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.

5. Mr. BYRNE (United States of America) said that paragraph (2) reflected the Working Group's conclusion that the parties could agree by contract that the risk of certain negligent behaviour be borne by one party rather than the other. Paragraph (2) set forth the limits to that ability.

6. The URDG and UCP rules made it clear that specific types of risk were borne by the principal/applicant; that was set forth contractually either expressly or by the incorporation of those standard sets of rules. To disrupt the freedom to contract out with regard to ordinary negligence would render the Convention unacceptable to the banking community. From the standpoint of public policy and public order, however, it was important to express in the article that there were limits to party autonomy.

7. Mr. BONELL (Italy) said that what was at stake was not the liability of a bank for negligent conduct, failing any limitation in the undertaking, but rather a limit to the freedom of the bank *vis-à-vis* the beneficiary to contract out of such liability in certain instances. The freedom to exclude liability for "near-negligence" was a well-established principle of contract law and should not be denied.

8. Though there might be discussion of the best formulation, he was convinced that the underlying idea of the current draft should be maintained.

9. Mr. CHOUKRI SBAI (Observer for Morocco) supported the remarks made by the representatives of the United States and Italy. The paragraph should be retained in its present form.

10. Ms. FENG Aimin (China) said that she disagreed with the representative of the United States. According to article 16 of UCP 500, the bank assumed no liability for errors in translation, but that did not mean that the bank should not assume any other liability for negligent conduct.

11. Mr. HERRMANN (Secretary of the Commission) said it was important to recognize the difference in legal status and effect of the UCP and URDG rules, which applied to contracts, and the draft Convention, which could effectively establish a firm legal limit. The problem addressed by paragraph (2) of article 14 was one which neither UCP, in most jurisdictions, nor URDG, could effectively address, namely, the limit to the freedom of the parties. There was no inconsistency between the rules on liability in article 15 of URDG and in the draft Convention.

12. Mr. GAUTHIER (Chairman of the Committee of the Whole) took it that the Commission wished to approve the draft of article 14 as it stood.

13. *It was so agreed.*

Article 15 (A/CN.9/408, annex)

14. Mr. GAUTHIER (Chairman of the Committee of the Whole) introduced article 15.

15. Ms. CZERWENKA (Germany) said that, to be consistent with article 2, which provided that the Convention should cover only those undertakings where the demand had to be in some documentary form, the last sentence of article 15 should probably be construed as covering only instances where no certification or other document accompanying the demand was required.

16. Mr. HERRMANN (Secretary of the Commission) said that, to understand the rationale of the phrase "certification or other document" in the last sentence of article 15, it should be remembered that, at an earlier stage, the Working Group had decided to include the words "upon presentation of other documents" in paragraph (1) of article 2 in order to avoid the misinterpretation that the demand was not a document. That had entailed consequential drafting changes.

17. The word "certification" in the last sentence of article 15 was intended to refer to an additional statement, so as to emphasize further that the demand was itself a document. The insertion of the words "in addition to the demand" after the words "or other document" might help to make that point clear. As the representative of Germany had suggested, a document accompanying the demand was referred to.

18. Mr. FARIDI ARAGHI (Islamic Republic of Iran) said that he supported the suggestion of the representative of Germany. There were two different types of demand: those which required documentary presentation and those which did not. However, even in the case of a simple demand, there had to be certification that the demand was not improper.

19. Mr. GAUTHIER (Chairman of the Committee of the Whole) explained that it should be understood from the last sentence of the article that, if certification was required, it had to be produced; however, in cases where no such certification was required, the mere fact of making a demand implied certification by the beneficiary that the demand was not being made in bad faith or was not otherwise improper.

20. Mr. EDWARDS (Australia) said that the last sentence of article 15 seemed to be predicated on the assumption that, where additional certification or documentation was provided, it would always be evidence of good faith. However, if that other documentation conveyed nothing about good faith, no such inference could be drawn.

21. Mr. HERRMANN (Secretary of the Commission) said that the wording did not imply an assumption as to whether there was good faith or not; it simply added a provision to cover the case of a simple demand for payment. In a document which called for a statement by the beneficiary concerning performance of a contract, the question of good faith could arise, but there could be no bad faith in a demand for payment as such.

22. Mr. EDWARDS (Australia) said that the Secretary's explanation did not meet his concern, since it appeared to confirm that the other documentation would of itself, and by its very nature, imply good faith. However, such documentation must constitute evidence, otherwise there could be no implied certification of good faith. Assuming that the intended meaning was that there was no requirement of certification or other document, to provide evidence from which good faith might be inferred, so that good faith was to be inferred from the demand itself, then the text should make that clear.

23. Mr. GAUTHIER (Chairman of the Committee of the Whole) explained that the Working Group had always considered that a demand accompanied by other documents would constitute sufficient grounds for payment. Not all documents would contain a certification or representation that the demand was in good faith, but if they were couched in the terms agreed, they would fulfil the obligation. It was only in the case of a simple demand that the Working Group considered that the Convention should state that, by making the demand, the person making it implicitly indicated that the demand was not in bad faith.

24. Mr. BONELL (Italy) said he had some difficulty in understanding the Australian representative's concern. He too would have thought that once a document of the kind envisaged under article 2 was presented, it could be inferred that payment was due. He wondered whether the last sentence in article 15 was in fact necessary, since, as he saw it, article 2, paragraph (1) also related

to simple demand. However, he could accept the formulation proposed.

25. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that article 2 was more definitional and did not fix the law or set boundaries, as this article would.

26. Ms. CZERWENKA (Germany) recalled that there had been some discussion in the Working Group as to whether a supporting statement should be required in addition to the demand. In the end, it had been decided to cover that point by means of the final sentence of article 15, which she believed should be retained.

27. She saw some merit in the question raised by the Australian representative as to why, if all demands were documentary, a distinction should be made between demands consisting of one document and demands consisting of several documents. That concern might be met if the last sentence were amended to read: "The beneficiary, when demanding payment, is deemed to certify that the demand is not in bad faith or otherwise improper".

28. Mr. LAMBERTZ (Observer for Sweden) said he could accept the German suggestion, although he would be inclined to prefer the existing text. Logically, the Australian representative was right to point out that it should be clear that good faith was also implied where the demand was accompanied by documents. However, the need for implied certification was much greater in the case of simple demand.

29. In his view, the first sentence was uncontroversial and self-evident, the second was non-mandatory and the third was a mandatory provision, though that need not be stated explicitly.

30. Mr. FAYERS (United Kingdom) agreed that the last sentence should be redrafted to meet the concern of the German and Australian representatives. However, it was important to include it, in order to provide an eventual cause of action by the principal against the beneficiary in the case of a fraudulent or improper demand.

31. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that in redrafting the sentence it should be borne in mind that its original purpose had been to focus attention on simple demand. The word "improper" might have to be deleted, since it had been agreed not to use it in article 19.

32. Mr. SHISHIDO (Japan) said he would regard the first and third sentences of article 15 as mandatory. The second sentence implied that the parties might stipulate other persons or places of presentation but did not mention time in that context. He asked whether the time referred to at the beginning of the sentence was the time of presentation of the demand or the time of dispatch, or whether there was party autonomy on that point.

33. Mr. HERRMANN (Secretary of the Commission) said that as he saw it the text was to be interpreted as being based on the theory of presentation and not of dispatch. He did not recall that the Working Group had discussed the question, but his impression was that the intent had been to create absolute certainty, even at the risk of thereby disregarding certain provisions, by requiring that the demand had to be presented within the time required if it was to be effective. If the Commission wished to rule that the provision was non-mandatory in regard to the time element, that should be made clear in the text. However, he himself would regard it as mandatory as to time.

34. Mr. BONELL (Italy) said that, if an undertaking fixed a time within which the demand had to be presented, the question of whether the time element was or was not mandatory did not arise: it was simply a case of *pacta sunt servanda.* With respect to the receipt versus the dispatch theory, on the other hand, his understanding of the second sentence was that it tended towards the receipt theory but, since it allowed for an alternative, it was in any case not intended to be mandatory.

35. Mr. GAUTHIER (Chairman of the Committee of the Whole) pointed out that the non-mandatory clause beginning "unless" related only to the question of to whom and where the document was to be presented, but not to the time aspect.

36. Mr. STOUFFLET (France) said he did not know whether the second sentence as it stood was to be interpreted as mandatory as to the time element. However, if it were not, he saw no reason to make it so, since it should be for the parties themselves to decide whether the time-limit stipulated should be date of dispatch or date of receipt of the document.

37. Mr. SHISHIDO (Japan) shared that view. Although he agreed with the Secretary's explanation of the second sentence, he considered that a rule based on date of receipt was much more reasonable than a rule based on date of dispatch. He did not see the need to make the time requirement mandatory, in view of the Commission's desire to make the Convention as non-mandatory as possible. The parties might consider it reasonable for the bank to take into account the risk of delays in the mail.

38. Ms. BAZAROVA (Russian Federation) said her delegation considered that the time requirement should be based on date of receipt, since date of dispatch would be very difficult to establish. Failure to include a mandatory time requirement could lead to difficulties and controversies for the guarantor. The issue was an important one which ought to be covered by the Convention, and the provision should not be made too flexible.

39. Mr. BYRNE (United States of America) drew attention to the existence in his country of the notion of warranty of truthfulness of presentation. Because of that, the last sentence of the article should not be modified in any way that touched on that issue; in other words, its substance should continue to be confined to the two issues of absence of bad faith and impropriety of the demand.

40. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that, if he heard no further comments, he would take it that the Commission referred article 15 to the drafting group with a request to incorporate in it the notion of full party autonomy with regard to the modalities and time of presentation, and to reconsider the use of the word "improper".

41. *It was so agreed.*

The meeting was suspended at 3.40 p.m. and resumed at 4.10 p.m.

Article 16 (A/CN.9/408, annex)

42. Mr. ADENSAMER (Austria) said that disputes frequently arose about the time from which periods such as the period of seven business days referred to in paragraph (2) began to run. In order to obviate that in the case of the Convention, he suggested the insertion, after the word "days", of the words "from the day following receipt".

43. Mr. MARKUS (Observer for Switzerland) said that, in his country's banking experience, stand-by letters of credit and guarantees normally required the presentation of fewer documents than commercial letters of credit, and three days would therefore be sufficient for the operations contemplated in paragraph (2). Accordingly, he suggested the replacement of the word "seven" by "three" or, if that was considered too short, by "five". By

virtue of the proviso at the beginning of the paragraph, the parties would always have liberty to agree on a different number of days if they wished.

44. Mr. CHOUKRI SBAI (Observer for Morocco) endorsed the Swiss proposal for specifying a shorter period of time, because of the importance of handling transactions quickly.

45. Mr. GAUTHIER (Chairman of the Committee of the Whole) reminded the Commission that the rule in paragraph (2) had been worded so as to cover many situations, from simple demand to that of a stand-by letter of credit requiring the presentation of a large number of documents; it was essentially a rule of reasonable time, not a seven-day rule, and one which accorded with practice, including the practice reflected in the UCP rules.

46. Mr. SHISHIDO (Japan) said that the period of seven business days should be available to each of the banks successively involved in handling a payment demand. That would be consistent with the corresponding provision in article 13*(b)* of the UCP rules. He therefore suggested the addition, after the words "seven business days", of text to the effect that the prescribed period should count for each entity concerned.

47. Mr. GAUTHIER (Chairman of the Committee of the Whole) reminded the Commission that the Working Group had discussed the point raised by Japan. In approving the provision as it stood, the Group had agreed that it might need to be reviewed.

48. Mr. CHOUKRI SBAI (Observer for Morocco) said that, while recognizing the force of the proviso at the beginning of the paragraph, if the stipulated period was not reduced, problems would arise. Also, it would be useful to specify that the last day of the period was counted, but not the first, and that the period should consist of not more than seven business days, beginning on the day of the demand, or alternatively on the day on which documents were presented.

49. Mr. LAMBERTZ (Observer for Sweden) said that he continued to hold the views about article 16 expressed by the Working Group (see A/CN.9/408, para. 54) and he trusted they were shared by the Commission. If so, paragraph (1) would be supplettive, not mandatory, in the relationship between the guarantor/issuer and the principal/applicant. In the relationship between the guarantor/issuer and the beneficiary, on the other hand, he felt it would be mandatory. That implied a contradiction, since paragraph (1) referred to the standard of conduct prescribed in article 14(1) which, because of the provision in article 14(2), was not itself mandatory. In drawing the Commission's attention to that situation, his delegation had no proposal for rectifying it and could accept the text as it stood.

50. In reply to a question put by Mr. GAUTHIER (Chairman of the Committee of the Whole), Mr. SHISHIDO (Japan) said that, in suggesting that the seven-day period should be allowed for each entity concerned, he had had in mind the counter-guarantor and the confirmer in addition to the guarantor. However, other entities might conceivably be involved, for example a nominated bank, as mentioned in article 13*(b)* of the UCP rules.

51. Mr. EDWARDS (Australia) asked whether the intention behind the Japanese suggestion was that the various periods of time should be cumulative.

52. Mr. HERRMANN (Secretary of the Commission) said it had been agreed in the Working Group that the provision in article 16(2) should be seen, in the light of the definition of the term "guarantor/issuer" in article 6, as including a counter-guarantor and a confirmer. In other words, paragraph (2) would mean that, whenever the question arose, the entity concerned, whether a guarantor/issuer or a counter-guarantor or a confirmer, would have a maximum of seven business days in which to act. Looking at article 13*(b)* of the UCP rules, he did not believe it was intended to have the cumulative effect that, if one entity acted in less than seven business days, for example three business days, the succeeding entity would have ten business days at its disposal. In his view, therefore, the present text of paragraph (2) and the version proposed by Japan had the same meaning.

53. In one respect, though, the two approaches differed, in that the Japanese representative had raised the possibility that a nominated bank might be involved as well. In regard to documentary credits, the UCP rules contemplated that situation in referring to a nominated bank appointed by another entity to act on its behalf in examining documents. In such a case, the nominated bank would simply be an agent, and the Working Group had agreed that the Convention should make no specific provision for the situation of agents, which would be governed by the general law of agency. That being so, article 16(2), as it stood, would apply to a nominated bank.

The meeting rose at 5 p.m.

Summary record of the 559th meeting

Wednesday, 10 May 1995, at 9.30 a.m.

[A/CN.9/SR.559]

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 16 (continued) (A/CN.9/408, annex)

1. Mr. GAUTHIER (Chairman of the Committee of the Whole) reminded the Commission of the three points that had been raised in connection with article 16 at the previous meeting: a suggestion by the representative of Japan that additional text be included in order to indicate that the reference to the guarantor/issuer was intended, where appropriate, to apply to the counter-guarantor or the confirmer; a suggestion by the observer for Switzerland that the maximum period referred to in paragraph (2) be reduced from seven to three business days; and a suggestion by the representative of Austria that, for purposes of clarification, a phrase such as