be carefully considered in drafting such key articles of the Convention.

42. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that one of the difficulties throughout the process of drafting the text had been the diversity of definitions of fraud and abuse. That was why, after long discussion, a descriptive approach had been adopted in paragraph (1)*(a)*. It would, in his view, be dangerous to return to concepts that were natural to some people because of their training but not to others. The aim must be to achieve consensus.

43. Mr. SHISHIDO (Japan) asked whether article 19 was mandatory or not and whether a party could agree to give the bank absolute freedom to pay or not to pay. If the article was not mandatory, it would not need to be discussed so seriously, but if it was, it would have to be worded very carefully. The whole structure of the article was based on the principle that when a demand was manifestly and clearly improper, no payment would be made, and the beneficiary could not seek damages against the guarantor/issuer and had no right to reimbursement. Problems would arise because of two exceptional cases that might occur involving misjudgement. In the first, the guarantor/issuer made a payment when he should not have done so. That payment would not be in good faith and the banker would not be able to obtain reimbursement from the principal. In that case, there was a difficulty with the wording of paragraph (1)*(a)*, in which the phrase "in the view of the guarantor/issuer" was ambiguous and misleading. Despite the reasons given for that wording in paragraph 70 of document A/CN.9/408, the terminology used suggested that the payment depended absolutely on the judgement of the guarantor/issuer, which was not the intention. He therefore proposed that the phrase "in the view of the guarantor/issuer" be deleted.

44. Mr. GAUTHIER (Chairman of the Committee of the Whole) said he would invite the representative of Japan to conclude his statement at the next meeting.

The meeting rose at 12.35 p.m.

Summary record of the 554th meeting

Friday, 5 May 1995, at 2 p.m.

[A/CN.9/SR.554]

Chairman: Mr. GOH (Singapore)

Chairman of the Committee of the Whole: Mr. GAUTHIER (Canada)

The meeting was called to order at 2.10 p.m.

DRAFT CONVENTION ON INDEPENDENT GUARANTEES AND STAND-BY LETTERS OF CREDIT *(continued)* (A/CN.9/405, A/CN.9/408 and A/CN.9/411)

Article 19 (continued) (A/CN.9/408, annex)

1. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that the Working Group had come to the conclusion that the terms "fraud" and "*abus de droit*" could not be used because they had so many different connotations, and that it was a better approach to describe certain circumstances under which payment would not be in good faith. That approach had been followed in subparagraphs *(a)*(i), (ii) and (iii) of paragraph (1). Similarly, paragraph (2) had given examples of situations in which a demand had no conceivable basis. The questions left open, on which the Commission should concentrate, were whether there should be an obligation not to pay, and, if so, what should be the mechanism for establishing such an obligation, or a right not to pay.

2. Mr. SHISHIDO (Japan) recalled that at the previous meeting he had proposed the deletion of the words "in the view of the guarantor/issuer" in paragraph (1)*(a)*, because they might be construed as giving the guarantor/issuer absolute freedom of action. The reference to good faith established a link with articles 14 and 15, implying that the guarantor/issuer need not investigate the propriety or impropriety of documents.

3. His second proposal concerned the eventuality that, through misjudgement, a guarantor/issuer did not pay when he should have paid, after which he might be sued by the beneficiary and be ordered by the court to pay the amount stated in the undertaking, but could recover it from the principal/applicant. The question who would then have to bear the risk of payment of damages to the beneficiary caused by the delay seemed to be covered by paragraph (1)*(b)*, but it could also be settled by means of an arrangement between the guarantor/issuer and the principal/applicant, so that paragraph (1)*(b)*, including the passage in square brackets at the end, was superfluous and should be deleted.

4. Mr. BYRNE (United States of America) said that his experience of discussions on the substance of the article had shown that it was of critical importance and offered both an opportunity to do much good and a grave danger of producing an imbalanced product that would not be acceptable in the commercial world.

5. A workable system was in place in every country, involving sometimes positive law, sometimes the judicial system, and so on. Whatever the elements of the system, they must be in overall balance in order to enable commerce to function.

6. It was important to bear in mind the elements of the balance and the various interests of all the parties in the eventuality that conforming documents were presented but there was nevertheless an allegation of fraud. One interest was that of the beneficiary, who was entitled to payment unless there was proof of fraud. Secondly, there was the social interest that the guarantor/issuer should not pay when there was clear and manifest evidence of fraud.

7. The third interest was that of the guarantor/issuer, in cases where it was not manifest and clear that there was fraud but there was nevertheless some suspicion or a basis for reasonable suspicion of fraud. The guarantor/issuer should not be put in a position of being required by a court in one jurisdiction to pay the beneficiary while a court in another jurisdiction ruled that it was

not entitled to reimbursement although it had paid in good faith without clear and manifest evidence of fraud.

8. Finally, there was the interest of third parties, such as confirming banks, and innocent third parties which had in good faith presented documents without knowledge of fraud.

9. Unless those interests could be balanced, the instrument would not be workable and acceptable.

10. It seemed to him that agreement should be reached on four questions, without which it would be pointless to discuss the niceties of drafting.

11. First was the question of the risk that the bank undertook with regard to fraud, i.e. what was the role of the guarantor/issuer when fraud arose. Was it the duty of the guarantor/issuer to examine documents for their genuineness and was it obliged to bear the risk of fraud? The answer to that question would greatly affect the rule to be drafted. He suggested that it was the universal understanding of the international operations community that it was not the guarantor/issuer but the principal/applicant that bore the risk of fraud or falsified or forged documents. A letter of credit was not a cheque, the beneficiary was not a customer of the issuer or guarantor but a stranger. The issuer or guarantor had no way of knowing who the beneficiary was or whether its signature was genuine, much less of knowing whether any document presented or any signature on the document was genuine. The undertaking of the issuer or guarantor was to examine documents for facial conformity. That was reflected in article 15 of UCP and article 12 of URDG. Commercial mechanisms were available to protect against the risk of fraud, for instance, through insurance which could be obtained by the applicant. It was not the duty of banks to act as detectives of fraud, nor were they insurers. Their duty was limited to examination of facial conformity.

12. The second question was related to the ability of an issuer or guarantor to dishonour a presentation on grounds of fraud and to the consequences of dishonouring a presentation. Had fraud to be proven? What would happen if a presentation were dishonoured, in good faith, but fraud could not be proven?

13. The third question, assuming that the source of the suspicion of fraud came from the principal/applicant, was whether the guarantor/issuer could contract with the principal/applicant to indemnify the latter for the cost of raising the question of fraud. If a rule were established that there was a duty to dishonour, a question arose in the mind of his delegation and of the banking community of the United States of America whether *ordre public* would prevent contracting for indemnification in such situations.

14. Finally there was the question whether or not there could be innocent third parties and, if so, what the effect would be.

15. It seemed to him that the first possible approach to that situation was not to speak to the question but simply to state grounds for non-payment despite facial compliance and set forth a general rule, without specifically indicating whether a duty, a right or a discretionary right existed with regard to payment.

16. The second approach was to predicate a duty to dishonour in specific situations. If that were to be acceptable, it would also be necessary to make it clear that there was a related right to indemnification.

17. The third approach was to indicate that, where the guarantor/issuer acted in good faith according to recognized standards of international practice in independent guarantees or stand-by letters of credit, it had the ability to dishonour where fraud was alleged and where it was not clear that there was in fact fraud. In that case, it must be prepared to prove such fraud in an action brought by the beneficiary.

18. It was essential to clarify those questions of principle in order to achieve a genuine consensus.

19. Mr. FARIDI ARAGHI (Islamic Republic of Iran) said that the article seemed to stress non-payment rather than payment. It was wrong to make "the view of the guarantor/issuer" a condition for payment or non-payment; the words "in the view of the guarantor/issuer" should be deleted.

20. He supported the proposal of Japan for the deletion of paragraph (1)*(b)*.

21. He agreed with the third option outlined by the delegation of the United States and thought that it should be incorporated in the text as paragraph (3).

22. Mr. FAYERS (United Kingdom), referring to the four principles enunciated by the representative of the United States, said that he accepted the proposition that if there were clear evidence of fraud there would be no payment under the guarantee. The more difficult concept was in areas where there was suspicion of fraud, which again included two types of cases.

23. Though banks should not be obliged to act as detectives, there was a case covered by (1)*(b)* where the guarantor was put in possession of facts by its customer, which raised the question what action should be taken. It could not be permissible that the bank should turn a blind eye, but, if it accepted the information, the question arose as to the extent to which it must assess the information. That was a difficult area. Investigation of the matter by the bank would entail a monetary cost and also slow down the mechanism of the guarantee. However, there might well be cases in which, as a result of information put before a bank by its customer, it was or should be quite clear that there was fraud.

24. He asked whether the United States banking community would flatly refuse to make any investigation when presented with evidence of fraud and if so whether they would suggest that the customer go to court. Perhaps the representative of the United States would expand on its position with regard to such cases.

25. He quoted a case where the seller diverted a shipment to a port in a different country but presented the documents that named the original port. He found it difficult to believe that, if the buyer pointed out that it was merely necessary to consult Lloyd's list to establish the facts, the bank would then decline to make that simple examination. That area should be investigated further.

26. Mr. LAMBERTZ (Observer for Sweden) welcomed the remarks of the United States and agreed that a balance had to be struck between various interests. A bank had an obligation towards the beneficiary, i.e. an obligation to pay; it also had an obligation towards the principal, namely, not to expose the latter to the risk of losing money. That obligation would exist if the bank was certain that the beneficiary was not entitled to payment. It was therefore justifiable to incorporate the subjective element implicit in the words "if in the view of the guarantor/issuer it is manifest and clear that . . ." in the article, though, at an earlier stage in the discussion of the question, he would have agreed with Japan.

27. Though it was impossible either to prove or disprove a subjective assessment by a bank, balancing the interests of the two sides seemed to show that the rule was acceptable.

28. The proposed indemnification clause in paragraph (1)*(b)* could also be accepted, though he agreed with the Japanese

delegation that the bracketed portion in the last lines of the paragraph should probably be deleted.

29. Taking up a point raised by the United States, he said that the Commission might discuss the inclusion in the Convention of a rule stating that in some instances the bank had a right not to make payment, when it was not sure whether there was fraud or not. That would be a right *vis-à-vis* the beneficiary, whereas the obligation not to pay was an obligation towards the principal. The right not to pay could exist when there was a high probability that the bank was under an obligation not to pay. He therefore favoured adding to the obligation not to pay a right not to pay.

30. He did not believe that it was desirable at the present juncture to discuss the question of innocent third parties—an extremely complex problem that went to the heart of national legislation. The provision in article 1(1) which permitted opting-out from the Convention ought not to apply to articles 19 and 20.

31. Ms. ASTOLA (Finland) said that she shared the views put forward by the representative of Japan. It would be preferable to delete the words "in the view of the guarantor/issuer" but acceptable alternatives would be to make a reference to international banking practice at the beginning of paragraph (1)*(a)* or to take up the Japanese proposal of simply referring to articles 14 and 16. She shared the view that paragraph (1)*(b)* should be deleted and replaced by a form of words similar to that used in article 8(3), stating that an amendment had no effect on the rights and obligation of the principal/applicant unless the latter consented to it.

32. The representative of the United States had said that there were three options before the Commission. In her view, however, a fourth possibility would be to avoid mentioning the idea of an obligation not to pay. It could be stated that the guarantor/issuer had a right not to pay in certain circumstances, mentioned in paragraph (1)*(a),* and that, if the guarantor/issuer chose to pay even when it had the right not to pay, that decision would have no effect on the principal/applicant unless otherwise agreed. Thus the question of indemnification would not be addressed in the article.

33. She did not think it would be possible to reach agreement that the guarantor must pay, whatever the eventuality. It would be more helpful to speak of a "right not to pay" and then link the protection of the principal/applicant to that right. She agreed with the observer for Sweden that the situation of innocent third parties could not be resolved in the article.

34. Mr. KOZOLCHYK (United States of America), speaking in answer to the questions raised by the representative of the United Kingdom, said that banks would generally not consult, say, Lloyd's list before deciding whether to make payment but would base their decision on actual documents.

35. The problem perceived by the representatives of Finland and Japan seemed to be that the phrase "in the view of the guarantor/issuer", i.e. of the bank, appeared to be a subjective and somewhat arbitrary criterion, which explained Finland's preference for a discretionary right not to pay. But that discretion would be based on standards of international practice or good local practice, so that the type of situation in question must, firstly, be serious and, secondly, be manifest and clear, and the criteria concerned would be based on the actual documents. So long as there was a clear and manifest standard that could be objectively established relating both to letters of credit and bank guarantees, it would be reasonable to accept a bank's discretion or right not to pay.

36. The CHAIRMAN, speaking in his capacity as the representative of Singapore, agreed with the United States suggestion that the real issue was related to the bank's role when the question of non-payment arose. Agreement should be reached on that issue before attempting to find satisfactory wording for the article. In his view, it would be best to follow accepted international banking practice.

37. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that the fundamental question before the Commission was one of policy—whether the guarantor/issuer had a duty or a right not to pay. Some speakers had suggested that it might be enough to state that in certain circumstances it would have a right not to pay or a discretionary power as to whether it should or should not pay. Other speakers had argued that, when an irregularity was "manifest and clear", payment must not be made. He pointed out that a right not to pay or to withhold payment had implications for article 20 on provisional court measures. Certain jurisdictions would insist that a request to the court to issue an order must be based on a definite obligation and not on a choice, as would be the case with a right not to pay.

38. Mr. STOUFFLET (France) referred to a distinction drawn by the Working Group between regulating merely the relationship between the guarantor and the beneficiary or including the relationship with the principal/applicant as well. In the first case, the word "may" would suffice. There would be no need for an obligation; the guarantor/issuer would merely have to justify its refusal to pay. In the second case, "may" would not be enough and there would have to be an obligation, with implications regarding the liability of the guarantor/issuer towards the principal/applicant. Ideally, the article should cover all cases but it might be preferable to take a more modest approach and leave the relations between the guarantor and the applicant to be determined by domestic law. That would be a realistic and logical approach, and would be consistent with what had been already decided.

39. Mr. KOZOLCHYK (United States of America), referring to the question whether non-payment should be a duty or a right, said that the representative of the Islamic Republic of Iran had pointed out that the Convention stressed non-payment and that it should contain a statement to the effect that, once any agreed standards of examination had been complied with, the guarantor/issuer must pay. There would then be no problem with stating that, under certain circumstances, the obligation to pay imposed upon the guarantor/issuer could be suspended or revoked. Even if there were facial compliance of the documents, the guarantor/issuer could use its discretion based on other objective factors.

40. Mr. OGARRIO (Mexico) said he had the impression that the question whether there was a duty or a right not to pay had already been dealt with. He asked for distribution of the informal proposal made by the representative of the United States.

41. Mr. BYRNE (United States of America) said that his proposal had simply outlined some possible options.

42. Mr. CHOUKRI SBAI (Observer for Morocco) asked whether the guarantor/issuer automatically had the right to check the authenticity of documents or whether notice from the principal/applicant was necessary. If the guarantor/issuer were notified that the documents were fraudulent, it would be obliged not to pay. In practice, banks paid only after the authenticity of the documents had been thoroughly checked. He suggested that, since the title of article 17 was "Payment on demand", article 19 should simply be entitled "Non-payment". The reference to non-payment in the last line of paragraph (1)*(a)* might engender some confusion, especially in the Arabic version of the text, so that it might be preferable to choose a form of words to the effect that payment would not be made to the beneficiary if the guarantor/issuer considered that the falsification was manifest as described in subparagraphs (i), (ii) and (iii) of paragraph (1)*(a).*

43. Mr. OGARRIO (Mexico) said that the provision should establish a right rather than a duty not to make payment. He therefore suggested that the title of article 19 be amended and the wording of the last phrase in paragraph (1)*(a)* be changed from "payment shall not be made" to "payment may not be made", or words to that effect.

44. For the reasons stated by the French representative, paragraph (1)*(b)* could be deleted entirely; in his view, the Convention need not cover the relationship between guarantor/issuer and principal/applicant. If the possibility of compensation were included, a principal/applicant might agree to the compensation of issuing banks, thereby inviting the banks not to make payment.

45. Ms. FENG Aimin (China) pointed out an inconsistency between paragraph (1)*(a)*, which gave the guarantor/issuer the right not to make payment in certain circumstances, and article 15 of UCP, which did not give banks such a right.

46. Moreover, article 19 contained no equivalent to article 18*(d)* of the UCP rules, which read: "The Applicant shall be bound by and liable to indemnify the banks against all obligations and responsibilities imposed by foreign laws and usages".

The meeting was suspended at 3.45 p.m. and resumed at 4.10 p.m.

47. Mr. GAUTHIER (Chairman of the Committee of the Whole) suggested that the Commission should consider what the impact on provisional court measures in the various jurisdictions would be if the guarantor/issuer had the right not to pay. In his country, it was unlikely that provisional court measures would succeed if the bank had the right not to pay.

48. Ms. BAZAROVA (Russian Federation) said that the provision should establish a duty rather than a right. The guarantor/issuer had to be protected. Demand guarantees, which obliged the guarantor to pay the beneficiary, were rather dangerous because of their official nature and offered serious potential for abuse.

49. Mr. BYRNE (United States of America) outlined possible amendments to article 19, as follows:

The title of the article should read:

"Grounds for non-payment despite facial compliance of the documents";

Paragraph (1) should read:

"(1) *(a)* A ground for non-payment to the beneficiary despite the presentation of facially correct documents exists if:

(i) any document is not genuine or has been falsified;

(ii) no payment is due on the basis asserted in the demand and the supporting documents; or

(iii) judging by the type and purpose of the undertaking, the demand has no conceivable basis."

A new subparagraph (1)*(b)* would reproduce the current paragraph (2), without any changes.

There were four possible options with regard to a new paragraph (2). The first would focus on a right not to pay and would read:

"If, in the view of the guarantor/issuer, with due regard to generally accepted standards of international practice of independent guarantees or stand-by letters of credit, it is clear and manifest that a ground for non-payment pursuant to paragraph (1)*(a)* exists and for that reason payment would not be in good faith, the guarantor/issuer has a right not to pay."

The reference to paragraph (1)*(a)* was to the proposed revised wording.

The second option would be to retain only paragraph (1) and say nothing further regarding duties or rights.

The third option, based on the current approach in article 19 (1)*(b)*, would be to link a duty not to pay with a contractual right to indemnification. In his delegation's view and in that of his country's banks, such a link was necessary. The text would read:

"(2) *(a)* If in the view of the guarantor/issuer, with due regard to generally accepted standards of international practice of independent guarantees or stand-by letters of credit, it is clear and manifest that a ground for non-payment exists, pursuant to paragraph (1)*(a)* and for that reason payment would not be in good faith, it shall not be made to the beneficiary.

(b) Unless otherwise agreed, the principal/applicant will indemnify the guarantor/issuer against the consequences of dishonour at the request of the principal/applicant."

The fourth option would introduce a discretionary right. The text would read:

"Even if a ground for non-payment has been alleged, a guarantor/issuer acting in good faith with due regard to generally accepted standards of international practice of independent guarantees or stand-by letters of credit may pay a beneficiary unless ordered otherwise by a court of competent jurisdiction."

50. Mr. GAUTHIER (Chairman of the Committee of the Whole) noted that many delegations could accept the idea of a duty not to pay on certain conditions, such as indemnification, as suggested by the representative of the United States. He asked delegations to state whether they wished article 19 to be couched in terms of a duty or of a right.

51. Mr. ILLESCAS (Spain) said that if a guarantor concluded that payment should not be made because documentary requirements were not met or the documents were false, he was obliged not to pay. However, the situation differed when the guarantor did not arrive at such a firm conclusion or when a third party claimed that the documents did not conform and so informed the guarantor. In such cases, the guarantor had the right not to pay. When there was uncertainty, discretion should be allowed.

52. Mr. GAUTHIER (Chairman of the Committee of the Whole) explained that his request for comments on the question of duty versus right was related only to paragraph (1)*(a)*, which, as currently drafted, restricted the possibility of non-payment to the three cases described in (i) to (iii) of subparagraph (1)*(a)*.

53. Mr. AL-NASSER (Saudi Arabia) considered that the guarantor had both a right and a duty not to pay. Paragraph (1)*(a)* should begin with the words: "If the guarantor proves . . .", instead of "If, in the view of the guarantor/issuer . . .". In his country's legal system, a guarantor could not decide for itself whether a document was genuine or false: that had to be proved in court. Moreover, since the concept of good faith was construed differently under various legal systems, his delegation thought that the expression "in good faith" should not be used.

54. Paragraph (1)*(b)*, requiring the principal to indemnify the guarantor, would run counter to practice in his country, where a guarantee was an obligation between a guarantor and a beneficiary. The guarantor, and not the principal, should apply for a judicial or arbitral determination that non-payment was justified.

55. Mr. ILLESCAS (Spain) said that the current wording of paragraph (1)*(a)*, with its three subparagraphs, was not acceptable to his delegation. There should be no categorical establishment of

bad faith in the event of the circumstances described in the three subparagraphs. There should be a reference to conduct in accordance with international standards.

56. Mr. STOUFFLET (France), referring to the use of the somewhat ambiguous term "discretionary" during the discussion, said that there was an element of arbitrariness in the French notion of "*discrétionnaire*". It would be wrong to convey the impression that in certain circumstances the guarantor/issuer was free to decide against payment. As he understood it, the practical implications of using either the word "shall", implying an obligation, or the word "may", implying an element of choice, did not differ greatly and the criteria to be applied by the guarantor/issuer were the same as those set out in articles 16 and 17. The word "shall", however, implied that the guarantor/issuer could be penalized for its behaviour, in certain circumstances.

57. Ms. FENG Aimin (China) said that she preferred the proposal put forward by the representative of the United States of America because the concept of a right might lead to abuse of rights by banks, whose credibility would suffer as a result.

58. Ms. JASZCZYNSKA (Poland) said that, as Legal Counsellor to the National Bank of Poland, she preferred, in practice, the concept of obligation in order to protect the bank as guarantor. That aspect was particularly important in the case of such instruments as independent guarantees with an international dimension.

59. Mr. VASSEUR (Observer for Monaco) said that formulating the question in terms of obligations and rights implied an underlying concern for the situation of the principal. Should the principal reimburse a guarantor who had made payment? The guarantor had issued the undertaking of its own volition and was not the principal's instrument in legal terms. Where the guarantor felt the need to pay in order to safeguard its international credibility, such conduct could not be held against it. With regard to the guarantor's entitlement to reimbursement, the instructions issued by the principal to the guarantor usually contained a clause permitting the latter, once payment had been effected, to debit the principal's account as a matter of course. The principal could then take action against the guarantor, on the understanding, however, that one of the basic principles of guarantee law was: pay first, contest later.

60. Mr. CORELL (Under-Secretary-General, The Legal Counsel), taking the floor at the invitation of the Chairman of the Committee of the Whole, said that the Commission was one of the many bodies served by the Office of Legal Affairs of the United Nations, which had very wide-ranging responsibilities. One of the current tasks of the Office was to assist in establishing the international tribunals set up by the Security Council for the former Yugoslavia and for Rwanda. Another was to provide services for the new organs being established following the entry into force of the United Nations Convention on the Law of the Sea. It was therefore virtually impossible to keep abreast of the substance of every activity under way in the bodies served by the Office.

61. The reports of UNCITRAL were referred to the Sixth Committee of the General Assembly, whose expertise was not, in his view, on a par with that of the Commission. The reports were therefore recognized as being more or less in a final state. It was important, however, to offer Member States an opportunity to comment on their content in the Sixth Committee.

62. When the report on UNCITRAL's current activities was submitted to the Sixth Committee, that Committee might decide to adopt it as it stood or to set up a working group to examine it prior to adoption, following which it would be submitted to the General Assembly. A diplomatic conference would not be necessary, as evidenced by the recent adoption by the General Assembly of the amendment to Chapter 11 of the Convention on the Law of the Sea or the Convention on the Safety of United Nations and Associated Personnel. It was a matter of convincing Governments that a text was sufficiently clear to allow its immediate adoption by the General Assembly.

63. He had been gratified to note the disciplined way in which the Commission went about its work. Such matters as the time when the meeting was called to order and the time at which it rose were placed on record and were noted by the Fifth Committee. It was important to show Member States that it was possible to work efficiently in the United Nations.

The meeting rose at 5.10 p.m.

Summary record of the 555th meeting

Monday, 8 May 1995, at 9.30 a.m.

[A/CN.9/SR.555]

Chairman: Mr. GOH (Singapore)

Chairman of the Committee of the Whole: Mr. GAUTHIER (Canada)

The meeting was called to order at 9.35 a.m.

DRAFT CONVENTION ON INDEPENDENT GUARANTEES AND STAND-BY LETTERS OF CREDIT *(continued)* (A/CN.9/405, A/CN.9/408, A/CN.9/411)

Article 19 (continued) (A/CN.9/408, annex)

1. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that the discussion on article 19 so far had shown that there existed in substance only two possible approaches, which might be called the "shall" approach and the "may" approach. Under the "shall" approach, where it was manifest and clear to the guarantor that, in view of the conditions stated in paragraph (1)*(a)*(i), (ii) and (iii), any payment made would be in bad faith, the guarantor must not pay. The alternative would be that, in the same situation the guarantor/issuer might—rather than must—refuse to pay. The exception to the obligation to pay a demand made in accordance with article 14 could therefore be expressed either by a prohibition limited to very specific circumstances, or by language that did not set out in detail the various types of fraud but merely indicated that in certain situations payment might be refused. He