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# REPORT OF THE WORKING GROUP ON INTERNATIONAL CONTRACT PRACTICES ON THE WORK OF ITS TWENTIETH SESSION
(Vienna, 22 November - 3 December 1993)

CONTENTS



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## INTRODUCTION

1. Pursuant to a decision taken by the Commission at its twenty-first session,[1] the Working Group on International Contract Practices devoted its twelfth session to a review of the draft Uniform Rules on Guarantees 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 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 and nineteenth sessions (A/CN.9/372 and 374), the Working Group considered further revisions

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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.

of the draft articles (contained in A/CN.9/WG.II/WP.76 and Add.1), 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 twentieth session in Vienna, from 22 November to 3 December 1993. The session was attended by representatives of the following States members of the Working Group: Austria, Canada, China, Costa Rica, Egypt, France, Germany, Hungary, India, Iran (Islamic Republic of), Japan, Mexico, Morocco, Nigeria, Poland, Russian Federation, Saudi Arabia, Slovakia, Spain, Thailand, United Kingdom of Great Britain and Northern Ireland, United States of America and Uruguay.

7. The session was attended by observers from the following States: Armenia, Australia, Bolivia, Czech Republic, Finland, Indonesia, Myanmar, Nicaragua, Romania, Sweden, Switzerland, Turkey, Ukraine and the United Arab Emirates.

8. The session was attended by observers from the following international organizations: United Nations Industrial Development Organization (UNIDO) and the Hague Conference on Private International Law.

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.79), a note by the Secretariat containing articles 12 to 27 of the draft Convention (A/CN.9/WG.II/WP.76/Add.1) and 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.

## I. DELIBERATIONS AND DECISIONS

12. The Working Group discussed draft articles 18 to 27 as set forth in A/CN.9/WG.II/WP.76 and draft articles 1 and 2(1) as set forth in A/CN.9/WG.II/WP.80, with special attention to the question whether a given rule was appropriate for both independent guarantees and stand-by letters of credit or for only one type of those undertakings.

13. The deliberations and conclusions of the Working Group relating to draft articles 18 to 27, and 1 and 2(1) of the draft Convention are set forth below in chapter II. The Secretariat was requested to prepare, on the basis of those conclusions, a revised draft of articles 18 to 27 and 1 and 2(1).

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

### CHAPTER IV. RIGHTS, OBLIGATIONS AND DEFENCES (continued)

#### Article 18. Request for extension or payment in the alternative

14. It was recalled that, at the seventeenth session, the suggestion had been made that the extend-or-pay procedure was incompatible with stand-by-letter-of-credit practice and therefore should not apply to guaranty letters issued in that form. The Working Group noted that deletion of article 18 would have the same result, of the extend-or-pay procedure applying only to demand guarantees. This was because stand-by letters of credit were subject to the Uniform Customs and Practice for Documentary Credit (UCP), which did not address the extend-or-pay procedure, and demand guarantees were likely to incorporate the Uniform Rules for Demand Guarantees (URDG), which, in article 26, contained rules that were roughly comparable with those suggested in variant A. Accordingly, the Working Group decided to delete article 18.

#### Article 19. Improper demand

Chapeau

15. Two variants of the chapeau of article 19 were before the Working Group. Variant A duplicated some elements already contained in article 17 (2), namely the duty of the issuer to reject a demand as improper and the requirement that the improper nature of the demand should be known or manifest and clear to the issuer. This duplication was widely considered to be problematic and unnecessary. There was general agreement in the Working Group with the present structure of defining, in article 19, improper demand and indicating, in article 17 (2), the legal consequences of a demand being improper. The Working Group expressed its understanding that the reference in article 17 (2) to article 19 was only directed

to the definition of improper demand, and was not intended to relate to the reference in variant A to the manifestness of the impropriety. Variant B was preferred by the Working Group for its clarity and simplicity, and because it did not duplicate, or overlap with, article 17 (2).

16. It was noted that application of article 19 to any obligation of the issuer not to pay was reserved for discussion until the review by the Working Group of article 17(2). It was also stated that, were such a duty imposed, stand-by letters of credit would have to be excepted.

Subparagraph (a)

17. Views were exchanged as to the requirement in square brackets that the beneficiary should have knowledge of any document being forged in order for such a forgery to render a demand improper. One view was that subparagraph (a) should be formulated in more objective terms, which might be done by deleting the reference to the knowledge of the beneficiary. It was stated that, since the forged character of a document should be objectively perceivable, or "clear beyond doubt" to a "reasonable person", and the determination as to whether a document presented in support of a demand for payment was forged would typically be made by the issuer of the guaranty letter, there was no need for any assessment as to what the beneficiary knew or ought to have known. It was therefore suggested that the subparagraph should be redrafted as follows: "It is clear beyond doubt that any document is forged". The Working Group, while it was open to the suggestion to remove the reference to the knowledge of the beneficiary, did not opt to include language relating to the degree of proof required. As noted in the discussion of the chapeau, it was agreed that that was a matter that should be dealt with separately, in article 17.

18. With respect to the use of the words "any document is forged", the view was expressed that the notion of forgery might have a rather technical meaning in some jurisdictions, thus resulting in the characterization of a demand as improper even though the falsification concerned was insignificant in that it did not alter the commercial balance of the transaction, and perhaps was even carried out unbeknownst to the beneficiary. It was pointed out that, for example, under existing case law in a number of countries, the presence of a forged date on a bill of lading presented in support of a demand for payment under a guaranty letter, without the beneficiary being aware of the forgery, would not necessarily affect the validity of the demand. It was therefore suggested that wording should be added along the following lines: "or is otherwise fraudulently completed", particularly if the reference to the knowledge of the beneficiary were deleted. It was recalled, however, that the Working Group had earlier decided that use of terms such as "fraud" or "abuse" should be avoided. An alternate suggestion was to refer to forgery that was "material". The prevailing view, however, was that the current reference to forgery should be maintained, subject to the deletion of the reference to the knowledge of the beneficiary.

Subparagraph (b)

19. A discussion took place as to whether subparagraph (b) should be retained. In support of deletion of the subparagraph, it was noted that the situation dealt with under subparagraph (b) could be described as a subset of the more general situation encompassed by

subparagraph (c). In that connection, the view was expressed that the scope of the paragraph was questionable, since the Working Group had already decided that simple demand guarantees should be covered by the draft Convention, thus making the words between square brackets ("on the basis asserted in the demand and the supporting documents") unnecessary. In support of retention of the subparagraph, it was stated that, while subparagraphs (b) and (c) might overlap, subparagraph (b) was needed to deal with the particular situation where the basis of a demand was limited by the text of the guaranty letter itself, for example in the case where non-performance of a given obligation would need to be asserted to obtain payment under a performance bond. Reference was made to the case where there was an internal inconsistency among documents submitted in a demand for payment. In the case where an apparently conforming demand for payment would be made by the beneficiary in such a situation, and the issuer would know that the guaranteed obligation had been satisfactorily performed, it was stated that subparagraph (b) was needed to make it clear that the issuer was under no obligation to investigate beyond the assertions of the beneficiary whether another basis for a demand would be conceivable, as might mistakenly be concluded from reading subparagraph (c). It was stated in response that banks were unable to make some of the determinations called for in subparagraph (b), whereas courts could do so and that accordingly there could be no such duty. The prevailing view was that subparagraph (b) should be retained.

20. As regards the contents of subparagraph (b), it was noted that the knowledge of the beneficiary was a pre-condition for the applicability of subparagraph (b). It was suggested that, for the same reasons that similar wording had been deleted from subparagraph (a), the opening words ("the beneficiary knows or cannot be unaware") should be deleted. In response, the concern was expressed that the requirement of knowledge on the part of the beneficiary was necessary to protect the beneficiary acting in good faith, who had presented a demand for payment without knowing that no payment was, in fact, due. It was stated that such a protective measure for the beneficiary acting in good faith existed in case law in a number of countries, and was a factor in providing certainty and reliability of the instrument. The prevailing view was that, irrespective of whether the beneficiary was aware or not of the manoeuvres that resulted in a demand being made where payment was not, in fact, due, no payment should be authorized by the draft Convention in such a case.

21. After discussion, the Working Group decided that subparagraph (b) should read as along the following lines: "no payment is due on the basis asserted in the demand and the supporting documents".

Subparagraph (c)

22. The Working Group found the substance of subparagraph (c) to be generally acceptable.

Paragraph (2)

23. It was noted that the purpose of paragraph (2) was to describe some typical cases in which it was evident that a demand had no conceivable basis. Two variants were before the Working Group, reflecting the proposals that had been made at the seventeenth session.

Variant X contained a general formula of lack of conceivable basis setting forth a number of cases in which the impropriety of the demand was generally clear and unambiguous. Variant Y contained a non-exhaustive list of particular situations arising under different types of instruments.

24. Differing views were expressed as to whether paragraph (2) should be retained. One general observation was that the definition of improper demand set forth in paragraph (1) was sufficient and that the difficulty in identifying clear cases in which it was evident that a demand had no conceivable basis would weaken the impact of paragraph (2). In that regard, a number of suggestions were made. One suggestion was that the contents of variants X and Y could be reflected in a commentary, thus eliminating paragraph (2). Another suggestion was that variants X and Y could be deleted and the matter of fraud and other problems arising in connection with the underlying transaction could be addressed elsewhere in the Convention, with an orientation towards the role of the courts rather than the duty of the issuer. Yet another suggestion was that variants X and Y could be deleted on the condition that a reference to the underlying transaction would be added to paragraph (1)(c) along the lines of "with due regard to the underlying obligations". In that regard, it was observed that the suggested addition to paragraph (1)(c) might cause uncertainty as to the extent to which the underlying transaction could be taken into consideration in the determination of what was an improper demand.

25. The prevailing view, however, was that paragraph (2) should be retained since it would serve as a useful guide as to when a demand had no conceivable basis.

26. Differing views were expressed as to the two variants of paragraph (2). Some support was expressed for variant Y on the ground that it contained a list of different cases that could arise with regard to different types of guaranty letters, which could serve as a guide. Support was also expressed for combining variants X and Y. In that regard, it was observed that variant X and Y were not mutually exclusive, as variant X contained general rules and variant Y a list of different situations. Another observation was that paragraph (2) should cover only the most evident cases in which a demand had no conceivable basis and should be recast so as to apply in the context of judicial proceedings. The broadest degree of support, however, was expressed for, variant X on the ground that it was simpler and clearer. It was noted that it gave a non-exhaustive list of general situations in which a demand had no conceivable basis.

27. Regarding the content of variant X, one concern was mentioned that subparagraph (b) raised the spectre of the issuer having to determine matters outside the issuer's area of expertise such as whether the court had jurisdiction and the legal value of an arbitral award. Another concern was that subparagraph (b), which provided that the demand would have no conceivable basis if the underlying obligation had been declared invalid by a court or an arbitral tribunal, was overly broad, since there might be cases in practice in which a guaranty letter was issued to cover precisely such a contingency. It was suggested that the problem might be resolved by making subparagraph (b) subject to the right of the parties to agree otherwise in the guaranty letter. A related suggestion was that the entirety of paragraph (2) should be subject to party autonomy. A concern was expressed that such a modification would allow the parties to exclude even the most serious cases of improper

demand, which could run counter to public order. The Working Group therefore agreed on a more limited modification, namely, to include in the next draft language in brackets indicating that the parties could provide in the guaranty letter that a demand would not be improper in case that at least one of the purposes of the guaranty letter was to cover the risk that the underlying transaction had been declared invalid by a court or an arbitral tribunal.

28. Another concern was that variant X did not cover the case in which there was a manifest disproportionality between the damage suffered and the amount claimed under the guaranty letter, a concern which had been expressed at the seventeenth session of the Working Group. In that regard, it was suggested that the manifest disproportionality idea should be covered, either under subparagraph (c) of variant X or under a separate new subparagraph (e), by the addition of language along the lines of "the amount demanded is manifestly disproportionate to the damage suffered". That suggestion failed to attract sufficient support, in particular since that situation was not one of complete lack of a basis for the demand and since it addressed a problem that could be dealt with by including in the guaranty letter a reduction mechanism.

29. The view was expressed that subparagraph (d) was ambiguous, in particular since it might be difficult for the issuer to determine the reasons for which the principal had not fulfilled the underlying obligation. In addition, it was said that there were a number of other acts or omissions of the beneficiary, beyond wilful misconduct, that might prevent fulfilment of the underlying obligation, which would indicate that there might not have been a basis for the demand. However, the suggestion made to delete subparagraph (d) did not meet with the approval of the Working Group.

30. After discussion the Working Group requested the Secretariat to prepare a revised draft of paragraph (2) along the lines of variant X, subject to the amendment agreed upon for subparagraph (b), so as to cover cases in which it was evident that the demand had no conceivable basis.

## Article 20. Set-off

31. It was recalled that the wording "by availing itself of a right of set-off" had been chosen in variant A, instead of the wording "by means of a set-off", in view of the understanding of the Working Group that the general law of set-off might impose further restrictions (A/CN.9/361, paras. 97-98). Taking this understanding one step further, variant B merely presented the restriction and prohibited, for claims assigned by the principal, the exercise of any right of set-off available under the general law of set-off. General preference was expressed in favour of the approach taken in variant A, which was said to express more clearly the principle that set-off would be available in the context of guaranty letters.

32. With respect to the opening words ("Unless otherwise agreed by the parties"), it was generally agreed that the principle of party autonomy should be mentioned with respect to set-off. It was generally felt that the principle of party autonomy should apply to the entire article, including the exception set forth at the end of variant A ("excepting any claim assigned to the issuer by the principal"), which the parties should also be allowed to waive.

As regards the use of the words "the parties", a concern was expressed that the mere reference to "parties" might not allow, in the case where payment was made by a bank that was not the issuer, that paying bank to avail itself of a right of set-off with a claim it might have against the party demanding payment. It was suggested that the words "the parties" should be replaced by "the party paying under the guaranty letter and the beneficiary". The suggested wording was objected to on the grounds that the relationship between the beneficiary and parties that were neither issuers nor principals was not regulated by other provisions of the draft Convention and, for the sake of consistency, no different solution should be adopted with respect to article 20. It was noted that, as in the rest of the text of the draft Convention, the words "the parties" would be replaced by the words "the guarantor or issuer and the beneficiary", pursuant to a decision made at the nineteenth session. It was noted, however, that article 9(3) referred to the party effecting payment.

33. With respect to the reference to the law of insolvency ("subject to the provisions of the law of insolvency"), the view was expressed that no such reference was needed. It was stated that the reference to the law of insolvency might raise difficulties as to which national law would apply, i.e., the law of the country of the guarantor, of the country of the beneficiary, or of the place of payment. Furthermore, the reference might cause uncertainty where bankruptcy had been adjudicated in several jurisdictions. In that connection, it was suggested that article 20 should establish the rule that only liquid obligations could be set-off under the draft Convention. The view was also expressed that the interplay of the draft Convention with the law of insolvency should be left to national legislation, particularly in view of the complexity of legal mechanisms dealing with priorities in secured transactions in cases of bankruptcy. Furthermore, a question was raised as to the appropriateness of singling out the law of insolvency from among all specific pieces of legislation that might interplay with the text of the draft Convention. While some support was expressed for the retention in the text of variant A of a reference to the law of insolvency, the Working Group decided, after discussion, that the reference should be deleted.

34. With respect to the substantive rule set forth in variant A ("the issuer may discharge its payment obligation under the guaranty letter by availing itself of a right of set-off with a claim against the person demanding payment"), the view was expressed that the notion of set-off should be defined in the draft Convention. It was recalled that, in the law of certain countries, set-off was restricted to claims of the guarantor arising out of the same transaction as the beneficiary's claim, while the law of other countries contained no such restriction. The Working Group, however, reaffirmed the decision made at its seventeenth session that the matter should be left to the general law of set-off in each country (see A/CN.9/361, para. 98) and noted that the words "avail itself of a right of set-off" were meant to reflect that deferral to national law. In that connection, a concern was expressed that article 20 might be misinterpreted as attempting to create rights of set-off where no such rights already existed in national law. It was thus suggested that the rule contained in article 20 should expressly be established "subject to the general law of set-off". It was recognized, however, that such a reference to the "general" law of set-off did not make it abundantly clear that any prohibition of set-off in matters related to guaranty letters should be displaced by the text of the draft Convention.

35. With respect to the words "with a claim against the person demanding payment", a concern was expressed that, in the case where the right to payment had been transferred by the beneficiary, set-off would not be available with a claim against the previous beneficiary. It was felt, however, that the legal position of the transferee under the draft Convention should not be more favourable than that of the previous beneficiary, i.e. the transferor. After discussion, the Working Group decided that the words "with a claim against the person demanding payment" should be deleted.

Paragraph (3) of Article 9 bis

36. Recalling the decision at the nineteenth session to consider the issue of set-off in the context of assignment of proceeds following a further review of article 20, the Working Group engaged in a discussion of paragraph (3) of article 9 bis. Two variants of paragraph (3) were before the Working Group (A/CN.9/WG.II/WP.80). Variant X expressly limited the right of set-off to claims against the beneficiary, thus excluding any possible claims against the assignee. Variant Y was a general provision which did not deal with that question.

37. The Working Group considered whether paragraph (3) should be retained or deleted. Retention of paragraph (3) was urged on the ground that it usefully clarified the circumstances under which the right of set-off could be exercised. The counter-view was that paragraph (3) should be deleted, since it touched upon the general law on set-off, which should be left to national law, as had been agreed in the review of article 20. While there was a general inclination to delete paragraph (3), the Working Group paused to consider the relative merits of variants X and Y. Some support was expressed for variant X on the ground that it was consistent with paragraph (1) of article 9 bis, which dealt with assignment of sums of money and not of claims. At the same time, variant X was criticized for adversely affecting rights of set-off under national laws. Variant Y attracted more support, on the ground that it was a more general provision, without the drawbacks of variant X. However, after deliberation, the Working Group decided to delete paragraph (3).

## CHAPTER V. PROVISIONAL COURT MEASURES

### Article 21. Preliminary injunction [against issuer or beneficiary]

General remarks

38. As had been the case at the seventeenth session, various opinions were expressed on the question of preliminary injunctions (see A/CN.9/361, paras. 102-103). There was a degree of hesitation to incorporate article 21 in the draft Convention, in particular to the extent that the article contained procedural rules on matters that were treated differently from State to State and that might better be left to local law. It was suggested that the acceptability of the draft Convention would be adversely affected if it presented legislatures with the prospect of having to revamp, for one particular area of the law, established rules governing injunctions generally. It was also pointed out that for some States the injunctive

relief envisaged in the draft article would be unfamiliar. In the light of the above, it was suggested that the article should be deleted, or at least directed only at those States in which injunctions were a recognized measure. As a possible alternative to complete deletion of article 21, it was also suggested that the draft Convention, while it should not attempt to establish any procedural rules, might contain a broad statement of principles, along the lines of the former article 23, deleted by the Working Group at its seventeenth session (see A/CN.9/361, paras. 119-121).

39. In favour of retaining a provision on injunctions, it was stated that such a provision was an integral element of the provisions dealing with fraud and abuse; it was pointed out that one of the main purposes, if not the main purpose, of preparing the draft Convention was to provide some solutions in this area, which was beyond the scope of instruments at the contractual level (e.g., UCP and URDG). It was also suggested that it was not the intent of the draft article to bring about drastic changes in current national procedures, although it was said to be precisely because of the diversity in national approaches that it would be salutary to include the provision in question in the draft Convention. To the extent that injunction procedures did not exist in some States, retention of provisions on injunctions was said to have the benefit of providing guidance to those States in formulating such provisions. Both with respect to such States, as well as to the problem of diversity of national approaches, inclusion of provisions on preliminary injunctions was said to be beneficial for international uniformity and for protection of the integrity of the guaranty letter.

40. After discussion, the Working Group decided to proceed with the consideration of draft article 21; the Working Group agreed to consider further the question of whether to retain article 21 after reviewing the contents of the draft article. Reference was made to the advisability of considering the matter after the Secretariat has had an opportunity to present a revised version of article 19 taking into account the deliberations at the present session (see above, paras 15 to 30). It was also noted that, in the context of an international convention, the possibility of allowing for reservations to be made by States at the time of ratification or accession with the effect of excluding application of article 21 would need to be discussed at a later stage.

Title

41. The view was expressed that, at least in certain countries, the term "preliminary injunction" might not adequately reflect the procedural techniques through which a court would typically issue a temporary decision aimed at preventing the beneficiary from collecting the benefits stipulated in the guaranty letter. It was generally agreed that a more neutral wording would be preferable. It was suggested, for example, that the article should refer to "court measures against acceptance or payment under a guaranty letter". While no specific wording was adopted by the Working Group, it was agreed that, in addition to being more neutral, the title should also emphasize the "provisional" or "temporary" character of court measures considered under article 21.

42. As regards the terms within square brackets ("against issuer or beneficiary"), it was felt by the Working Group that establishing a limitative list of persons against whom provisional measures might be sought in the context of article 21 might overly restrict the

discretion of the courts to order provisional measures that might be relevant in certain countries in the context of an improper demand under a guaranty letter. The Working Group decided to delete those terms.

Paragraph (1)

"Where [, on an application by the principal]"

43. It was generally agreed that provisional court measures should only be ordered on the basis of "an application", rather than also on the initiative of the court. Various concerns were expressed with respect to paragraph (1) being limited in scope to situations where an application for provisional court measures was made by the principal. A first concern was that the current text would result in provisional court measures being unavailable to the guarantor or issuer. It was stated that it was conceivable, although article 17 established an obligation for the guarantor or issuer not to pay when a demand was manifestly and clearly improper, that the guarantor or issuer itself might apply for a court decision enjoining it from paying under a guaranty letter, particularly in situations where an improper demand was expected to be made. Another concern was that reference to an application by the principal might prevent other persons, for example a liquidator, to substitute their application for that of the principal. It was generally felt that, with respect to provisional measures, access to a court should be given to all persons that had an interest in preventing payment in case of an improper demand. It was realized, however, that it would be difficult to establish an exhaustive list of such persons and that a general rule on access to courts by all persons having a legitimate interest to stop payment might conflict with national laws regarding such issues as standing to sue. After discussion, the Working Group decided to delete the words "by the principal". (The discussion on that issue was reopened in the context of paragraph (5) and the above decision was modified, see below, para. 72).

"it is manifestly and clearly shown"

44. A discussion took place as to whether article 21 should establish a standard of proof to be applied by a court in deciding on an application for provisional measures to stop payment. In favour of deleting any reference to a standard of proof, it was stated that issues regarding the level of proof should be left to applicable procedural law and that the text should not limit the discretion of courts. It was thus suggested that, instead of establishing a standard of proof, article 21 should merely refer to cases where "the court is convinced that a demand is improper". In the same vein, another suggestion was to replace the current text of paragraph (1) by the following: "A competent forum, according to the requirements of its procedural law, may issue a preliminary order in case the demand made by the beneficiary is improper in the sense referred to or prescribed by article 19, enjoining the issuer from meeting the demand". It was generally felt that such a text would not contribute to the harmonization of law in the field. In favour of establishing a standard of proof, it was stated that an important feature of the draft Convention would be to establish a "level playing field" i.e., equality of treatment for users of guaranty letters in countries where, currently, the possibility to interfere with the obligation to pay under a guaranty letter was interpreted restrictively by the courts and in countries where courts, particularly in the context of

provisional measures, were more open to allowing for exceptions to the payment obligation.

45. As to the substance of a possible standard of proof, a question was raised as to whether the standard of proof set forth for provisional court measures in the context of article 21 should be parallel to the standard of proof set forth for refusal to pay by the guarantor or issuer under article 17. The view was expressed that the highest possible standard of proof should apply equally to both situations, in order not to jeopardize the reliability of the guaranty letter. The following text was suggested: "A court shall not interfere with the obligation to honour a guaranty letter or with presentation of documents to obtain payment under such a guaranty letter unless, in addition to complying with its regular procedures, it finds that the demand is manifestly and clearly improper and will result in serious harm to the applicant". Among the reasons given for applying the same standard of proof in articles 17 and 21, it was said that both articles were geared to protecting the principal. Under article 17, the principal was entitled to have the guarantor refuse payment in case of improper demand. Similarly in the context of court measures, the principal was entitled to seek protection from courts if irreparable harm would result from payment. It was stated that the judge, in making a decision under article 21, would be placed in the shoes of the guarantor in determining whether the demand was manifestly and clearly improper.

46. It was generally agreed, however, that the respective contexts in which articles 17 and 21 applied were of a different nature and that standards of proof to be applied in the two contexts might differ. The standard of proof under article 17 was to be applied by the guarantor or issuer in determining whether, on the face of a demand, it was sufficiently clear that a demand was improper for the issuer to be obliged not to pay. Among the reasons given for making the standard of proof as high as possible under article 17 were the following: the guarantor or issuer who would make a determination as to the improper character of a demand should not be allowed to escape easily, through such a determination, from its original obligation to make payment upon demand; a high level of proof was also needed to provide a valid excuse for the bank that did not refuse payment on the basis of mere allegations by the principal that the demand was improper. As regards the standard of proof to be applied by a judge under article 21, it was stated that the above considerations should not apply, in particular in view of the provisional nature of the measures being treated.

47. Various views were expressed as to the standard of proof to be applied by the court. One view was that the standard should be the highest possible in order not to jeopardize the reliability of the instrument by allowing courts to dictate various standards. In that connection, it was also stated that the standard of proof should be high in view of the fact that, in many jurisdictions, a preliminary injunction or other provisional court measure would be granted by the court in the context of an ex parte procedure, i.e., without the defendant being given an opportunity to be heard. It was stated, however, that providing in the draft Convention that a judge should determine whether a demand was "manifestly and clearly improper" would in many jurisdictions result in no provisional measures being available, since a determination as to the "manifestly and clearly" improper character of a demand could be made only by the court that would make the final decision on the merits of the demand. In favour of adopting a slightly lower standard of proof, it was stated that, in

most jurisdictions where provisional court measures were in existence, the standard to be applied referred to notions such as "high probability", or "very high likelihood" that a demand was improper, or "high probability of success on the merits" of the case. It was stated that such slightly lower standards of proof were still considered to be difficult to meet and that a temporary order restraining payment on the basis of such standards would, in many countries, be valid only for a few days. As a possible improvement for such standards, it was suggested that the draft Convention should contain a reference to the notion of "liquid proof". Another view was that, with respect to the standard of proof to be applied by a court, a lower standard should be adopted, for example, "the court is prima facie satisfied", "it is seriously arguable", or " the court has reasonable grounds to believe" that the demand is improper. It was widely felt, however, that a low standard along those lines, while not limiting the discretion of the courts, might jeopardize the reliability of the guaranty letter.

48. After discussion, the Working Group decided that a standard of proof relying on the clearly and manifestly improper character of the demand was too high in the context of provisional court measures and that the test to be included in a future draft should be along the lines of a "high probability" that the demand was improper.

"[by documentary and other readily presentable means of evidence]"

49. The view was expressed that the words between square brackets should be deleted in order not to impinge on the discretion of the courts. Another view was that the need for courts to base a decision on documents and other readily presentable means of evidence was linked to the definition of an improper demand under article 19. The view was also expressed, however, that a reference to the "liquid" (i.e., readily available) character of the proof to be taken into account by the court might still need to be added to the current text, which might otherwise be considered to be too vague. After discussion, the Working Group decided to delete the words between square brackets.

"that a demand made [or expected to be made] by the beneficiary is improper according to article 19,"

50. It was generally agreed that there existed a need for allowing anticipatory injunctive relief, which might be particularly relevant in the context of a guaranty letter with successive payments. The Working Group decided to maintain the words "or is expected to be made".

"[the] [a competent] court may issue a preliminary order:"

51. It was generally felt that the reference to "a competent" court could be misinterpreted as an attempt to create specific grounds for judicial competence. The Working Group decided to delete the words "a competent".

Subparagraphs (a) and (b)

52. The Working Group considered the merits of subparagraphs (a) and (b). Subparagraph (a) provided for two types of provisional orders directed against the issuer,

one order precluding the issuer from paying on demand and another, within brackets, precluding the issuer from debiting the account of the principal. Subparagraph (b) provided for three types of provisional orders directed against the beneficiary, one enjoining the beneficiary from accepting payment, a second ordering the beneficiary, in case a demand was made, to withdraw the demand, and a third ordering the beneficiary, in case a demand was imminent, not to make a demand.

53. The Working Group reviewed the contents of the subparagraphs in order to assess whether it was appropriate to include the type of listing of possible measures envisaged in the present draft. No objections were raised to mentioning, in subparagraph (a), the order enjoining the issuer from meeting the demand for payment. Views differed, however, as to the appropriateness of referring to the order enjoining the issuer from debiting the account of the principal. One view was that making express provision for this type of injunctive relief for the principal was in line with the general purpose of article 21, which was said to be to protect the interests of the principal. It was pointed out that, as a practical matter, an order enjoining the issuer from debiting the account of the principal would in many cases be more important for the principal than to obtain an injunction, against payment to the beneficiary, since a payment in contravention of article 17 would be at the risk of the issuer.

54. The prevailing view, however, was that providing for such a provisional order was problematic. Views that combined to swing the Working Group in favour of deletion included that such an order: could leave the issuer enjoined from debiting the account of the principal, but still obligated to pay the beneficiary; concerned an aspect of the principal-issuer relationship and was therefore not within the main focus of the draft Convention; since the draft Convention in specifying the rights and obligations of the parties made no reference to debiting of accounts, such a reference in article 21 should be avoided. As an alternative to deletion, it was suggested that the two kinds of injunctions could be joined by replacing the word "or" by the word "and", with the effect that the two measures could be treated as a package, thereby eliminating the possibility of the issuer being placed under conflicting obligations. However, that suggestion failed to attract sufficient support.

55. Differing views were expressed as to whether subparagraph (b), which provided for provisional measures to block the beneficiary from taking steps to obtain payment, should be retained or deleted. One view was that subparagraph (b) would in principle not be objectionable, if a number of modifications were made to make it clearer. One observation was that the notion of acceptance of payment was unclear, would not be uniformly understood and could be replaced by a reference to collection of the proceeds. Another suggestion was that the order ordering the beneficiary to withdraw the demand should be deleted. Yet another suggestion was that the words "enjoining the beneficiary ... " were not appropriate and should be replaced by language along the lines of "declaring that the beneficiary may not accept payment". The prevailing view, however, was that modifications of that type would not overcome the difficulties that they were meant to address and that subparagraph (b) should therefore be deleted. In support of deletion, it was said that the nature of the injunction provided in subparagraph (b) was unclear, that it was unknown in many jurisdictions, and that subparagraph (a) was sufficient. A concern was also expressed that an order ordering the beneficiary not to make or to withdraw a demand might result in his failure to submit a timely demand, if in the meantime the expiry date passes.

56. The discussion of the remedies mentioned in subparagraphs (a) and (b), and the inclination to eliminate mention of some of them, prompted the Working Group to consider whether to use an approach other than one attempting to enumerate, in an exhaustive or indicative way, types of measures that would be available to the parties. It was suggested in this vein that subparagraphs (a) and (b) should be replaced by a general rule along the lines of "the court may take any measure which would protect the interests of the principal and the issuer", with a clear emphasis on the provisional nature of the measures. After discussion, it was decided that language along the following lines might be added to the end of the chapeau of paragraph (1) so as to replace subparagraphs (a) and (b): "a provisional order to the effect that the beneficiary shall not receive payment".

Closing proviso to paragraph (1)

57. A number of concerns were expressed as to the wording of the proviso at the end of paragraph (1). That proviso made the granting of the provisional orders envisioned in paragraph (1) subject to the requirement that the principal would have to suffer "serious harm" or, in an alternative formulation, "irreparable loss" as a result of a refusal by the court to grant the order.

58. One concern was that the words "provided that" were too strong in restricting the court's discretion to consider the risk of damage to the principal, and would contradict national procedural rules providing for such a discretion. It was, therefore, suggested that language along the lines of "taking into account that" would be more appropriate. While the concern was raised that such language might not be sufficiently clear as a guideline for courts, the Secretariat was requested to attempt to incorporate a wording along those lines.

59. Another concern was that the words "the refusal of the court" might suggest that the court could be held responsible for the damage that might be caused to the principal should the provisional measure not be granted, when in point of fact that responsibility lay with the beneficiary submitting an improper demand. Yet another concern was that the words "would cause" might reduce the possibility of the granting of a provisional measure, since it would be very difficult to prove with certainty that serious damage would be caused. Language along the lines of "would be likely to cause" was, therefore, suggested.

60. Various views were presented as to the alternative presented in the proviso within brackets for expressing the degree of the damage that would have to be likely to result from a refusal to grant the provisional measure being sought. One view was that the words "irreparable loss" were preferable since they were clearer and, combined with the word "loss", better reflected the financial character of the damage that would result for the applicant. However, the word "irreparable" was criticized as being vague and potentially too high an across-the-board standard to set, since the principal, if it succeeded on the merits at a later stage, might eventually be able to retrieve funds that it had paid to cover the payment of an improper demand. It was suggested that the word "serious", combined either with the word "loss" or the word "harm", would suffice. Another view was that "irreparable loss" was too high a standard and "serious harm" was too low, and that the words "not easily reparable" should be used instead. Yet another view was that either standard could be accepted. A further view was expressed to the effect that the guarantor or

issuer would not be entitled to reimbursement from the principal or applicant if it paid despite an obligation to refuse payment according to article 17(2) and that therefore a proviso requiring the principal or applicant to prove that it would suffer harm would make it necessary for a court to refuse to order a provisional measure in those cases in which it was shown facts that made the demand manifestly and clearly improper according to article 19. The prevailing view, however, was that the words "serious harm" should be retained.

Paragraph (2)

61. The Working Group considered a proposal to delete paragraph (2), which authorized the court to hear the respondent on the application for a preliminary order. It was said that the significance of a provision referring to a discretionary power would be unclear, and that it anyway concerned an elementary procedural question of due process, which should be left to national procedural law. In addition, it was said that such deletion would not preclude courts from allowing the beneficiary to be heard in appropriate circumstances, which circumstances might not always be present, in particular in ex parte type of proceedings encompassed in article 21. Moreover, it was said that paragraph (2) might create a problem in distinguishing between provisional measures, which were covered by article 21, and final procedures, which were not covered. In view of those considerations, the Working Group did not accept a proposal to make the opportunity for the respondent to be heard mandatory, so as to foster due process for the beneficiary and provide the court with the respondent's side of the story as early as possible. The prevailing view, rather, was that paragraph (2) should be deleted.

Paragraph (3)

62. It was agreed that paragraph (3) providing for the possibility that the court may require the applicant to furnish appropriate security before granting a provisional measure was useful and should be retained. It was observed that such a provision was fair and reflected some balance in the consideration of the interests of the applicant and of the respondent. It was also said that paragraph (3) might have a disciplinary effect, precluding applicants from submitting frivolous applications, and as such might have an educational value. As a refinement, it was agreed that the word "security" would be replaced by a broader term, so as not to give the impression that a particular form of security was being referred to. One suggestion was to use the following wording: "undertaking, security or other document".

Paragraph (4)

63. The Working Group considered the three variants contained in paragraph (4). It was noted that variant A contained a broad statement that courts were not precluded from issuing any provisional measures that might be available under applicable procedural law. The only limitation on the discretion of the court in that variant was contained in a sentence between square brackets, included in response to a concern expressed at the seventeenth session that it would be especially disruptive if an injunction were allowed on the ground of non-conformity of documents (A/CN.9/361, para. 109). Variant B stated that the only ground other than improper demand on which a provisional court measure might be obtained was invalidity of

the guaranty letter. Variant C was the most restrictive of the three variants, since it did not allow courts to issue a preliminary order on any grounds other than improper demand.

64. Preference for variant A was expressed on the ground that no limitation should be imposed on the discretion of the courts. For the same reason, it was suggested that the restriction contained in the sentence between square brackets should be deleted. Support for variant A was also expressed, based on a concern that, should the draft Convention overly restrict the possibility of judicial intervention in the context of guaranty letters, by means of provisional measures, this might increase the risk that guaranty letters could be used for illicit purposes such as money-laundering or tax evasion. It was noted that such misuse of guaranty letters would not be prevented by the current text of article 19, since the demand for payment in such instance would not suffer from having "no conceivable basis", but would rather be on an illegal basis. In response to that concern, the Working Group generally agreed that, whichever variant were retained, wording to prevent the use of guaranty letters for illegal purposes should be included either in article 19 or in article 21.

65. In support of variant C, it was stated that the possibility of judicial interference with the guaranty letter should be limited to a minimum in order not to jeopardize the reliability of the instrument, the main function of which was to provide assurance of payment, pending resolution of any dispute that might arise. It was stated that, should courts be broadly allowed to interfere with the issuer's obligation to pay in cases other than improper demand as defined in article 19, there would be a risk that courts, at the request of the principal, would intervene in the context of the underlying transaction between the principal and the beneficiary. With a view to further strengthening variant C, it was suggested that injunctions that might be allowed on the ground of non-conformity of documents should be expressly disallowed in the text of variant C.

66. There was wide support for the view that the scope of the procedural rule set forth in paragraph (4) as to the right for the principal to seek injunctive relief should be drafted so as to parallel the substantive rule set forth in article 19 as to the conditions under which payment could be prevented. A question was raised, however, by proponents of variant A as to the reasons for which invalidity of the guaranty letter should be discriminated against as a means of preventing payment under the draft Convention, while improper demand would be regarded as an acceptable ground for seeking injunctive relief. It was stated that payment made upon receipt of an improper demand and payment made where the guaranty letter was manifestly invalid might equally result in irreparable harm being done to the principal. It was also questioned whether the principal would be left with any procedural remedy in circumstances where a demand for payment would be presented despite the guaranty letter being invalid.

67. In response, it was stated that the nature of the instrument was to ensure prompt payment (a feature labelled as "moneyness") and that, typically, it would be beyond the competence of a court ruling on an application for an interim measure to assess the validity of the guaranty letter. It was further stated that the guarantor or issuer was under an obligation to verify the validity of the guaranty letter and that, should it pay under an invalid guaranty letter, it would not be entitled to reimbursement from the principal. It was suggested that wording should be included in article 21 to make it clear that the article did

not deal with the relationship between the principal and the issuer or guarantor (a relationship sometimes referred to as the "account relationship"). The effect of the suggested clarification was to emphasize that the principal would not be precluded access to court by the draft Convention, for example in the context of an application for a provisional court measure enjoining the guarantor or issuer from debiting the principal's account, if the guarantor or issuer had paid upon receipt of a non-conforming demand.

68. After discussion, the Working Group decided that, subject to its above decision on illegality (para. 27), matters of non-conformity or invalidity of a guaranty letter should not be considered as subject to provisional court measures under article 21. Variant C was adopted. Furthermore, it was generally agreed that the subject-matter of the draft Convention was the relationship between the guarantor or issuer and the beneficiary. The Secretariat was requested to make it clear in the next draft that article 21(4) does not prevent the principal from seeking provisional court measures in respect of its contract with the guarantor or issuer. It was decided that the wording between square brackets in variant C should be retained to limit the prohibition embodied in variant C to applications based on objections to the payment demanded by the beneficiary. In the same vein, it was decided that the words "any objection to payment" should replace the words "any ground".

Paragraph (5)

69. It was noted that paragraph (5) subjected the attachment and seizure of the assets of the beneficiary or of the issuer, in addition to the requirements of the respective national procedural law, to the conditions contained in paragraph (1), in order to limit judicial interference with the payment of guaranty letters. It was also noted that in some jurisdictions attachment and seizure of assets could take the form of an administrative rather than a judicial procedure.

70. Various doubts were raised as to the necessity and appropriateness of retaining paragraph (5). Those doubts included that: it dealt with procedural law and that it would be too difficult to unify the conditions under which courts could grant any kind of extraordinary relief; the scope of the provision was uncertain, in particular since the Working Group had decided under paragraph (1) not to limit the scope of article 21 only to claims filed by the principal; paragraph (1) was sufficient in achieving a reasonable limitation to judicial interference with the commercial purpose of guaranty letters, namely, certainty of payment; in some jurisdictions the types of measures referred to in paragraph (5) were not considered provisional measures of a judicial nature, but rather were available fairly routinely and simply for a short period of time, without judicial involvement; the provision should not appear to suggest the possibility that all assets of the applicant would be subject to attachment and seizure, but just the proceeds of the guaranty letter.

71. The prevailing view was that a rule along the lines of paragraph (5) should be included in article 21, since such measures, however they might be characterized or obtained under different legal systems, were an essential element in giving meaning to the measures provided for in paragraph (1); and it was at the same time important to ensure, for the preservation of the commercial viability of guaranty letters, the application of the safeguards against abusive resort applied to provisional measures generally under article 21. However,

it was decided to forgo inclusion of paragraph (5), and to implement the substance of the Working Group's decision by further broadening the formulation of paragraph (1) by inserting in paragraph (1), after the word "may", wording along the lines of "effect the blockage of payment of funds or issue a provisional order".

72. The deliberations on paragraph (5) led the Working Group to reconsider its decision to avoid identifying in paragraph (1) the parties that could apply for the provisional measures provided for in article 21. It was generally agreed that, to limit some of the difficulties that had been referred to in the review of paragraph (5), paragraph (1) should limit article 21 to actions brought by the principal and that reference should also be made to the instructing or account party, so as to cover in particular the counter-guarantee context.

73. Upon the completion of the review of article 21, the Working Group returned, as had been agreed, to the general question of whether to retain or delete article 21. The considerations for and against retention of article 21, referred to above in paragraphs 38 and 39, were restated. Particular emphasis was placed, on the one hand, on the difficulties that would be encountered in attempting to craft a uniform rule in this area, and, on the other hand, on the position that a main function, if not the main function, of the draft Convention was to address the matters taken up in article 21. The prevailing view was that it would be premature to take a final decision at this stage and that the Working Group should await the next draft from the Secretariat, at which point it would resume its consideration of article 21.

## CHAPTER VI. JURISDICTION

### Article 24. Choice of court or of arbitration

and

### Article 25. Determination of court jurisdiction

74. In view of the link between the provisions contained in articles 24 and 25, the Working Group considered the two articles together.

75. A variety of questions and views were considered as to the approach taken in the current versions of the two articles. A general question was whether provisions of the type proposed in chapter VI were found in other multilateral instruments. In response to that question, the view was expressed that at this stage the focus of the deliberations should be on the utility of addressing the matters covered in chapter VI in the context of guaranty letters, rather than giving predominant weight to the presence or lack of provisions on jurisdiction in other conventions.

76. The view was expressed that article 24, which recognized the autonomy of the parties to designate a court or to stipulate arbitration for the settlement of disputes arising under the guaranty letter, failed to achieve anything useful since it did not provide for a sanction, in particular exclusivity of jurisdiction, of the designated forum. It was suggested that the resulting uncertainty was compounded further, in the absence of a successful designation

under article 24, by the lack of a rule of exclusivity also of the determination of jurisdiction by a court under article 25. It was further observed that the simple affirmation of the principle of party autonomy, without any mention of connecting factors to the designated jurisdiction, might run afoul of policy considerations in States that were concerned with supporting the burden of litigation in cases having little or no connection to the jurisdiction.

77. Those concerns, however, were generally outweighed by the view that article 24 served to provide useful support for the principle of autonomy of the parties with respect to court jurisdiction and might encourage the use of arbitration. It was also noted that article 24, while it still permitted a designated court to decline jurisdiction (e.g., on forum-non-conveniens grounds), and while it did not provide for exclusivity, had to be read in conjunction with article 25, which provided a direct rule on jurisdiction in the event that no jurisdiction resulted under article 24 and that some of the questions raised by article 24 could not be resolved until the provisions in article 25 on residual competence had been finalized and were more precise, in particular as to whether they were of a mandatory character. It was also pointed out that articles 24 and 25, since they would be in an instrument of a legislative character, would support the similar approach found at the contractual level in article 28 of the URDG.

78. A concern was expressed as to whether the viability of article 24 might be jeopardized in the event of a selection by the parties of a court that was not competent to resolve the dispute in question. It was suggested in that light to insert the word "competent" before the word "court" in paragraph (1), though it was also noted that article 25 was intended to provide a fall-back rule for cases of this type.

79. The question was raised as to whether the differences in formulation between article 24(1) and article 25(2) were intended to suggest a broader scope for the former provision, in particular as regards the parties to which reference was being made. Similarly, it was questioned whether differences as to formulation and content between article 24(2) and article 25(2) might give rise to the unintended interpretation that the latter provision was somehow intended to limit the jurisdiction of [court not referred to in the provision], which might raise difficulties if it were read to exclude the jurisdiction of courts where assets were located. The suggestion was made to add to article 25(2) a specific reference to article 21 in order to achieve greater clarity. It was also questioned whether the present formulation was intended to exclude the possibility, in the counter-guaranty letter context, of the principal pursuing directly a legal action in the jurisdiction where the guaranty letter supported by the counter-guaranty letter was payable. It was suggested that, if the intention was to permit such an action, reference could be made in the provision to the instructing party. At the same time, the Working Group was reminded of the question of whether to permit the instructing party to take legal action against the beneficiary of the related guaranty letter would run afoul of the requirement of privity of contract that would be applied in some jurisdictions.

80. Another broad area of concern was the relationship, both from the standpoint of the risk of possible inconsistency as well as possible benefit of positive interaction, between the rules in chapter VI and other multilateral instruments containing general rules on similar matters, in particular the 1968 Brussels Convention on Jurisdiction and the Enforcement of

Judgments in Civil and Commercial Matters and the 1988 Lugano Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters. It was noted in this regard that while those Conventions were open for accession by all States, they had been formulated on a regional level and that the degree to which those Conventions could support the provisions of chapter VI was thereby limited. A related question was whether, for States that were not parties to such a multilateral recognition and enforcement scheme, implementation of chapter VI would be viable. In response to that concern, it was pointed out that the possibility of recognition and enforcement did not rest solely on participation in such multilateral arrangements. In the first place, arbitral awards were subject to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and enforcement of judicial decisions might be available under bilateral arrangements. It was also pointed out that even States that were parties to the Brussels and Lugano Conventions faced enforcement problems, in particular when the enforcement of a judgment involved other States that were not parties to the Conventions.

81. The Working Group next considered a number of general proposals reflecting the various views and questions that had been expressed. One proposal was simply to delete chapter VI. In support of that proposal it was suggested that in their present form of non-exclusivity of jurisdiction the provisions were unnecessary, and, if they were amended to provide for exclusive jurisdiction, significant difficulties would arise, in particular in the absence of a recognition and enforcement scheme. In support of that proposal, it was pointed out that, at least as regards article 24, deletion would have limited practical effect since, in practice, the matter of jurisdiction was rarely addressed in guaranty letters, in particular since it was a matter that, if raised, might be seen as undermining the undertaking. However, as noted above, the general view was that an attempt should be made to address the matter of jurisdiction in the draft Convention since this was an area of considerable importance.

82. Another approach that was considered was to revise chapter VI so as to make the choice of jurisdiction exclusive. A variant of that approach was to delete article 24, leaving simply an objective rule on jurisdiction in article 25. Objections were raised to any approach that would confer exclusive jurisdiction. Primary among the concerns was that exclusivity was incompatible with an approach that did not ensure recognition and enforcement of decisions, since it would be more likely to give rise to cases in which, practically speaking, decisions were unenforceable. A related concern was that such an approach might give rise to difficulties if exclusive jurisdiction were conferred on the courts in one jurisdiction, while the assets that were the subject of enforcement were located in another jurisdiction.

83. Yet another type of approach was aimed at combining elements of exclusivity, non-exclusivity and party autonomy. One proposal along those lines was, unless otherwise agreed, to permit the claimant to pursue an action in one of the following jurisdictions: where the guaranty letter was issued; the place of business or residence of the beneficiary; or the place of business or residence of the principal. A suggestion that attracted wider interest was to provide that a designated court would have exclusive jurisdiction, unless it was shown that the decision was not recognized or was unenforceable, in which case another court may exercise jurisdiction.

84. While a doubt was expressed as to whether the latter proposal would work in the absence of a recognition and enforcement scheme, the Working Group decided to request the Secretariat to prepare for the consideration of the Working Group two variants of chapter VI. One variant would in essence retain articles 24 and 25 along their present lines, clearly showing that the choice or determination of jurisdiction was a non-exclusive one. The other variant would make the choice of jurisdiction under article 24 exclusive, while an article 25 determination of jurisdiction would remain non-exclusive. An attempt would be made to add to article 25 a safety valve, the possibility of a court other than the one chosen by the parties under article 24 taking jurisdiction if the decision of the article 24 court would not be capable of recognition and enforcement.

## CHAPTER VII. CONFLICT OF LAWS

### Article 26. Choice of applicable law

and

### Article 27. Determination of applicable law

85. The Working Group first discussed whether provisions on conflict of laws should be included in the draft Convention. One view was that it was not necessary or appropriate to retain chapter VII since the aim of the draft Convention was to provide a set of uniform substantive rules for guaranty letters. A related concern was raised as to the implications of including chapter VII for States that were parties to the 1980 Rome Convention on the Law Applicable to Contractual Obligations. Another view was that chapter VII should be retained. In support of that view, it was stated that, even with the draft Convention in place, there would be room and need for conflict-of-laws rules, whether they be found in national law or in a convention. Inclusion of such rules in the draft Convention would strengthen the reliability and commercial utility of the instruments being covered by recognizing party autonomy in the choice of law and reducing the extent to which disputes would arise as to determination of the applicable law.

86. The Working Group considered the question whether the scope provisions of article 1 should apply also to the conflict-of-laws provisions in articles 26 and 27, should those articles be retained. It was noted that were articles 26 and 27 to be subject to the same scope rules as the rest of the draft Convention, articles 26 and 27 would apply only if the draft Convention as a whole applied, and thus only to issues not covered by the draft Convention; by contrast, independent applicability of articles 26 and 27 would mean that those articles would apply even when the rest of the Convention was not applicable, thus unifying the conflict-of-laws rules of contracting States in this field. Such an approach would require the express exclusion of articles 26 and 27 from article 1. In view of the relationship between chapter VII and article 1, the Working Group felt that it would be in a better position to decide the question of whether or not to retain chapter VII, and on its content and scope of application, after the further review, in which it was about to engage, of article 1 (see below, paras. 90 to 106).

87. In the context of article 1, doubts were raised relating to the prospect of including in the draft Convention conflict-of-laws rules that would be applicable in the absence of applicability of the Convention pursuant to the scope provisions of article 1. Such an approach was said to be unusual and with very little precedent if any in a multilateral convention. It was stated that conflict-of-laws rules were characteristic features of national legislation, and thus might have to be considered if the Working Group were to decide to use the form of a model law, but they were not appropriate for inclusion in the draft Convention and should be better left to national law. The focus of the draft Convention, it was said, should instead be limited to defining clearly in article 1 the general scope of application of the draft Convention, and that, should conflict-of-laws provisions be included, they should apply only in cases in which the Convention as a whole applied, thus limiting their scope to issues not covered by the draft Convention. A further concern was that a general and fixed rule on conflicts would be of limited utility, as it might not provide the detail and flexibility of a national system of conflicts rules, and it might also stifle progressive development toward more flexible approaches. Yet another concern was that the preparation of viable and sufficiently detailed provisions on conflict of laws that meshed well with various types of legal systems might raise the spectre of further delaying completion of the draft Convention by the Working Group. In this context it was pointed out that, inter alia, a more detailed description of the rights, obligations and defences that would be covered or that would not be covered by such rules would be necessary in order to avoid different interpretations in the various legal systems; by way of example, reference was made to the question of prescription.

88. In response to those concerns, it was pointed out that the inclusion of chapter VII on an independent basis should not necessarily be regarded as an intrusion into an inappropriate area, since States would in any case have to have conflicts rules to cover cases in which the Convention did not apply. It was also pointed out that the rules set forth in chapter VII represented the prevailing, widely accepted approach. While this fact was cited by some as a factor for not including chapter VII, supporters of inclusion pointed out that it meant that a conflict-of-laws convention in this area -- the formulation of which was said to be unlikely -- would contain essentially the same rules, and that chapter VII should therefore not be regarded as raising matters of controversy or particular difficulty. In that light, it was suggested that there was no reason not to retain chapter VII, with independent applicability, so as to further unify the law applicable to guaranty letters in contracting States, in particular with regard to the important notion of party autonomy in choice of law matters. The Working Group was told that this would help courts to solve practical problems they were encountering in this field and that this practical need should be the predominant consideration, and not whether the procedures involved were categorized as substantive or procedural. It was also pointed out that chapter VII would not be the only portion of the draft Convention addressing matters of procedure, were chapter VI to continue to be retained. A related view was that, even if chapter VII were not made generally applicable independent of the scope provisions in article 1, it might be retained so as to provide a conflicts rule for issues not covered by the convention.

89. After deliberation, the Working Group decided, as a working assumption, that articles 26 and 27 would be retained in the draft Convention, and that their applicability would be independent of whether or not in any given case the draft Convention applied under the

general scope rules in article 1. The Working Group requested the Secretariat to prepare, in consultation with the Hague Conference on Private International Law, a revised version of articles 26 and 27 to reflect the working assumption and observations that had been made by the Working Group as to the content and approach of articles 26 and 27. It was noted that this approach would be reviewed on the occasion of the next reading of those articles.

## CHAPTER I. SCOPE OF APPLICATION

### Article 1. Scope of application

90. As the Working Group began its review of the revised provisions of the draft Convention, it was generally agreed that this reading of the text should be considered as the final reading by the Working Group in order that the text could be submitted to the twenty-eighth session of the Commission in 1995, as requested by the Commission at its twenty-sixth session.[3]

"This Convention"

91. The Working Group engaged in an exchange of views on whether the draft text should eventually be adopted as a convention or in the form of a model law. Some support was expressed for the form of a model law since that form would provide States with a wider latitude for determining which provisions of the text were acceptable and could readily be incorporated into the national law. It was noted, however, that a certain degree of flexibility might also be achieved if the draft text were to be adopted in the form of a convention, since the possibility might be opened for implementing States to make reservations on a limited number of issues.

92. Somewhat wider support was expressed for the form of a convention since that form was more in line with the character of the rules envisaged and since it would better foster uniformity and certainty as to applicable rules, which was said to be essential for the smooth operation of international guaranty-letter transactions and for the credit-worthiness of guaranty letters used as financial instruments. It was also stated that a convention, although less flexible in nature than a model law, might be more easily acceptable for implementing States for the reason that, at least in certain countries, a convention regulating international guaranty letters might be incorporated in national legislation through a simplified legislative process that would not necessarily imply elaboration of a national law on guaranty letters.

93. After discussion, the Working Group confirmed the working assumption made at its seventeenth session (A/CN.9/361, para. 147) that the final text would take the form of a convention. It was agreed that the possibility for implementing States to make reservations would need to be discussed by the Working Group as it proceeded with its reading of the

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[3] Official Records of the General Assembly, Forty-eighth Session, Supplement No. 17 (A/48/17), para. 273.

provisions of the draft Convention. It was also noted that the decision made by the Working Group as to the form of the instrument did not preclude the possibility that the Commission might revert to the more flexible form of a model law at the final stage of the work, when it would review the draft Convention prepared by the Working Group.

"applies to international guaranty letters"

94. Divergent views were expressed as regards the term "international guaranty letters" used in article 1 to delimit the substantive scope of application of the draft Convention. One view was in favour of retaining that term since it embraced in a suitably short way the two types of undertakings to be covered by the Convention, i.e. demand guarantees and stand-by letters of credit. Moreover, the term was in line with the current approach of having common provisions for both types of undertaking unless in particular cases there was a need for referring to only one of those types. It was noted, however, that in the draft Convention, the common name as a shorthand expression was used only in the provisions of the draft Convention but not in its title, where the naming of both types of undertaking was thought to better signal to the reader what the Convention was intended to cover. It was suggested that the title of the draft Convention might instead read "Draft Convention on guaranty letters (independent guarantees and stand-by letters of credit)". Another suggestion was that, in article 1, a reference to "international guaranty letters as defined in article 2" might make it sufficiently clear that the subject-matter of the convention was limited to independent guarantees and stand-by letters of credit.

95. Another view was that the term "guaranty letter" was inappropriate since it was not reflective of terminology used in practice, especially stand-by-letter-of-credit practice. Furthermore, it was stated that the reference to "guaranty" might raise regulatory concerns in certain countries, where the draft Convention might be misinterpreted as empowering banks to issue accessory guarantees, a practice that was expressly disallowed by existing banking regulation. It was thus suggested that the expression "guaranty letters" should be replaced by terms such as "independent guarantees and stand-by letters of credit". If, however, there was a need for using a short common name, a truly neutral term such as "undertaking", "independent financial instrument", "international financial assurance" or "demand letter" should be used, which would not raise the concern about leaning towards one of the two types of undertakings. However, a note of caution was struck about the use of any such neutral term, which could generate confusion as to which instrument was being dealt with, particularly in situations involving the issuance of a chain of guarantees and counter-guarantees. With respect to the use of the expression "independent guarantees and stand-by letters of credit", a concern was that such terms might insufficiently cover "equivalent undertakings" referred to in article 2.

96. Another concern was that the use of the term "guaranty letter" in the title and article 1 of the Convention might not be sufficiently neutral, since it might suggest a preference for independent guarantees over accessory guarantees. It was therefore suggested that the qualifier "independent" should be added in the title and article 1 in order not to suggest that bank guarantees and other independent instruments defined under article 2 were the only conceivable "guaranty letters". It was stated in reply that article 2 made it clear that only independent guarantees were covered by the Convention.

97. The prevailing view was that, in view of the practical difficulties raised in certain countries by the use of an artificially created term such as "guaranty letter", no further attempt should be made to adopt terminology that would be descriptive of practice. The draft convention should, instead, refer to a neutral term such as "undertaking" to refer to both types of instruments being covered by the draft Convention. With respect to article 1, it was decided that it should contain a reference to undertakings as defined in article 2, while the expressions "independent guarantees and stand-by letters of credit" would be used in the title of the draft Convention.

"[issued in a contracting State]

98. The Working Group discussed the wording between square brackets as a possible criterion for the territorial scope of application of the Convention. It was noted that, should the wording be deleted, the determination of the territorial scope of application of the Convention would be left exclusively to applicable conflict-of-laws rules. Should the wording be retained, the territorial scope of application of the draft Convention would be determined by a factor connecting the transaction to a Contracting State autonomously, i.e., without reference to conflict-of-laws rules. It was suggested that another approach that might be taken, which would broaden the scope of application of the draft Convention, along the lines of article 1(1) of the United Nations Convention on Contracts for the International Sale of Goods (hereinafter referred to as "the United Nations Sales Convention"), would be to establish a connecting factor such as the one contained in the wording between square brackets and, in addition, provide for the applicability of the draft Convention in cases where conflict-of-laws rules pointed to the law of a Contracting State.

99. In favour of adding a reference to cases where conflict-of law rules would point to the law of a contracting State, it was stated that such a reference might be necessary for the Convention to deal satisfactorily with the situation where only the counter-guarantor but not the second bank issuing an indirect guarantee was in a Contracting State. It was noted, however, that in practice, the effect of the suggested addition would be limited, since most national conflict-of-laws rules would point to the law of the country where the guaranty letter was issued. A contrary view was that the insertion of a reference to the rules of private international law might raise uncertainties where a court in a contracting State would need to apply the draft Convention as the law of another contracting State and the interpretation of the draft Convention in those two contracting States lead to divergent solutions. It was noted that, for that reason, a number of countries had made a reservation to article 1(1)(b) of the United Nations Sales Convention.

100. After discussion, the Working Group decided that the wording between square brackets should be retained and that, in addition, the draft Convention should provide for the applicability of the Convention in cases where conflict-of-laws rules pointed to the law of a Contracting State.

"[unless otherwise stipulated therein]"

101. There was general agreement that parties should be allowed to agree that the draft Convention would not apply to a guaranty letter transaction ("opting out clause"). It was

generally felt that such a decision to opt out of the draft Convention should be expressly mentioned in the text of the undertaking. It was noted, however, that, in most countries, there currently existed no specific legislation with respect to guaranty letters. If parties chose to opt out of the draft Convention, the guaranty letter transaction might be submitted by courts either to general contract law or to the draft Convention, which might be regarded as the only national legislation on the subject. The practical effect of a decision to opt out of the draft Convention might thus be limited. After discussion, the Working Group adopted the wording between square brackets.

102. A question was raised as to whether, in addition to being allowed to opt out of the Convention as a whole, parties should be allowed to derogate from individual provisions of the draft Convention. It was suggested that a provision along the lines of article 6 of the United Nations Sales Convention might be adopted. It was noted, however, that a provision allowing parties to derogate from or vary the effect of specific provisions would only be appropriate if the final text was to be essentially non-mandatory in nature. The prevailing view was that the question of party autonomy with respect to individual provisions of the draft Convention would need to be discussed after review of the articles of the draft Convention, only some of which were currently stated to be non-mandatory.

", and to any other guaranty letter that provides that it is subject to this Convention."

103. Various questions were raised in the context of the discussion as to whether the draft Convention should include a provision allowing parties to a guaranty letter to make the guaranty letter subject to the draft Convention ("opt-in clause").

104. A first question was whether an opting-in clause should allow parties to a domestic guaranty letter transaction to opt for the international regime provided for by the draft Convention. In favour of adopting such a provision, is was stated that it might be particularly desirable to allow parties in the context of domestic transactions to make reference to an international regime that might be expected to express fair solutions to problems that might be insufficiently resolved by domestic legislation. It was also stated that the possibility for parties to opt for the application of the draft Convention might make it more acceptable to adopt a restrictive definition of "internationality" under article 4. The contrary view was that parties should not be allowed to avoid application of the mandatory rules of domestic law by opting for the application of the draft Convention. It was noted that, where no such mandatory rules existed, parties would be able to adopt the draft Convention as a contractual regime even if the draft Convention contained no specific provision to that effect. After discussion, the Working Group agreed that the text of the draft Convention should not be drafted so as to create any specific right for parties to adopt the draft Convention for domestic transactions.

105. A second question was whether an opting-in clause should allow parties to submit to the draft Convention an international guaranty letter that would not otherwise fall within the territorial scope of application of the draft Convention, for example if the guaranty letter was issued in a non-contracting State. The Working Group generally agreed that, while parties should be free to adopt the legal regime set forth in the draft Convention indirectly by means of a reference to the law of a contracting State, no specific provision should allow them to

opt directly for the application of the draft Convention in the absence of such a reference to the law of a contracting State that applied the Convention in such cases.

106. A third question was whether an opting-in clause should allow parties to make the draft convention applicable to an instrument that would not otherwise be regarded as a guaranty letter under article 2. The view was expressed that the possibility of opting for the application of the draft Convention should be limited to commercial letters of credit, which were of the same legal nature as stand-by letters of credit and were said in some cases to be apparently indistinguishable from them. It was stated that the application of the draft Convention to commercial letters of credit would be appropriate because they operated on the same principles as stand-by letters of credit. It was further stated that express mention of an opting-in possibility should be made in the draft Convention in view of the possible exclusion of commercial letters of credit from the definition of the guaranty letter under variant C in draft article 2(1). An objection was raised against expressly mentioning in the draft Convention that the possibility for parties to agree on an opting-in clause would be limited to commercial letters of credit. It was stated that such a provision might produce the unintended effect of excluding any possibility that other instruments could be made subject to the draft Convention, as might otherwise be possible under applicable law. After discussion, the Working Group decided that the general opting-in provision in the current draft should be replaced by a provision allowing parties to commercial letters of credit to opt for the application of the draft Convention to such letters of credit. It was noted, that in its review of the remaining articles of the draft Convention the Working Group would have an opportunity to assess the appropriateness of that decision and to reconsider it if necessary.

## Article 2. Guaranty letter

### Paragraph (1)

#### chapeau

107. Various suggestions were made to make it clear that the issuance being referred to in the opening words of the definition was intended essentially to refer to the issuance of the undertaking on a professional basis. To that end, it was suggested to add the word "financial" before the word "institution". The Working Group considered such a modification as not providing additional clarity. Suggestions in generally the same direction were also made with a view to excluding cases in which an undertaking was issued by a consumer. Those suggestions included: permitting a reservation to exclude consumer issuance; including a statement to the effect that the draft Convention did not affect the application of consumer protection law; to add words along the lines of "other than a consumer" to describe the "person" referred to in the definition; to delete the word "person", or at least to refer to a "commercial" person; to refer to the "business or professional" realm. In regard to the latter suggestion, it was pointed out that there were cases in which it was impossible to determine the purpose of the undertaking from the face of the instrument. The Working Group did not find that those proposals achieved their aim of providing additional clarity as to the types of situations intended to be covered. It was also noted that the private-issuance cases in question were relatively infrequent on the international plane.

Furthermore, the Working Group generally shared the understanding that issuance of an undertaking by an individual for consumer or other private purposes involved a question which was properly within the sphere of national law, and not affected by the draft Convention.

Variants A, B and C

108. Three variants were presented to the Working Group with respect to the manner of describing the forms or types of undertakings being covered by the draft Convention. Variant A, which referred simply to demand guarantees and to stand-by letters of credit, attracted little support. A view was expressed that the more detailed approach in variant B, which included a description of the typical purpose of the undertaking, was unnecessary. A concern was raised that the definition in variant B did not sufficiently concentrate on the actual characteristics of the instruments to be covered by the Convention and would cover some instruments not intended to be covered, for example, promissory notes. However, the widely prevailing view was that the variant B approach was preferable. As will be seen below, after the discussion of variant B, the Working Group also decided to incorporate elements of variant C, which expressly excluded certain types of instruments.

109. Within variant B, two options were presented in square brackets as to the precise language to be used to describe the purpose of the undertaking. The Working Group preferred the second option, which included references to the payment upon simple demand or upon the presentation of documents stating that payment was due, and reference to other types of contingencies or purposes, in particular the direct-payment functions often performed by financial stand-by letters of credit.

110. The concern was expressed that the formulation "upon simple demand or upon presentation of documents" might inadvertently suggest that a simple demand undertaking was not of a documentary character, a question that had aroused some controversy among observers of practice. It was suggested that a more appropriate formulation would be "upon simple demand or presentation of other documents". The Working Group agreed to the proposed modification.

111. The suggestion was made that the words "documents stating that payment was due" should be replaced by the words "documents stating or implying that payment is due". The concern was that the existing language was unnecessarily narrow, since there would be cases in which the undertaking required the presentation of certain documents with the demand for payment in the case of default in performance, but that those documents would not necessarily be ones "stating" that payment was due. The concern was voiced that using the word "implying" might give rise to the unintended and undesirable interpretation that the doctrine of strict compliance of the documents with the terms of the undertaking was being watered down or made subject to modification by paragraph (2). In order to address both concerns, the Working Group decided to use wording along the following lines: "documents, in conformity with the terms and conditions of the undertaking, indicating that payment is due ...".

112. As to variant C, which expressly excluded commercial letters of credit, insurance contracts and negotiable instruments, the Working Group was generally of the view that it should be retained, subject to the decision to expressly permit the application of the draft Convention to commercial letters of credit by the agreement of the parties. It had been suggested that variant C could be deleted, in particular since the listing of instruments contained therein could be misinterpreted as exhaustive. It was noted that it would have to be understood that the deletion of variant C should not be an indication of an intent to cover those instruments. However, that approach was not supported, in particular since it was felt that variant C would be useful to dispel doubts that might arise in view of the broad approach decided upon for paragraph (1).

## Future work

113. The Working Group noted that its twenty-first session would take place in New York, from 14 to 25 February 1994, at which time the Working Group would consider the remainder of the revised articles in A/CN.9/WG.II/WP.80. It was also noted that, subject to the agreement of the Commission, the twenty-second session would take place from 19 to 30 September 1994 in Vienna.