Summary record of the 557th meeting

Tuesday, 9 May 1995, at 9.30 a.m.

[A/CN.9/SR.557]

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 12 (A/CN.9/408, annex)

1. Mr. GAUTHIER (Chairman of the Committee of the Whole), introducing article 12, said that subparagraph *(a)* dealt with the case where an undertaking expired on a particular date. In subparagraph *(b)* expiry depended on the occurrence of a particular event. If neither of those conditions was met, subparagraph *(c)* provided for the undertaking to expire six years after issuance. That would allow a clear five years' validity, given that in the first year it might be some months after issuance before the instrument took effect.

2. Ms. CZERWENKA (Germany) said she had two drafting points to raise on article 12. With regard to subparagraph *(b)*, she noted that the term "confirmation" was given a specific definition in article 6, and therefore thought it would be better to replace it with another word, such as "affirmation" or "assurance".

3. Secondly, she felt that the drafting of subparagraph *(c)* was incomplete. It might well be an undertaking both stated that an act or event had to occur and set an expiry date. As the text stood, it might be taken to mean that in such cases, if the act or event had not yet been established, the stated expiry date was to be ignored in favour of the six-year limit. It would be preferable to add, after the word "document", the words "and an expiry date has not been stated in addition".

4. Mr. HERRMANN (Secretary of the Commission) said he thought the intention was that whenever an expiry date was stated, it would apply, however long the period might be. The six-year limit would then not apply. It made no difference if the undertaking also stipulated the occurrence of an act or event. In that situation, whatever occurred first would trigger expiry—either the expiry date, or an earlier event. If that was not the intention, the text would have to be redrafted.

5. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that he agreed with the representative of Germany on the first point she had raised, concerning the word "confirmation". It was a matter of drafting, and a better word should be found.

6. The second point raised the question of the Working Group's understanding of what subparagraph *(c)* was meant to achieve. He asked whether the Commission wished to keep to the policy position adopted by the Working Group—namely, that if no date was specified, or if an event was specified but did not occur, then the expiry period was six years beyond the date of issuance, but that the parties were free to provide for an expiry date extending beyond six years if they wished.

7. Ms. CZERWENKA (Germany) said that the matter was not one of substance, but of drafting. As it stood the text was not clear. Subparagraph *(c)* stated baldly that if an act or event condition had not been met, the six-year limit would apply. It did not say that that would not be so if an expiry date was also specified.

8. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that if the undertaking stated an expiry date, even if it also stated an expiry event, then the mere fact that there was an expiry date meant that subparagraph *(c)* would not apply.

9. Mr. FAYERS (United Kingdom) said he agreed with the representative of Germany and that the Commission had to make a policy decision. Where there was both an expiry date and an act or event, the Commission should specify that it was the first of those to occur that would be decisive.

10. Mr. LAMBERTZ (Observer for Sweden) said he supported the analysis made by the representative of Germany. It was not a policy issue; the word "or" caused a problem, which should be dealt with by the drafting group.

11. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that the drafting group might be asked to consider if there was a better way to express what was intended, bearing in mind the fact that other provisions in the Convention were drafted along similar lines.

12. Mr. MAHASARANOND (Thailand) asked whether in subparagraph *(b)* the phrase "not within the guarantor/issuer's sphere of operations" was necessary, because the act or event on which expiry was to depend was based on an agreement between the guarantor/issuer and the principal/applicant.

13. Mr. HERRMANN (Secretary of the Commission) said that the idea had been that where there was a clause in the undertaking making expiry dependent on an act or event, it should in general be limited to a documentary condition, to the exclusion of non-documentary conditions. Bankers did not wish to get involved in the investigations the latter might entail. There was, however, a small range of possible non-documentary acts or events which the Working Group had wished to include and which did not create the risk of placing bankers in that position. One example was when a presentation was made at the bank counter, which the guarantor, by his very presence, could easily verify. Another was where an advance payment had been made or repayment guarantee given at the same bank. Such transactions fell within the sphere of operations of the guarantor/issuer. The Group had felt that it would not be reasonable to exclude them and require documentation of something which the guarantor could verify from his desk, without having to contact another bank.

Article 13 (A/CN.9/408, annex)

14. Mr. GAUTHIER (Chairman of the Committee of the Whole) introduced article 13, drawing particular attention to the fact that there had been much discussion in the Working Group, in particular of the latter part of paragraph (2), and more especially of the exact position in the sentence of the word "international".

15. Mr. BONELL (Italy) said that the opening phrase of paragraph (1), "subject to the provisions of this Convention", was the kind of wording that usually indicated the mandatory character of the provisions. With such language the terms in the contract would bind the parties only if consistent with the provisions of the Convention. But that was not the intention with the present text; some conditions were mandatory, but not all of them. As a result he had some difficulty with the language used.

16. Another point of concern to him was that there was an explicit reference in paragraph (1) to the rights and obligations of the guarantor/issuer and the beneficiary, but no mention of the principal/applicant. Certain versions at least of articles 19 and 20 dealt specifically with the rights and duties of the principal/applicant, and he wondered whether they should not also be covered in article 13.

17. Mr. HERRMANN (Secretary of the Commission) said that he did not think the second point raised had ever been discussed in the Working Group. The omission of any reference to the principal/applicant was probably due to the fact that paragraph (1) was concerned with the parties whose rights and obligations were determined by the terms and conditions of the undertaking, not by the provisions of the Convention.

18. As for the introductory phrase, "subject to the provisions of this Convention", it was a form of words that could be found in other UNCITRAL texts. It had been suggested that "subject to the mandatory provisions of this Convention" would be preferable, but that wording would produce a different result. In the present wording, a non-mandatory provision of the Convention gained mandatory effect if not derogated from, that is, if the parties to the undertaking did not stipulate otherwise, either by excluding a particular provision or by regulating the matter differently. If not derogated from, even a non-mandatory provision became applicable and determined the rights and obligations in a given situation. Insertion of the word "mandatory" would imply that the rights and obligations were subject to the mandatory provisions only, thus leaving a gap. The Working Group had chosen the present wording as a more comprehensive formula that did not exclude the non-mandatory provisions.

19. Mr. LAMBERTZ (Observer for Sweden) said that the representative of Italy had raised two important issues, which should, if possible, be dealt with in the report. His understanding of the introductory phrase in paragraph (1) was the same as the Secretary's: to refer to "mandatory provisions" would produce a different meaning. The present wording made it possible to invoke the entire Convention, so that any provision not derogated from became mandatory. In his view, the wording should be kept as it stood, but it might be advisable to consider the problem as and when other articles were examined.

20. In regard to the other point raised by the representative of Italy, in his understanding, article 13(1) did not affect either the rights of the principal/applicant himself or the rights of the guarantor/issuer in relation to the principal/applicant.

21. Mr. HERRMANN (Secretary of the Commission) said that when he had explained his understanding of the phrase "subject to the provisions of this Convention", he had not gone into the issue of whether any given provision of the Convention was mandatory or not, or how that should be expressed. It could have been stated, for instance, that all provisions were mandatory—or, if preferred, non-mandatory—unless otherwise specified. The chosen solution had been to use in any individual provision a form of words such as "unless otherwise stipulated in the undertaking or elsewhere agreed . . ." in order to show that it was a non-mandatory provision. If the word "mandatory" were inserted in the first phrase of paragraph (1), the provisions referred to would then be only mandatory provisions, which would then prevail over the terms and conditions set forth in the undertaking. There could, however, be a practical problem in situations where the parties had not derogated from non-mandatory provisions by excluding a particular provision or by incorporating some positive regulation. It would then not be clear whether the non-mandatory provisions applied or not.

22. Mr. BONELL (Italy) said that he agreed in substance with the Secretary's explanation, but still felt that the present wording "subject to the provisions of this Convention" might be a little ambiguous. It might be preferable to say "The rights and obligations of the guarantor/issuer and the beneficiary are determined by the provisions of this Convention and . . .".

23. On the question of mentioning only two of the three parties involved, he would urge that it be made absolutely clear that article 13 referred only to rights and obligations arising from the undertaking.

24. Mr. BYRNE (United States of America) said that the discussion initiated by the first phrase of paragraph (1) had been very interesting and the Secretary's explanation very persuasive. However, an easier way of achieving the desired result and avoiding divergent interpretations might be to delete that opening phrase and add the words "arising under this Convention" after "and the beneficiary". He pointed out that the words "subject to" were used in article 17 to create an exception.

25. Mr. EDWARDS (Australia) said that it would be difficult for him to accept the United States proposal, because, in his view, the rights being protected in paragraph (1) were far more extensive than was suggested by that wording. Any change in the present wording might create more problems than it solved. The present formulation was not an unusual one, and it did not really matter if some room was left for interpretation. He thus supported the text as it stood.

26. Mr. STOUFFLET (France) said that paragraph (2) provided guidance for the judge regarding the interpretation of guarantees and stand-by letters of credit, so that if something was not clear in the text, the judge could take account of international rules and usages. But if the parties in their specific contracts had excluded some international instrument or other, he wondered whether the judge would, even so, be able to take account of such an instrument. It might be more rational to state that international rules and usages of independent guarantee or stand-by letter of credit practice would be taken into account "unless reference to such texts is explicitly excluded".

27. The CHAIRMAN, speaking as representative of Singapore, said that, as his country understood it, the phrase "subject to the provisions of the Convention" in paragraph (1) referred to all provisions in the Convention relevant to a particular problem, and not just to mandatory provisions.

28. Mr. ILLESCAS (Spain), referring to article 13(1), said that it was not entirely clear whether the Convention was mandatory or not in regard to the rights and obligations of the guarantor/issuer and beneficiary. He agreed with the Secretary's explanation, but had his doubts as to whether the terms employed in the text were the most appropriate ones. His delegation would prefer to have a reference at the beginning of article 13 to article 1(1), thus recognizing a possibility for the parties to come to an agreement as to whether or not the guarantees concerned were subject to the Convention. Thus article 13(1) could begin "Subject to the provisions in article 1, paragraph (1), of the present Convention" and then continue as in the present text. That would clarify the mandatory or non-mandatory nature of the provisions of the Convention used by the parties, which were free to decide for

themselves whether or not their agreement was subject to the Convention. The parties could decide that article 1(1) would apply or that the rules and obligations should be determined by the Convention, by the terms and conditions set forth in the undertaking, or by any other rules, general conditions or usages. A similar clause could be introduced into the second paragraph.

29. Mr. MARKUS (Observer for Switzerland) said that he himself agreed with the interpretation of the first phrase of paragraph (1) given by the Secretary, but had come to realize that it could be understood differently by others. It might lead to the erroneous conclusion that every provision not containing the phrase "unless otherwise stipulated or elsewhere agreed" was mandatory. Article 15, for example, did not contain that form of words but was not in his view mandatory. As he saw it, the real problem was with the phrase "subject to" and he wondered whether a more satisfactory term could be found.

30. Mr. FAYERS (United Kingdom) suggested that, in view of the divergent interpretations, the discussion be adjourned and the drafting group asked to submit alternative forms of words from which a choice could be made.

31. Mr. GAUTHIER (Chairman of the Committee of the Whole) suggested that the phrase "subject to the provisions of this Convention" be deleted and the paragraph amended to read: "The rights and obligations of the guarantor/issuer and the beneficiary arising from the undertaking are determined by the provisions of this Convention and by the terms and conditions as set forth in the undertaking, including any rules, general conditions or usages specifically referred to therein".

32. Mr. EDWARDS (Australia) said that some of the problems connected with the words "subject to", which he understood to create difficulties in certain languages, could be resolved by replacing the phrase "Subject to the provisions of this Convention" by "Except where the application of this Convention otherwise determines".

33. Mr. AL-NASSER (Saudi Arabia) said that he had understood that the Spanish proposal had been to amend the provision to read: "The rights and obligations of the guarantor/issuer and the beneficiary are determined by the terms and conditions set forth in the undertaking in conformity with the provisions of this Convention and any rules and general conditions specifically referred to therein".

34. Ms. CZERWENKA (Germany) said that the expression "the rights and obligations arising from the undertaking are determined by the terms and conditions set forth in the undertaking" was somewhat circuitous. She believed that there was in fact a common understanding of the meaning of the words "subject to the provisions of this Convention" and therefore suggested that those words be retained.

35. Ms. FENG Aimin (China) endorsed those views. However, if the text was to be amended it would be better to say: "The rights and obligations of the guarantor/issuer and the beneficiary arising from the undertaking shall be determined by the provisions of this Convention. In the absence of any such provisions, they shall be determined by the terms and conditions of the undertaking."

36. The CHAIRMAN, speaking as representative of Singapore, said that if the suggestion by the Chairman of the Committee of the Whole were accepted, it would not be clear, in the event of a conflict between the provisions of the Convention and any of the terms and conditions in the undertaking, which should prevail, whereas the formula "subject to the provisions of this Convention" in the present text implied that the provisions of the Convention would prevail.

37. Mr. LAMBERTZ (Observer for Sweden) did not agree that all delegations had understood the words "subject to the provisions of this Convention" in the same way. He had always understood that an article would be mandatory if nothing to the contrary was stated. If that was not the right interpretation, the fact should be made clear. The Commission would then have to specify in each article whether it was mandatory or not.

The meeting was suspended at 11.10 a.m. and resumed at 11.40 a.m.

38. Mr. GAUTHIER (Chairman of the Committee of the Whole) suggested that the reference to the provisions of the Convention might be moved to the end of article 13(1), which would then read: "The rights and obligations of the guarantor/issuer and the beneficiary are determined by the terms and conditions set forth in the undertaking, including any rules, general conditions or usages specifically referred to therein, and by the provisions of this Convention."

39. Several techniques existed to make it clear which articles of the Convention were mandatory. One would be to list them, another to include in the non-mandatory articles the words "unless otherwise agreed". The context, moreover, would indicate whether or not the provision was mandatory.

40. Ms. CZERWENKA (Germany) said that article 13(1) as it stood was sufficiently clear to explain the relationship between the guarantor/issuer and the beneficiary, but that she would have problems if it were amended to include the words "arising from the undertaking".

41. Mr. BONELL (Italy) was in favour of the wording suggested by the Chairman of the Committee of the Whole, which clarified the scope of the provision.

42. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that he took it that in the absence of any objections, the Commission agreed to the wording he had suggested for article 13(1).

43. He invited comments on the French proposal to amend article 13(2) by inserting the phrase "unless reference to such texts is specifically excluded" after the words "regard shall be had".

44. Ms. CZERWENKA (Germany) supported that proposal.

45. Mr. BYRNE (United States of America) said that the present text of article 13(2) was a delicate compromise reached after much deliberation. To introduce the words proposed would upset the balance achieved. He believed that if the parties to an undertaking excluded certain practices that would itself be one of the terms and conditions of the undertaking.

46. Mr. BONELL (Italy) considered that the French proposal would create problems and should not be adopted.

47. Mr. CHOUKRI SBAI (Observer for Morocco) said that his delegation believed that the additional text proposed by the representative of France complicated matters. Judges should have the possibility of taking international standards of practice into account when seeking to find suitable solutions. The text of paragraph (2), as it currently stood, was sufficiently flexible and should remain unchanged.

48. Mr. BOSSA (Uganda), agreeing with the observer for Morocco, said that the French proposal could lead to problems regarding the standards to be applied in cases where neither the undertaking nor the Convention dealt with a particular question and reference to international rules and usages had been excluded.

49. Ms. CZERWENKA (Germany) said that, according to the drafting practice adopted in the Working Group, whenever a provision was not mandatory and it was possible to derogate from it, that possibility had to be expressly stated. Her delegation felt that such a proviso afforded greater flexibility, by allowing the parties to agree whether or not particular rules should be applicable. That was why she had supported the French proposal. In its consideration of article 14(1), the Working Group had discussed at length the degree to which regard should be had to generally accepted standards, and it had finally been agreed, in the interests of flexibility, to employ the phrase "due regard". A similar result might be achieved in article 13(2) by replacing the words "regard shall be had" by "regard may be had".

50. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that the current wording of paragraph (2) was the outcome of efforts by the Working Group to achieve a compromise and a balance. He did not believe that the Working Group had ever considered that the text of that paragraph should constitute an invitation to judges or arbitrators to disregard a stipulation made elsewhere by the parties to the effect that specific international rules should not be referred to. Perhaps the issue could be resolved by leaving the text unchanged and stating clearly in the records that it was not the Commission's intention that article 13(2) should imply any such invitation.

51. With regard to the Working Group's agreed practice of inserting a proviso in order to indicate the possibility of derogation, the need for such an insertion did not always arise if it was abundantly clear from the context or the construction of an article that its provisions were not mandatory.

52. Mr. FARIDI ARAGHI (Islamic Republic of Iran) said that his delegation supported the view that the current text of paragraph (2) possessed sufficient flexibility and should not be amended.

53. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that he took it that the Commission wished to adopt article 13(2) as it stood.

54. *It was so decided.*

Article 14 (A/CN.9/408, annex)

55. Mr. GAUTHIER (Chairman of the Committee of the Whole) introduced the article.

56. Mr. SHISHIDO (Japan), referring to paragraph (2), asked whether the reference to liability applied to the guarantor/issuer's relationship with the beneficiary or also included its relationship with the principal/applicant.

57. Mr. HERRMANN (Secretary of the Commission) said that the question of liability had to be viewed on the basis of the criteria of good faith and reasonable care in the guarantor/issuer's performance of its obligations under the undertaking and the Convention, as indicated in paragraph (1), which had to be read in conjunction with paragraph (2). Thus it was essentially liability towards the beneficiary that was intended, but not exclusively, since, under the Convention, the guarantor/issuer had certain obligations towards the principal/applicant, although they were now fewer than in the earlier stages of its drafting.

58. Ms. FENG Aimin (China) said that her delegation disagreed with the use of the term "grossly" in paragraph (2). It was unlikely that acts constituting gross negligence would occur in banking practice. Banks had to be liable for any negligent conduct on their part.

59. Mr. CHOUKRI SBAI (Observer for Morocco) said that under Moroccan law a prior condition granting exemption from liability could be established in regard to simple negligence but not in regard to gross negligence or fraud. His delegation was therefore in favour of retaining the reference to gross negligence.

60. With reference to the question raised by the representative of Japan, he believed that non-exemption from liability applied primarily to the relationship between the guarantor/issuer and the principal/applicant, since the undertaking was drawn up between those two parties. But the general rules also established protection for the beneficiary. The guarantor/issuer should not be permitted to act towards the beneficiary in bad faith or be grossly negligent in its conduct *vis-à-vis* the beneficiary.

The meeting rose at 12.30 p.m.

Summary record of the 558th meeting

Tuesday, 9 May 1995, at 2 p.m.

[A/CN.9/SR.558]

Chairman: Mr. GOH (Singapore)

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

The meeting was called to order at 2.05 p.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 14 (A/CN.9/408, annex)

1. Mr. GAUTHIER (Chairman of the Committee of the Whole) invited the Commission to continue its discussion of article 14.

2. The CHAIRMAN, speaking in his capacity as the representative of Singapore, said that he supported the proposal by the representative of China to delete the word "grossly". If a bank was negligent, it should be liable.

3. Mr. EKENTA (Nigeria), also endorsing the proposal made by the representative of China, said that the provision as it stood allowed the guarantor too much room for manoeuvre.

4. Ms. FENG Aimin (China) said that there was still a problem as to whether negligence resulted in recourse by the applicant.