further version of article 6 had been elaborated.

Subparagraph (a) ("guaranty letter")

41. It was recalled that at the twentieth session the Working Group had decided to replace the term "guaranty letter" throughout the Convention by the term "undertaking" (A/CN.9/388, para. 97). It was further noted that the implementation of that decision in the next revision might have implications not only for subparagraph (a) but also for certain other provisions of article 6, as well as other provisions in the draft Convention. An example of the latter was article 2 (1), where the drafting should avoid suggesting that all undertakings were independent.

42. The Working Group revisited briefly its decision to use the term "undertaking", prompted to do so by a question as to whether the term was too broad. Some residual preference was expressed for use of the term "guaranty letter", on the ground that, although currently unknown, it was more precise and would come to be accepted in practice. However, the Working Group again opted for "undertaking", recalling the concerns raised previously regarding "guaranty letter", in particular that that term was unknown in practice and might inadvertently interfere with the use in practice of similar terms to describe accessory guarantees.

43. Some interest was expressed in the possibility of defining the term "undertaking", although the Working Group generally felt that an adequate and properly placed description was to be found in articles 1 and 2. A drafting suggestion of a similar sort was to add a definition of "stand-by letter of credit", in particular to assist legislators in jurisdictions where such instruments were not widely known or used. It was pointed out, however, that defining the stand-by letter of credit would raise the necessity of defining or distinguishing bank guarantees and possibly other forms of undertakings and that such an endeavour had been earlier found to be not feasible in a generally acceptable manner.

Subparagraph (b)

44. The Working Group decided to delete subparagraph (b), as it was generally felt to be self-evident that a reference to the undertaking should be understood as a reference to the latest version of the undertaking.

Subparagraph (d) ("counter-guaranty letter")

45. The view was expressed that the definition as formulated in subparagraph (d) was not clear and that there might not be a need to retain it. It was suggested that the implication might inadvertently arise that counter-guarantees were always issued by the instructing party of the indirect guarantee or that there would always be a counter-guarantee. It was noted that

that was not the intended implication. It was pointed out that the need to use such "counter-undertakings" in the context of stand-by letters of credit was minimal because of the reimbursement procedure found in the UCP 500 and the availability of the confirmation procedure.

46. Questions were also raised as to the meaning of the reference to "another guarantee or another letter of credit", which was intended to indicate that the counter-guaranty letter could be given to support a commercial letter of credit or an undertaking of a type not covered by the draft Convention, namely, an accessory guarantee. A view was expressed that including the said wording would blur the scope of the draft Convention. An alternate formulation might be simply to refer to "another undertaking", which, however, would be narrower in scope.

47. The Working Group requested the Secretariat to review subparagraph (d) with a view, to the extent possible, to addressing the concerns that had been raised.

Subparagraph (e) ("counter-guarantor")

48. The possibility was suggested that subparagraph (e) might be one instance in which it would not be practical to implement the general decision to use the term "guarantor or issuer". It was submitted that the notion of a "guarantor" of a counter-guaranty letter would be confusing and should be avoided. It was suggested that reference might instead be made to the party or person that issued the counter-guaranty letter. It was recalled that the decision of the Working Group with respect to the use of the term "guarantor or issuer" or "guarantor/issuer" reflected the absence of a term familiar in both the guarantee and the stand-by letter of credit environments.

Subparagraph (f) ("confirmation")

49. The question was raised as to whether the scope and effect of subparagraph (f) was clear with respect to a number of issues that might arise in the context of confirmation. Those issues included: when, if ever, did the presentation of a demand for payment to the confirmer free the issuer from its undertaking; was there an order in which the beneficiary was to exercise its right to demand payment from either the confirmer or the issuer; were these possible different considerations applicable to confirmation of stand-by as opposed to commercial letters of credit. In considering those issues, the Working Group noted that confirmation in practice was used in stand-by letter of credit practice, but relatively rarely in the guarantee context.

50. Having considered the above observations, the Working Group affirmed that a definition along the lines of subparagraph (f) should be retained. It did so on the basis of an understanding that the provision was intended to recognize that confirmation established an additional right for the beneficiary, i.e., the right to demand payment at the counters of the confirmer. It was felt that the provision should make it clear that under the draft Convention presentation to the confirmer did not extinguish the right to proceed with a demand against the issuer if the confirmer dishonoured. It was understood that the provision was not intended to deal with issues that might properly be settled in the terms of the undertaking, such as the ones alluded to above, in particular whether there

should be a Convention rule on a controllable order for the presentation of the demand to the confirmer or to the issuer.

51. The Working Group noted that it might turn subsequently to the question of whether to include in the draft Convention a provision on "silent confirmation".

Subparagraph (g) ("confirmer")

52. The Working Group found the substance of subparagraph (g) to be generally acceptable.

Subparagraph (h) ("document")

53. The need for a definition of "document" was questioned, but the Working Group decided in favour of retention. Among the reasons cited for that decision was the utility of the provision in facilitating the use of electronic data interchange (EDI) and other emerging communications technologies.

54. Extensive consideration was given by the Working Group to whether to retain the reference to authentication. The concern in that regard was that the mention of authentication might raise a cluster of issues not actually intended to be settled in the Convention, but properly left to the terms of the undertaking and to the applicable law. For example, the question might arise as to whether the draft Convention was intended to regulate discrepancies or inconsistencies between authentication requirements under the terms of the undertaking and under the applicable law. In addition, it was suggested that mention of authentication might perpetuate notions not responsive to the evolution of documentation technology. The concern was further expressed that any definition mentioning authentication in conformity with applicable law would place a burden on the document checker beyond the scope of document checking, i.e., having to verify conformity with applicable law. It was suggested that it would be preferable to avoid the question altogether rather than to risk creating uncertainty by including a limited treatment of the matter.

55. While recognizing that subparagraph (h) was not intended to impose any authentication requirement but merely to "raise the flag" about authentication, the Working Group decided, in view of the concerns that had been raised, to delete the text referring to authentication.

56. As to the precise formulation of subparagraph (h), it was suggested that the word "representation" should be used instead of the word "communication", but that suggestion was not accepted.

Subparagraph (i) ("issuance")

57. The Working Group found the substance of subparagraph (i) to be generally acceptable.

Subparagraph (j) ("effectiveness")

58. Questions were raised as to the necessity of retaining the definition of "effectiveness" of the undertaking, added pursuant to an earlier decision by the

Working Group. The re-evaluation was prompted in part by the realization that the draft Convention was no longer using the twin term "binding and effective", as well as by the view that the matter was adequately dealt with in article 10 (1 bis). While support was expressed for retention of subparagraph (j) as a useful tool for distinguishing the notions of "effectiveness" and "irrevocability", the Working Group decided to delete the subparagraph.

CHAPTER III. EFFECTIVENESS OF GUARANTY LETTER

59. The Working Group agreed that it would consider in its review of the substantive provisions of the draft Convention which provisions should be mandatory and which should be non-mandatory.

Article 7. Establishment of guaranty letter

Paragraph (1)

60. The view was expressed that paragraph (1) should be regarded as an element of the scope of the draft Convention and that it might be combined with article 2 or otherwise referred to in chapter I. It was stated that such redrafting was necessary to make it clear that certain undertakings (e.g., an oral promise) that did not meet the form requirement specified in article 7 (1) should not be treated as illegal or invalid under the draft Convention but should merely be placed outside its scope of application. Support was expressed in favour of the view that the purpose of the draft Convention was not to invalidate such undertakings, which would, in certain legal systems, be recognized by other applicable rules of law. Examples were given of independent oral undertakings established in the context of individual relationships of a commercial or non-commercial nature, which might be valid under applicable rules of national law. In response, it was stated that the draft Convention should seek to unify the legal regimes applicable to independent undertakings. By placing purely oral undertakings outside its scope, the draft Convention would perpetuate or even create uncertainty and potentially give rise to difficult conflict-of-laws issues. It was stated that the unifying effect of the draft Convention should not be jeopardized merely for the purpose of recognizing the possible use of purely oral undertakings between private individuals in an international context, a situation which was described as marginal in practice. In addition, it was recalled that the same question had been raised at the fourteenth session of the Working Group in a proposal that the draft Convention should not establish any requirement of form or that it should exclude purely oral undertakings from its scope of application. At that session, the Working Group had not accepted that proposal, on the ground that purely oral undertakings created uncertainty and did not conform to sound banking practice (A/CN.9/342, para. 58).

61. After deliberation, the Working Group confirmed its position that the substance of paragraph (1) was generally acceptable.

Paragraph (2)

62. A concern was expressed that the reference in the same paragraph to the two notions of effectiveness and irrevocability might give rise to difficulties in the interpretation of the draft Convention. For example, it was suggested that, should a given undertaking be stipulated to become effective at a time that was different from the time of issuance, the text of paragraph (2) might be misinterpreted as implying that such an undertaking was not irrevocable until the time when it became effective. In response, it was stated that the notions of irrevocability and effectiveness were not linked. While the notion of effectiveness operated as a condition for demanding payment, irrevocability or revocability was a characteristic of the undertaking to be determined at the time of issuance. There was general agreement that any undertaking should be revocable or irrevocable as of the time when it was issued. Suggestions of a drafting nature were made to clarify that point beyond doubt by indicating that an undertaking was irrevocable unless, when issued, it was stipulated to be revocable, and that such an undertaking became effective at that time, provided that it did not state a different time of effectiveness. The Secretariat was requested to take those suggestions into account in the preparation of the next draft of article 7.

63. A question was raised as to whether an undertaking could become effective under the draft Convention irrespective of the fact that the beneficiary might refuse the benefit of the undertaking. In response, reference was made to article 10 (1) (a) and to the related, more general question of whether there was in fact a bilateral agreement between the guarantor or issuer and the beneficiary or whether the undertaking constituted essentially a unilaterally established obligation. It was recalled that that issue had been discussed previously (see A/CN.9/316, para. 120; A/CN.9/330, paras. 16 and 107; A/CN.9/372, para. 115) and that the Working Group had decided not to address it in the draft Convention in view of its controversial nature, given the different types of instruments involved.

Article 8. Amendment

Paragraph (1)

64. Divergent views were expressed with respect to the form requirement established in paragraph (1). One view, for which some support was expressed, was that, whatever the form requirement might be, it should be the same for the amendment of an undertaking as for the establishment of the undertaking itself. The text of article 8 (1) should thus parallel article 7 (1). In support of that view, it was recalled that among the possible reasons for requiring that the amendment be established in the form in which the corresponding undertaking was established might be the consideration that the amendment modified in part that undertaking. A contrary view was that paragraph (1) should be retained. It was recalled that the Working Group had discussed the same issue at its sixteenth session and that it had agreed that imposing the same form requirement for an amendment and for the establishment of the undertaking would be too restrictive in practice (A/CN.9/358, para. 89). That agreement had been confirmed by the Working Group at its eighteenth session (A/CN.9/372, para. 119)

and it was suggested that the debate should not be reopened at the present stage.

65. With regard to the difference in the substance of the form requirements contained in articles 7 (1) and 8 (1), it was questioned whether it would be appropriate for the draft Convention to authorize an amendment to be made in a form that did not preserve a record of the text of the amendment (i.e., in a purely oral form). It was noted that the current text would allow a purely oral amendment where such a form had been agreed upon by the guarantor or issuer and the beneficiary. The prevailing view was that, while such an agreement might rarely exist in practice, the draft Convention should not limit party autonomy in that respect. It was agreed, however, that the specific form of amendments envisaged by the parties had to be stipulated in the undertaking itself.

66. As a matter of drafting, the view was expressed that, in the context of paragraph (1), it should be made clear that the draft Convention envisaged possible amendments only as exceptions. It was thus suggested that more restrictive wording might be appropriate to indicate, through the use of a negative formulation, that an undertaking could not be amended, except in the form specifically stipulated in the undertaking or, failing such a stipulation, in a form referred to in article 7 (1).

67. After discussion, the Working Group requested the Secretariat to prepare a revised draft of paragraph (1) to reflect the above decisions.

Paragraph (2)

68. It was noted, at the outset, that both variants A and B established that, except for amendments consisting solely of an extension of the validity period, the consent of the beneficiary was necessary for an amendment to become effective but that the two variants differed as to the point in time at which an amendment became effective. General preference was expressed for variant B.

69. With respect to the words between square brackets ("or consisting solely of an extension of the validity period of the guaranty letter"), it was generally agreed that wording along those lines should be retained since such an amendment often resulted from a request by the beneficiary and, in any event, was beneficial to the beneficiary so that no consent needed to be required.

70. As a matter of drafting, it was generally felt that the opening words ("Unless otherwise agreed by the guarantor or issuer and the beneficiary") should be reconsidered with a view to making it clear that the agreement could be either embodied in the text of the undertaking or reached otherwise. It was also decided by the Working Group that, with respect to the situation where the agreement of the parties would be embodied in the text of the undertaking, the notion of "agreement" should be replaced by more neutral wording such as "stipulation", in order for the draft Convention to remain neutral as to whether the undertaking should be regarded as a bilateral agreement or as a unilaterally established obligation (see para. 63 above).

Paragraph (3)

71. The Working Group found the substance of paragraph (3) to be generally acceptable. It was decided that the reference to the rights and obligations of an instructing party should be retained.

Article 9. Transfer of beneficiary's right to demand payment

Paragraph (1)

72. A view was expressed that the scope of the draft Convention would lead to its application to instruments that, under some legal systems, were considered transferable without any specific authorization in the undertaking, and that the application of the rule in paragraph (1) to those instruments would therefore be problematic. In response to that concern, it was pointed out that the draft Convention was intended to be applied only to the limited range of undertakings referred to in articles 1 and 2. It was also noted that the draft Convention did not deal with transfer by operation of law or succession (e.g., due to the death of the beneficiary), a type of issue not dealt with in other UNCITRAL legal texts either. It was also understood that the provision in paragraph (1) would not bar a subsequent agreement to render a non-transferable undertaking transferable, something that would be accomplished through the amendment procedure under article 8 (2).

Paragraph (2)

73. It was noted that the current formulation of paragraph (2) reflected the decision of the Working Group to opt for a rule requiring that, for a transferable undertaking actually to be transferred to a particular transferee, the specific consent to the transfer had to be obtained from the guarantor or issuer. The utility and fairness of such a rule was questioned from the perspective that an undertaking designated as transferable should simply be that, transferable, without the need of the consent of the guarantor or issuer to the specific request to transfer. It was also questioned whether the solution in paragraph (2), based on a similar rule in the UCP, should be applicable to non-UCP instruments.

74. The prevailing view, however, was that the approach in paragraph (2) should be retained. Particular attention was drawn to the complexity of the transfer situation, in which the rule would usefully make it more likely that attention would be paid to concerns such as: ensuring that the documentation requirements were consistent throughout the chain; ensuring that proper account was taken of amendments; taking into account deadlines. It was felt that the specific-consent procedure would protect not only the issuer that had taken the probably inadvisable step of issuing a transferable undertaking without stipulating transfer procedures, but also the other parties to the transaction and the principal or applicant. The Working Group also decided to remove the inverted commas around the word "transferable" and to delete the words "or contains words of similar import", but to retain the words "or another authorized person".

Article 9 bis. Assignment of proceeds

75. A question was raised as to whether the procedure described in paragraph (2) might not be a matter better left to the general law of assignment of claims. Another suggestion was to retain the provision, but to alter the title to read "assignment of claim to proceeds". The view of the Working Group, however, was that article 9 bis was acceptable along its present lines. The provision was intended merely to deal with the right of the beneficiary to give specific payment instructions to the guarantor or issuer for proceeds generated by the payment demand by the beneficiary and with the discharging effect of any payment pursuant to such instructions; it did not otherwise deal with the law of assignment of claims, or with any claim as such, or with issues such as validity of assignment or the rights of creditors of the beneficiary. The Working Group noted that the reference to party autonomy would be patterned on the wording in that respect agreed for article 8 (2).

Article 10. Cessation of effectiveness of guaranty letter

Paragraph (1)

Subparagraphs (a) and (b)

76. The view was expressed that subparagraph (b) was redundant with respect to subparagraph (a), since agreement between the guarantor and the beneficiary as to the termination of the undertaking under subparagraph (b) would amount to renunciation by the beneficiary of its rights, a situation already addressed in subparagraph (a). Another view was that subparagraph (b) was redundant with respect to article 8, under which such an agreement would also be allowed. While support was expressed in favour of the deletion of subparagraph (b), the prevailing view was that subparagraphs (a) and (b) might cover somewhat different situations since release from liability under the undertaking and agreement on the termination of the undertaking were notionally different.

77. After deliberation, the Working Group found the substance of subparagraphs (a) and (b) to be generally acceptable. As regards the words between square brackets in subparagraph (b), it was generally felt that a reference to the form requirement of article 7 (1) should be retained so as to avoid a purely oral agreement as to the termination of the undertaking.

Subparagraphs (c) and (d)

78. Divergent views were expressed with respect to the words "unless the guaranty letter provides for its automatic renewal or for an automatic increase of the amount available or otherwise provides for continuing effectiveness" at the end of subparagraph (c). One view, which did not receive support, was that similar wording should be included at the end of subparagraph (d). The contrary view was that those words should be deleted from subparagraph (c). In support of deletion, it was said that, where the whole amount available under the undertaking had been paid, the undertaking would cease to be effective. It would not be necessary to refer to the automatic renewal since in that case it should be considered as if the whole amount had not yet been paid. The

prevailing view, however, was that the wording should be retained to accommodate the needs of certain instruments of a revolving nature, which might provide for automatic renewal either immediately after payment or after a stipulated period of time had elapsed. It was recalled that several suggestions for the inclusion of a reference to the undertaking as not having been "renewed or renewable" or to include some other specific language to cover the cessation of effectiveness in special cases such as revolving credits had been made at the sixteenth session (A/CN.9/358, para. 129).

79. After deliberation, the Working Group decided to retain the substance of subparagraphs (c) and (d).

Paragraph (1 bis)

80. A view was expressed that the text of the paragraph should indicate more clearly that the reference to "other rights or obligations of the beneficiary" was a reference to the rights and obligations of the beneficiary under the undertaking, as opposed to the rights and obligations the beneficiary might have under the underlying commercial transaction. In that connection, a question was raised as to what the rights and obligations of the beneficiary might be after the undertaking ceased to be effective. Examples of such rights and obligations that were mentioned in response include: the right to bring a lawsuit or to initiate arbitration proceedings; the right to seek payment from the issuer of the undertaking after expiration of the validity period in the case where a conforming demand for payment made to the confirmer of the undertaking was not honoured; the possible obligation to pay the bank fees where the beneficiary so agreed in the undertaking; and, in general, any rights and obligations of the beneficiary that might accrue after expiry of the undertaking.

81. After deliberation, the Working Group found the substance of the paragraph to be generally acceptable. In terms of drafting, it was agreed that reference should be made to the time when the rights and obligations of the beneficiary "accrued".

Paragraph (2)

82. The Working Group had before it two variants of paragraph (2) dealing with the possible legal significance of the retention or the return by the beneficiary of the instrument embodying the undertaking. Under variant A, paragraph (1) applied irrespective of whether any document embodying the undertaking was returned to the guarantor or issuer. The retention of any such document by the beneficiary would not preserve any rights of the beneficiary under the undertaking unless the parties agreed that the undertaking would not cease to be effective without the return of the document embodying it. Variant B established that, as a general rule, non-return of the undertaking would have no effect. At the same time, it recognized that the parties might wish to agree that return of the instrument, either alone or in addition to the events referred to in paragraph (1) (a) or (b), would be required in order to terminate the undertaking. However, any such agreement would have no effect beyond the expiry date or, if no expiry date was stipulated, beyond the period established in article 11 (c).

83. Considerable support was expressed for the retention of variant A and the deletion of the party-autonomy proviso ("unless the guaranty letter stipulates, or the guarantor or issuer and the beneficiary agree elsewhere, that the guaranty letter does not cease to be effective without the return of the document embodying it"). It was stated that such a clause would not reflect sound practice and that there was no role for party 26 autonomy to play in that case. A contrary view, however, was that a party-autonomy proviso was necessary to make the rule non-mandatory, thus taking due account of the fact that, in practice, guaranty undertakings would continue to be issued with clauses linking expiry to return of the instrument in countries that imposed a return requirement.

84. There was general agreement that the retention of the document embodying the undertaking should not preserve any rights of the beneficiary under the undertaking where full payment had occurred or, in any event, beyond the validity period of the undertaking as defined under article 11. It was decided that a mandatory provision in the draft Convention should reflect that understanding by the Working Group. A suggestion was made that paragraph (2) should be limited to setting forth that mandatory rule.

85. The Working Group, however, proceeded with a discussion of the extent to which return of the instrument before the cessation of effectiveness of the undertaking might carry legal significance. The view was expressed that in no instance should return of the instrument have such significance. It was suggested again that the text of variant A, without the party-autonomy proviso, should be retained and that the draft Convention should provide for no exception to that rule. With respect to a suggestion that release under paragraph (1) (a) could be effected by returning the instrument to the guarantor or issuer, it was said that no exception should be made to the rule that release should be issued in the form referred to in article 7 (1). In support of that view, it was stated that there might be difficulties with ascertaining what constituted a procedure functionally equivalent to the return of the instrument in the case of the issuance of the undertaking in non-paper form. It was also stated that return of the instrument, in itself, should not be equated with release since the instrument embodying the undertaking was merely a means of evidencing the undertaking, which was intangible in nature.

86. The prevailing view, however, was that parties should be allowed to stipulate in the undertaking, or otherwise agree, that an undertaking stipulating a date of expiry could cease to be effective prior to that date if the beneficiary released the guarantor or issuer by returning the instrument, either alone or in conjunction with one of the events referred to in paragraph (1) (a) or (b). It was stated that, should variant A be retained without any exception, the return of the instrument embodying the undertaking could never constitute one of the events referred to in paragraph (1) (a) or (b). It was generally agreed that such a consequence would be excessive since there seemed to exist no reason why the return of the instrument should not be allowed as one possible instance of an expiry event under article 11.

87. At the close of the discussion, the Working Group agreed that paragraph (2) should leave parties free to agree that return of the document embodying the undertaking to the guarantor or issuer, either alone or in conjunction with one

of the events referred to in subparagraphs (a) and (b) of paragraph (1), would be required for the cessation of effectiveness of the undertaking. It was also agreed that such an agreement should have no effect after payment or beyond the validity period of the undertaking. The Working Group found the substance of variant B to be generally consistent with that decision, although some redrafting may be necessary for purposes of clarity.

88. As a matter of drafting, it was generally felt that the final words of variant B ("any such stipulation or agreement has no effect beyond the validity period of the guaranty letter according to article 11") should be replaced by wording inspired from variant A along the following lines: "retention of any such document by the beneficiary after the undertaking ceases to be effective does not preserve any rights of the beneficiary under the undertaking". It was also felt that the text should contain wording to the effect that retention of any documents after full payment had been made should have no legal effect.

89. After deliberation, the Secretariat was requested to prepare a revised draft of paragraph (2) reflecting the above-mentioned decisions.

Article 11. Expiry

Subparagraph (a)

90. The Working Group found the substance of subparagraph (a) to be generally acceptable.

Subparagraph (b)

91. The view was expressed that, since the Working Group had decided not to provide for the conversion of non-documentary conditions into documentary conditions under article 3, no such conversion mechanism should be provided under article 11. It was thus suggested that the closing words of subparagraph (b) ("or, if no such document is specified, of a certification by the beneficiary of the occurrence of the event") should be deleted. The prevailing view, however, was that the conversion mechanism should be retained. It was generally felt that such a provision created no inconsistency with article 3, which dealt with the conditions under which payment could be made, while the provision under subparagraph (b) was dealing merely with the time of expiry of the undertaking.

92. A concern was expressed that, by establishing that non-documentary confirmation of an event should be converted into "certification by the beneficiary of the occurrence of the event", subparagraph (b) might create a situation where expiry would depend exclusively on action by the beneficiary, thus recognizing perpetual undertakings in cases where the beneficiary chose not to issue the required certificate. It was stated that, should subparagraph (b) result in the recognition of perpetual undertakings, stand-by letters of credit would need to be excluded from the scope of that subparagraph. In response, it was stated that no risk was created of potentially perpetual undertakings since both variants under subparagraph (c) established a maximum validity period that would apply in cases where occurrence of a stipulated expiry event had not been

established by presentation of the required certificate. With respect to stand-by letters of credit, it was noted that such instruments were intended to be excluded from the scope of variant B of subparagraph (c), which dealt with cases where the undertaking contained an express stipulation of indefinite validity. It was also noted that such instruments would in most instances be subject to article 42 of UCP 500 under which an expiry date had to be stipulated.

93. After deliberation, the Working Group found the substance of subparagraph (b) to be generally acceptable, subject to the decision to be made with respect to subparagraph (c).

Subparagraph (c)

94. The Working Group had before it two variants of subparagraph (c), which differed as to the manner in which they dealt with the question of undertakings of indefinite duration. Both variants provided for a five-year cap on the validity period and referred to the possibility of cessation of effectiveness by way of presentation of a document concerning the occurrence of an expiry event. However, variant B provided for an exception to the five-year cap for demand guarantees containing an express stipulation of indefinite validity. Under variant A, the parties could set a period longer or shorter than the default five-year period, but such an indefinite undertaking was not envisaged.

95. A view was again expressed with respect to the reference to an expiry event, found in both variants, that it would be unfamiliar in stand-by letter of credit practice and thereby lead to uncertainty. However, the Working Group found that aspect of subparagraph (c) to be acceptable, noting that provision had been made for the presentation of a document concerning the occurrence of the expiry event and for a time-limit on the exposure of the issuer. It was also generally agreed that the draft Convention should not deal with the relationship between the five-year cap and national rules on limitation periods for the filing of claims. As it had in the past, the Working Group took the view that the matter was beyond the purview of the draft Convention, in particular in view of differences at the national level as to the effect and operational rules of limitation periods.

96. Competing considerations were raised with respect to the two variants of subparagraph (c). Support was expressed for variant B on the ground that, by providing for undertakings of indefinite duration, it reflected the needs of the market-place. An allusion was made to the fact that in some countries the issuance of such undertakings was required by law or by practice, although the extent to which such requirements were still enshrined in law, or were rather a matter of practice, was questioned. The concern was expressed that, without the recognition of party autonomy contained in variant B, the acceptability of the Convention would be affected, in particular to the extent that guarantors in Convention States might fear losses due to inability to issue indefinite guarantees.

97. The prevailing view, however, was that the approach in variant A was preferable. In support of that preference, it was pointed out that the notion of indefiniteness would raise difficulties in legal systems that considered

indefinite or perpetual undertakings to be subject to unilateral dissolution. Another advantage of variant A was that it would not raise the need to differentiate between independent guarantees and stand-by letters of credit. It was also felt that sufficient allowance was made in variant A for party autonomy and the needs of the market-place, since the parties could utilize techniques such as stipulating distant expiry dates or automatic-renewal provisions to accomplish the objectives of indefiniteness without the uncertainty attendant to sheer indefiniteness.

98. As to the drafting of variant A, it was noted that the introductory portion was not intended to suggest that the undertaking could stipulate indefiniteness. It was suggested that the opening phrase of variant B was clearer and might be used instead. It was also suggested that it might be preferable to use the term "termination" to refer to cessation of the effectiveness of the undertaking prior to the expiry date. It was pointed out in response to the latter suggestion that the term "cessation of effectiveness" was meant to encompass "termination".

99. The Working Group next turned to the question of the point at which the five-year period provided in variant A should commence. The general preference, from the standpoint of clarity and predictability, was that it should commence with the issuance of the undertaking. The view was expressed, however, that the relevant moment should be the effectiveness of the undertaking, since otherwise the full five-year period would not always be available to the beneficiary, where a later time of effectiveness was stipulated on the undertaking. The suggestion was even made that the period should be lengthened to 10 years, since it might be judged to override national limitation-period rules. In response to those concerns, the Working Group decided to add an additional year to the five years already provided. It was noted that this would take into account the fact that, as shown by practice, the great majority of undertakings, if not effective upon issuance, would become so within a year of issuance.

100. During the discussion of subparagraph (c), the view was expressed that consideration should be given to dealing in the draft Convention with the effect of embargoes on the expiry of the undertaking, a problem that was said to arise and raise difficulties in practice. It was suggested that the matter might be considered on the basis of a study by the Secretariat or of draft provisions at the next session. Such draft provisions might provide for suspension of the running of the expiry period in the event of circumstances beyond the control of the beneficiary that prevented presentation of a demand for payment, for the period of the inability only. Such a policy orientation did not attract sufficient support. Furthermore, the prevailing view was that the question of embargoes and the wider range of related issues, including restraint-of-trade questions generally, were beyond the scope of the draft Convention, or at least should not be dealt with therein, and therefore did not merit the utilization of already scarce Secretariat resources in this forum. It was also noted that such matters were not addressed in other UNCITRAL legal texts and it was felt that any decision to embark in that direction would be better taken following consideration of the matter by the Commission.

CHAPTER IV. RIGHTS, OBLIGATIONS AND DEFENCES

Article 12. Determination of rights and obligations

Paragraph (1)

101. The Working Group found the substance of paragraph (1) to be generally acceptable. It was agreed that the word "specifically" should be retained to make it clear that the paragraph contemplated a reference by the parties to specific usages, not simply a general reference by them to usages.

Paragraph (2)

102. A view was expressed that the draft Convention should support only usages expressly incorporated by the parties, rather than also providing for the applicability of usages not referred to by the parties. In that connection, a question was raised as to whether paragraph (2) was consistent with paragraph (1), particularly in view of the adoption of a reference to usages "specifically" referred to by the parties in paragraph (1) (see para. 1 above). In response, it was stated that there was no inconsistency between the two paragraphs, which served two different purposes: paragraph (1) provided for the incorporation of usages by the parties as part of the undertaking; paragraph (2) was intended to establish a default rule for interpreting the terms and conditions of an undertaking in cases where questions arose, which had not been addressed by the undertaking itself or by the provisions of the draft Convention.

103. Another view was that the text of paragraph (2) should be combined with the provisions of article 5 since both provisions dealt with the interpretation of the draft Convention. It was generally felt, however, that paragraph (2) was not intended to establish merely a rule on the interpretation of the draft Convention but that it established a construction rule for specific rights and obligations under a given undertaking.

104. After deliberation, the Working Group found the substance of paragraph (2) to be generally acceptable, subject to possible drafting improvements to indicate more clearly the purpose served by the provision.

Article 13. Liability of guarantor or issuer

Paragraph (1)

105. With respect to the words between square brackets ("under the guaranty letter and this Convention"), it was generally felt that such wording was needed to make it clear that, under the draft Convention, the ambit of the reference to good faith and to reasonable care was confined to the realm of the issuer's obligations under the undertaking. Such obligations did not include any duties the issuer might have vis-à-vis its clients outside the context of the undertaking.

106. Various views and concerns were expressed as regards the use of the words "as determined with due regard to good guarantee or stand-by letter-of-credit practice". A concern was that a reference to "good" practice established a subjective criterion and that it might create uncertainty as to what would constitute "good" practice. In addition, it was stated that, at least in certain jurisdictions, a reference to "good" practice might produce the unintended result that determination of the applicable standards would be treated as a question of fact to be decided upon by a jury. It was thus suggested that those words should be replaced by a reference to "applicable standards of practice" or, possibly, "generally accepted international rules and usages of guarantee or stand-by letter of credit practice", wordings that would provide, in addition to a more ascertainable criterion, consistency with article 12 (2). In support of the suggested wording, it was stated that, with respect to independent guarantees and stand-by letters of credit, such standard practice would, to a large extent, be contained in the UCP 500 and in the URDG, which could be regarded as "good" practice.

107. In response, it was stated that, through a reference to "good" practice, paragraph (1) had been intended not to refer merely to existing standards or generally accepted practice, but to suggest a higher standard by providing a normative criterion that would make it possible to distinguish among standards, between those that constituted "good" practice and those that did not. Accordingly, support was expressed for the retention of the reference to "good" practice. The prevailing view, however, was that the term "good practice" could be replaced by a reference to "generally accepted" practice. It was recalled that the focus of paragraph (1) was on "good faith" and "reasonable care", which were not to be determined only by reference to either "good" or "generally accepted" practice but also by reference to the overall circumstances of the case. It was thus agreed that, even after deletion of the reference to "good" practice, the standard of good faith and reasonable care would remain as a higher standard than a mere reference to generally accepted practice.

108. Another concern was that references to practice contained in articles 13 (1) and 16 were expressed in different wordings. While the view was expressed that the same wording should be adopted in both articles, it was recalled that the Working Group at its nineteenth session had decided that it was useful to distinguish between standards applicable to two distinct phases of the document examination process: the standard of good faith and reasonable care to be followed by the issuer in examining the demand, i.e., in looking for any discrepancies; and the measure to be used in determining the weight or significance to be attached to certain minor discrepancies that might be found, i.e., whether the discrepancies should result in rejection of the demand (A/CN.9/374, para. 95). It was noted that this type of approach reflected practice, and was incorporated in article 13 of UCP 500.

109. As a matter of drafting, it was suggested that the qualifier "independent" should be added to the words "guarantee practice" to avoid misinterpretation of the draft Convention as addressing also guarantee undertakings of an accessory nature. It was also agreed that reference should be made to the "international" character of practices contemplated under paragraph (1).

110. After deliberation, the Working Group decided to replace the words "as determined with due regard to good guarantee or stand-by letter of credit practice" by the words "having due regard to generally accepted standards of international practice of independent guarantees or stand-by letters of credit".

Paragraph (2)

111. The Working Group found the substance of paragraph (2) to be generally acceptable.

Article 14. Demand

First sentence

112. The Working Group found the substance of the first sentence to be generally acceptable.

Second sentence

113. A proposal was made that, should the undertaking not specify the place where the time of effectiveness of the undertaking was to elapse, the draft Convention should establish that a demand for payment or any other document required by the undertaking was validly presented if it was dispatched by the beneficiary within the time of effectiveness (calculated at the place of business of the beneficiary), irrespective of whether it reached the guarantor or issuer before or after expiry (calculated at the place where the undertaking had been issued). No support was expressed for that proposal. It was generally agreed that the provision that documents had to be presented to the guarantor or issuer at the place where the guaranty letter had been issued should be interpreted as implying that documents had to be received by the guarantor or issuer within the time of effectiveness, that time being calculated at the place where the undertaking had been issued.

114. With respect to those specific cases where an undertaking would stipulate that payment was to be made by a bank other than the guarantor or issuer, it was generally agreed that such a stipulation should be interpreted as implying also that another place was stipulated in the undertaking.

115. After deliberation, the Working Group found the substance of the sentence to be generally acceptable.

Third sentence

116. A suggestion was made that, where a demand for payment was presented and no statement or other document was required under the guaranty letter, the draft Convention should establish an obligation for the beneficiary to issue a statement indicating that payment was due. While some support was expressed for the proposal, the prevailing view was that the suggestion would produce the undesirable result of prohibiting simple demand guarantees and clean stand-by letters of credit. It was recalled that the Working Group, at previous sessions, had discussed extensively the manner in which guaranty letters payable

on simple demand should be accommodated by the draft Convention and decided that it would not be appropriate for a legislative text such as the draft Convention to encourage or discourage the use of any specific type of guaranty letter. Instead, the draft Convention should take into account, and provide certainty for, all types of guarantees in use (see A/CN.9/361, paras. 20-21; A/CN.9/374, para. 82). The Working Group reaffirmed its earlier decision.

117. After deliberation, the Working Group found the substance of the sentence to be generally acceptable. As a matter of drafting, it was agreed that the words "statement or document" should be replaced by the words "certification or other document" to ensure consistency with the second sentence of the article.

Article 15. Notice of demand

118. In accordance with what had been agreed previously, the Working Group resumed its consideration of whether to retain article 15. (For the previous discussion of article 15 at the nineteenth session, see A/CN.9/374, paras. 86 to 92.) While the view was expressed that article 15 should be retained, in particular since it provided for party autonomy, the views were again stressed that article 15 should either be deleted, or, at the least, that the notice procedure provided therein should not be applied to stand-by letters of credit. It was suggested that the relevance of such a procedure to bank guarantees was evidenced by the fact that a similar procedure had been included in the URDG, while its inapplicability to stand-by letter of credit practice was said to be evidenced by the absence of a notice requirement in the UCP 500. Support for the retention of article 15, with its application limited to guarantees, was expressed in particular because of a concern that deletion of the provision might be interpreted as a preference in the draft Convention for the UCP approach, which did not provide for notice. Suggestions were made that, were article 15 to be retained, the second sentence should be deleted or clarified, in particular the words "entitles the principal or applicant".

119. While the above notion of blanket inapplicability of the notice procedure to stand-by letters of credit was questioned by reference to the actual practice, at least in some States, the Working Group concluded that it would be preferable to delete article 15. It was felt that a notice requirement should not be established by the draft Convention, but that the matter could be left to contractual disposition by the parties and to development in practice, a result that would flow from the deletion of article 15. It was also widely felt that, in the light of the views that had been expressed, the question did not merit providing expressly divergent rules for stand-by letters of credit, a divergence that up until that point had been avoided. It was further stated that the question essentially concerned the relationship between the principal or applicant and the guarantor or issuer and, as such, was beyond the intended ambit of the draft Convention. The Working Group also felt it important to note that the decision that it had taken was intended to render the Convention neutral on the question of a notice requirement of this type.

Article 16. Examination of demand and accompanying documents

Paragraph (1)

120. The question was raised as to whether it was sufficiently clear that the principal or applicant and the guarantor or issuer could agree to lower the standard of examination of the demand and accompanying documents. It was suggested that additional clarity might be useful, though such a rule could be inferred from the combination of articles 13 and 16. The Working Group, however, was reluctant to alter the basic approach set forth in paragraph (1). It was recalled that the current approach was the result of extensive deliberations at the nineteenth session and was based on the view that the draft Convention should focus on the relationship between the guarantor or issuer and the beneficiary. As had been the case at the nineteenth session, it was stated that the wording of the provision should not be construed as preventing the principal or applicant and the guarantor or issuer from establishing agreed standards.

121. From the standpoint of drafting, the Working Group noted that the upcoming Secretariat redraft would reflect the earlier decision of the Working Group that a demand for payment would be considered a "document" for the purposes of the draft Convention (A/CN.9/388, para. 110). Accordingly, a formulation such as "the demand and any other, accompanying documents" would be used. It was also noted that reference would be made to "independent guarantee", rather than simply to "guarantee", in line with the term used in the title of the draft Convention.

Paragraph (2)

122. The concern was expressed that the seven-day cap on the time allowed for examination of the demand for payment would raise difficulties for States in which clusters of holidays at given points of the year would render the rule in paragraph (2) inadequate. While it was recognized that the current reference to seven calendar days had been included to avoid immersing practitioners in differing understandings of "business" days, it was suggested that paragraph (2) also did not take adequate account of the needs of States in which weekends did not fall on the same days as in other regions. Alternatives proposed included five business days and seven business days at the place where the demand is to be made or at the place where the documents are to be examined. Though some hesitation was expressed that a seven-business-day rule would create uncertainty for beneficiaries, and that use of the word "business" would not take account of private guarantors or issuers, the Working Group settled on the seven-business-day approach. In doing so, the Working Group recognized that a distinction might be drawn between "business days" generally and those days on which guarantors or issuers were open for business ("banking days"). It was understood that paragraph (2) would make it clear that it was referring to the latter category (in line with article 13 (b) of UCP 500), so as to reflect the understanding of the Working Group that "business days" meant days when the guarantor or issuer was open for business.

Article 17. Payment or rejection of demand

Paragraph (1)

123. It was agreed that the intended effect of the second sentence should be made clearer, namely, that payment of a non-conforming demand would not deprive the principal or applicant of a right to refuse reimbursement to the guarantor or issuer in such a case. Such additional clarity might be achieved by deleting the words "and obligations" and using the words "does not prejudice" instead of "does not affect". It was also noted that the provision was not meant to override an agreed lower standard. The Working Group suggested that the provision should be redrafted to address the concerns that had been raised.

Paragraph (1 bis)

124. The Working Group noted that the reference to the beneficiary in paragraph (1 bis) was mistaken and should be replaced by a reference to the guarantor or issuer.

125. Differing views were expressed as to the decision to be taken by the Working Group on the retention or deletion of the paragraph. Support was expressed for deletion on the ground that the provision restated a principle (prompt payment of a conforming demand) that was self-evident in paragraph (1). Doubts about paragraph (1 bis) were also expressed on the ground that the meaning of the word "promptly" was unclear. Additional misgivings focused on the procedure provided for acknowledgement of conformity of a demand in the deferred-payment context. While some interest was expressed in such a procedure, it was generally felt to be unfamiliar to practice and not relevant as a Convention rule for cases of acceptance of a demand for payment rather than rejection, in which case a communication to the beneficiary was a necessary rule.

126. The prevailing view, which the Working Group adopted, was that paragraph (1 bis) served a useful purpose by stating clearly the principle of prompt payment, unless otherwise agreed, in which case payment should be made at the time stipulated. At the same time, it was agreed that no reference would be made in paragraph (1 bis) to acknowledgement of conformity of a demand in the deferred-payment context. The Working Group also noted that it would be made clear in the next redraft that the obligation to pay promptly followed the decision to pay, without affecting the time allowed under article 16 (2) for examining the demand and deciding whether to pay.

Paragraph (1 ter)

127. The Working Group decided to delete paragraph (1 ter). It was felt that the rule contained therein, that the guarantor or issuer could not avail itself of the financial difficulty of the principal or applicant to the detriment of the obligation to pay, was self-evident. It was also stated that the paragraph might be interpreted as suggesting the applicability of the draft Convention to the relationship between the principal or applicant and the guarantor or issuer.

Paragraph (2)

128. As had been the case previously, the concern was expressed that the rule in paragraph (2) was inappropriate, if not for all the undertakings within the scope of the draft Convention, at the least for stand-by letters of credit. The view was emphasized that, by mandating non-payment when the guarantor or issuer was shown facts that rendered the demand clearly improper, the draft Convention would place the document checker in the position of determining facts, a role that should be left to a court or other trier of fact. In this regard, the attention of the Working Group was drawn to the generally accepted principle of letter-of-credit practice, as reflected in article 15 of UCP 500, that the issuer was not responsible for the authenticity of documents. It was suggested that an acceptable alternative would be to give the guarantor or issuer the discretion not to pay in such cases. In support of such an approach, it was suggested that the obligation to act with reasonable care and in good faith would be sufficient to guide the guarantor or issuer in the event that it was shown evidence of fraud.

129. Having exhausted the time available for deliberations at the current session, the Working Group requested the Secretariat to prepare for the next session alternative formulations reflecting the views that had been expressed so as to facilitate further consideration of paragraph (2), without in any way prejudicing the discussion at the next session.

IV. FUTURE WORK

130. The Working Group decided, subject to approval by the Commission, that the next session would be held at Vienna from 19 to 30 September 1994.

131. The Working Group noted that it was the intent of the Secretariat to prepare for the next session a revised version of the draft Convention, implementing the decisions and conclusions of the Working Group.
