



UNITED NATIONS  
GENERAL  
ASSEMBLY



Distr.  
LIMITED

A/CN.9/WG.IV/WP.35  
27 August 1987

ORIGINAL: ENGLISH

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UNITED NATIONS COMMISSION  
ON INTERNATIONAL TRADE LAW  
Working Group on  
International Payments  
Sixteenth session  
Vienna, 2-13 November 1987

ELECTRONIC FUNDS TRANSFERS

Note by the Secretariat

1. At its nineteenth session in 1986 the Commission decided to begin the preparation of Model Rules on electronic funds transfers and to entrust this task to the Working Group on International Negotiable Instruments, which it renamed the Working Group on International Payments 1/. It also decided that the first meeting for this purpose (sixteenth session of the Working Group) should be held in 1987 after the twentieth session of the Commission 2/. The session of the Working Group has been scheduled to be held at Vienna from 2 to 13 November 1987.

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1/ Report of the United Nations Commission on International Trade Law on the work of its nineteenth session, Official Records of the General Assembly, Forty-first Session, Supplement No. 17 (A/41/17), para. 230.

2/ Ibid., para. 273.

2. The Commission decided that the Model Rules should be flexible and should be drafted in such a way that they did not depend upon specific technology. Where appropriate, the Model Rules should present alternative solutions in order to take into account differences in banking systems. Furthermore, the Model Rules should deal with the relationship between banks as well as the relationship between banks and their customers 3/.

3. It was suggested that the Working Group should begin its work by considering the list of legal issues set forth in the final chapter of the UNCITRAL Legal Guide on Electronic Funds Transfers 4/ (hereafter cited as UNCITRAL Legal Guide) as well as any other issues the secretariat might consider appropriate to place before the Working Group.

4. This report presents issues that might be considered for inclusion in the Model Rules. Since the list of legal issues in the UNCITRAL Legal Guide and the commentaries thereon did not envisage the preparation of a specific legal text and additional issues might be considered in the Model Rules, it was thought preferable to prepare a new report oriented towards the preparation of these Rules. The list of issues in this report is based on the list of legal issues in the UNCITRAL Legal Guide. In many cases it repeats the question in a modified form and either refers to the commentary or repeats some portion of it. It should be noted that the terminology used in this report is that used in the UNCITRAL Legal Guide.

5. The Working Group may consider it desirable to consider the various issues without reaching final decisions and, at the end of its review of those issues, to decide on the next actions to be taken.

## I. SCOPE OF APPLICATION

I.1 Should the Model Rules apply only to international funds transfers or also to domestic funds transfers?

6. The principal reason for the Commission to undertake the preparation of these Model Rules is to reduce conflicts in legal rules in cases of international funds transfers. A common means used to reduce the conflicts in legal rules governing international trade is to adopt a special legal regime whose scope of application is limited to international transactions of the type in question. This technique works best when international transactions can be clearly distinguished from domestic transactions. In some cases certain domestic aspects of an international transaction cannot be ignored. If a special international legal regime is nevertheless desired, that legal regime will have to include the domestic aspects of the transaction that cannot be ignored. The alternative is to adopt harmonized or unified rules governing all transactions of the type in question, whether domestic or international.

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3/ Ibid., para. 231.

4/ A/CN.9/Ser.B/1. The list of legal issues is also found unchanged in substance in the draft UNCITRAL Legal Guide, A/CN.9/266/Add.2.

7. In the case of international funds transfers, it would not be possible to construct a legal regime that included the relationship between the customer and the bank, as directed by the Commission, without including some domestic elements. It is undoubtedly in large part for this reason that the 1930 Geneva Convention providing a Uniform Law for Bills of Exchange and Promissory Notes and the 1931 Convention providing a Uniform Law for Cheques were intended to unify the law governing domestic as well as international transactions.

8. As a result it may be thought that the preparation of the Model Rules might proceed on the assumption that they will apply to both domestic and international funds transfers.

I.2 Should the Model Rules apply only to electronic funds transfers or also to paper-based funds transfers?

9. The increase in international funds transfers that stimulates an interest in preparing these Model Rules has been brought about by the increased use of electronic funds transfer techniques. These techniques apply both to the transmission of a customer's funds transfer instruction between banks and to the transmission of an instruction between the customer and the bank. Commercial law issues arising in the context of electronic funds transfers can be divided into three categories: those that are common to all forms of electronic data transfer (e.g. proof of transactions), banking law issues unique to electronic funds transfers and, as shown by the discussion in the UNCITRAL Legal Guide, general banking law issues that are as much at question in paper-based funds transfers as they are in electronic funds transfers. This suggests the usefulness for the Model Rules to apply both to electronic funds transfers and to paper-based funds transfers, with the probable exception that they should not apply to negotiable instruments, including cheques.

10. If it were to be decided that the Model Rules should apply only to electronic funds transfers, a definition of the term would be necessary for determining the scope of application. The definition used in the UNCITRAL Legal Guide that

"an electronic funds transfer ... is a funds transfer in which one or more of the steps in the process that were previously done by paper-based techniques are now done by electronic techniques" 5/

served a useful purpose in the context of the Legal Guide, since it furnished a basis on which to analyse the impact of various types of electronic techniques on the pre-existing legal rules governing paper-based funds transfers. However, the definition would serve less well for determining the scope of application of the Model Rules, or other legal text.

11. The definition of an electronic funds transfer, and therefore the scope of application of the Model Rules, might be restricted to funds transfers where the customer initiated the transaction by giving his instruction in electronic form. Such a definition was used in the Electronic Funds Transfer Act of 1978 in the United States of America, the purpose of which was to protect consumers. However, such a definition would exclude all funds transfers, including large international commercial funds transfers executed by electronic means, from the scope of application of the Model Rules when the customer's instruction to transfer the funds was given on paper or orally.

12. The definition and therefore the scope of application might be restricted to funds transfers where the inter-bank instruction was sent by electronic means. However, that would make the application of the Model Rules to the bank-customer relationship depend on the method used by the bank to forward the instruction, a matter which is often outside the control of the customer, and which the customer might not even know. Furthermore, instructions might be sent between several banks to implement the customer's instruction. Some of those instructions might be paper-based and some might be electronic.

I.3 Should the Model Rules apply to both credit transfers and debit transfers?

13. Interbank funds transfers, whether debit transfer or credit transfer, are effectuated by debits and credits to accounts in banks. As a result of this basic similarity, some of the legal issues might be treated in an identical manner, or at least in a substantially similar manner. However, there are a number of differences in banking practices between debit transfers and credit transfers that call for totally different legal rules.

14. It may be thought that it would be preferable to begin the preparation of the Model Rules for credit transfers only, since these are operationally less complicated than debit transfers. At a later time it could be decided whether it would also be desirable to include debit transfers, and what changes or additions would be necessary in order to do so. If this approach were taken, care should be taken when preparing the Model Rules for credit transfers to avoid decisions that would later increase the difficulty of incorporating debit transfers.

15. It may be noted that some of the issues in this report are applicable only to credit transfers. Several additional issues will need to be considered if it is decided that the Model Rules should also apply to debit transfers.

16. In any case, it may be thought that funds transfers effectuated by the use of negotiable instruments, including cheques, should be excluded from the Model Rules. Issues arising because of truncation in the collection process of such instruments or because of other use of electronic techniques might better be handled by modifications to the existing law governing such instruments.

- I.4 Should the Model Rules apply only to funds transfers where accounts at banks are to be debited and credited or should they also apply where accounts at other financial institutions are to be debited and credited?

17. It may be thought that this issue need not to be addressed in the preparation of the Model Rules, even though it may be an important issue within any given country. The word "bank" could be used throughout the preparation of the Model Rules without prejudice to the definition that the word might be given at a later time or by users of the Model Rules.

18. It may be thought that the Model Rules should apply where the account of the transferor is to be debited but cash is to be paid to the transferee or where the transferor pays in cash to a bank for credit to the account of the transferee at the same or a different bank, but that the Model Rules should not apply where funds are paid in by the transferor and are to be paid in cash to the transferee.

- I.5 Should consumer electronic funds transfers be excluded from the scope of application of the Model Rules?

19. All types of electronic funds transfers, including those that might be classified as consumer transfers, were considered in the UNCITRAL Legal Guide. In most cases the legal issues in consumer and non-consumer funds transfers were found to be the same. In those cases where different legal issues arose, or in the more frequent cases where the same legal issues arose but a different legal rule might be envisaged for consumer funds transfers, this was pointed out. For that purpose it was not necessary to define what was a consumer funds transfer.

20. If consumer funds transfers were to be excluded from the scope of the Model Rules, a definition would have to be given. It could be based on the characterization of the transferor or of the transferee of the funds, e.g. a party who was neither characterized as a commercial party nor as an agency of the State might be considered to make consumer funds transfers, but it could not be based on the purpose of the funds transfer, as it was in the United Nations Convention on Contracts for the International Sale of Goods, where sales of goods for personal, family or household use were excluded. Other bases for distinguishing consumer funds transfers could be the amount of money involved (a generally unsatisfactory distinction) or the funds transfer technique used. It can be assumed, for example, that funds transfers executed by use of plastic card technology are, at the present time, normally consumer funds transfers while certain high-value systems are normally for non-consumer purposes.

21. However, while the current technology and its uses offer some means of distinguishing between consumer and non-consumer funds transfers, the distinction between the two is not inherent in the technology. It is possible that the plastic card technology will evolve in such a way that it will serve as the basis for most electronic funds transfer authentications, both consumer and non-consumer. Similarly, facilities that are currently used for high-value on-line funds transfer instructions may also be used for batch transmission of low-value funds transfer instructions. Therefore, the criteria for distinguishing between consumer and non-consumer funds transfers on the basis of the funds transfer technology utilized may be different in the future from what it might be today.

22. Since the Commission has decided that the Model Rules should present alternative solutions in order to take into account differences in banking systems, the Working Group might consider the possibility of indicating those issues where some countries might wish to adopt different rules for consumer funds transfers. It would be a separate question whether the Working Group wished to consider what the nature of those different rules might be.

## II. DEFINITIONS AND GENERAL PROVISIONS

### A. Definitions

II.1 What terms should be defined in the Model Rules and what should be the orientation of the definition given?

23. Definitions of certain terms will be necessary, especially since there is a wide discrepancy in the terms used for both legal purposes and banking purposes in different countries. Important policy choices are often reflected in the terms chosen and the definitions given to those terms. The following are terms and types of terms that might be defined:

#### a. Parties to a funds transfer

24. There are three principal variables to be considered in choosing the terms to be used in describing the parties to a funds transfer: (1) whether the parties are to be described in terms of the flow of funds (e.g. transferor, transferor bank, transferee, transferee bank as used in the UNCITRAL Legal Guide) or in terms of the flow of the instructions (e.g. initiating bank, destination bank, reimbursing bank); (2) whether the same terminology can be used for both debit transfers and credit transfers, if both are to be covered by the Model Rules; and (3) whether the parties are to be described in terms of the entire funds transfer, as suggested by the terms in the UNCITRAL Legal Guide, or in terms of a particular segment of the funds transfer (e.g. sending bank, receiving bank), as is the case with the terminology proposed by the Banking Committee of the International Organization for Standardization (ISO TC 68) for its international standards, e.g. ISO DIS/7982.

25. The number of terms used should be kept to a minimum consistent with clarity. A proliferation of terms means that the same party may be described by several terms depending on the point of view (i.e. the first bank in a credit transfer might be the "transferor bank", the "initiating bank", the "receiving bank" of the instruction from the customer and the "sending bank" of an instruction to the second bank). This may make it more difficult to know which party is being referred to. However, it may make it easier to state legal rules governing all parties who act in a similar way. For example, a "sending party" may be required to take certain precautions whether that party is a non-bank customer, a transferor bank or an intermediary bank.

#### b. Bank

26. If the word "bank" is defined, the definition would be an important determinant of the scope of application of the Model Rules. See issue I.4.

c. Funds transfer instruction

27. This term was used throughout the UNCITRAL Legal Guide to indicate all types of instructions from customers to bank and from one bank to another for both debit transfers and credit transfers.

d. Dates relevant to the funds transfer

28. One important source of confusion in international funds transfers has been the inconsistent use of terms to designate dates relevant to funds transfers. The following are the dates defined in the UNCITRAL Legal Guide and the definitions given there.

Entry date:

Date on which entries are made in the records of an account.

Interest date: Date on which the funds credited to an account begin to earn interest or funds debited to an account cease to earn interest.

Pay date: Date on which the funds are to be freely available to the transferee for withdrawal in cash.

29. In addition to these definitions ISO DIS/7982 also defines:

Value date: Date on which funds are to be freely available to the receiving bank.

30. The term "value date" was not defined in the UNCITRAL Legal Guide because it is also widely used in some countries to denote the date on which the funds are to be made available to the transferee (see "pay date") or the date on which the funds begin or cease to earn interest if credited or debited to an account (see "interest date").

B. General Provisions

31. Several general provisions that may well be desirable in the Model Rules are suggested in this section. The general provisions suggested are only for the purpose of establishing a possible framework for later consideration and additional ones may appear to be desirable as the work progresses.

II.2 Should the Model Rules contain a rule as to the effect of contracts on matters governed by the Rules?

32. No matter how detailed the Model Rules, or specific national legislation, might be, many questions arising in funds transfers are, and will continue to be, governed by contracts between banks and their customers, between banks and clearinghouses and between the banks themselves. The existence of these contracts raises several questions that might be considered in the Model Rules. The Model Rules might state to what extent the Model Rules themselves are intended to be mandatory (if adopted by a State) and to what extent they could be varied by contract.

33. Since contracts between banks and their customers are almost always prepared by the banks and, with rare exceptions involving large customers, the banks will not negotiate special terms with their customers, these contracts present a classic example of contracts of adhesion. The Model Rules might, therefore, provide for some means of ascertaining the fairness of the contract terms and the extent to which they would be enforceable. Such a means might be specific to the Model Rules or might partake of more general means of controlling contracts of adhesion.

34. The inter-bank funds transfer procedures are almost always the subject of bilateral or multilateral agreements, including agreements in the nature of clearinghouse rules. Under classical contract theory, these agreements bind only the parties to them and neither create rights in nor impose obligations on third parties. Nevertheless, to the extent these agreements establish the framework within which a customer's funds transfer instruction will be carried out, they have an important practical effect on those third parties. It might be considered, therefore, whether the Model Rules should provide to what extent such agreements would create rights in and impose obligations on third parties.

#### II.3 Should the Model Rules contain rules for their interpretation?

35. Rules of interpretation can be of several types. A standard provision in recent conventions on international trade law calls for regard to be given to the international character of the convention and the need to promote uniformity in its application. The Model Rules may provide a standard by which to interpret the intent of a party. Of particular relevance to funds transfers might be a rule that provides whether the amount expressed in words or the amount expressed in figures prevails when the two are not identical. A similar rule might indicate which is to prevail when the account to be debited or credited is indicated both by name and by number and they are not consistent.

#### II.4 Should the Model Rules contain provisions on conflict of laws?

36. The UNCITRAL Legal Guide, Issue 6, suggests that conflict of laws problems are serious in international funds transfer cases. The funds transfer may traverse banks in several countries, be in the currency of yet another country for the discharge of an obligation governed by the law of yet a third country. It is this transnational dimension of international funds transfers that calls for the preparation of these Model Rules with the aim of harmonizing the underlying law and banking practices.

37. In addition, agreement on conflict of laws rules would be helpful to determine which law was applicable to those matters not covered by the Model Rules. Such conflict of laws rules could be contained in the Model Rules themselves or they could be elaborated as a separate instrument by an appropriate international organization.



## III. OBLIGATIONS OF PARTIES

A. Form of the instruction

III.1 Should these Model Rules include a provision on the form and minimum content of a funds transfer instruction?

38. The most important element for the smooth operation of funds transfer systems is to establish clearly the rights and obligations of the parties. The issues relevant to the remedies for failure to fulfil those obligations are considered in chapter IV.

39. In addition to the obligations that would be provided by the Model Rules, further or more precise obligations may be required by the rules of a clearinghouse or other funds transfer system.

40. There is strict statutory regulation of the form and content of negotiable instruments, including cheques. This is at least in part because negotiable instruments create rights in the holder that may be greater than the rights of the transferor of the instrument to the holder. However, it may be thought that similar statutory regulation is not required for other types of funds transfer instructions that do not create such rights.

41. Nevertheless, a credit transfer from a customer cannot be carried out unless the transferor's instruction contains at least certain data elements, namely: (1) the amount to be transferred, including the designation of the currency where that is not self-evident, (2) the account to be debited, (3) the identification of the bank, including branch if necessary, where the account to be credited is located, and (4) the account to be credited. In addition, the instruction should be dated and should be authenticated in an adequate manner (see issue I.7). While all of these data elements may be in words on a paper-based funds transfer instruction, they may all be in figures or even in code in a funds transfer instruction in electronic form.

42. Other important information for the funds transfer process itself may include the date on which the transfer is to commence or the date on or by which the transferee's account is to be credited, in those cases when the transfer is not for immediate processing. In addition, there must be some means of identifying the transaction, which may be in the nature of a transaction sequence number or, in the case of a cash dispenser or point-of-sale transaction, an indication of the location of the machine or nature of the transaction. In some funds transfers the purpose of the funds transfer must be indicated, perhaps by reference to an invoice number.

43. Whether or not the Model Rules require certain data elements, the parties will agree to use prescribed formats for electronic funds transfers where the receiving bank is expected to process the instructions by computer. Inter-bank agreements may be in the form of adherence to the rules of a clearinghouse or telecommunications service. The format requirements might well include data elements that would not be required by the Model Rules.

III.2 Should the Model Rules require funds transfer instructions to be authenticated? If so, should they prescribe mandatory or acceptable forms of authentication? Should they state the consequences of following the form of authentication agreed for the type of instruction used?

44. Instructions sent by customers to banks and between banks can be expected to be authenticated. The authentication will usually be of the individual instruction but, where instructions are transmitted in batches, the authentication may relate to the entire batch. Authentication may be on paper, usually in the form of a signature or of a stamp or facsimile thereof, or it may be in electronic form suitable for the type of electronic system used. The form of authentication used in transmitting instructions from a customer to a bank, and the security features of that form of authentication, are usually established by the bank rather than by the customer. However, the customer may have a choice between different on-line or off-line technologies to deliver his funds transfer instructions with varying degrees of security, convenience and cost. Authentication requirements between banks are usually established by agreement or by the clearinghouse or transmission system used.

45. While it might be thought appropriate to require by law that instructions from customers and between banks be authenticated, it may be thought less appropriate for the form of the authentication to be stipulated, as signature has often been stipulated in the past, since there are so many possible means to authenticate an electronic funds transfer instruction and new means will evolve in the future. Consideration might be given as to whether it would be possible and appropriate to provide criteria by which to measure the adequacy of the form of authentication used. Yet another possibility would be to provide that each country might provide the types of authentication required or permitted, or the criteria by which to measure the adequacy of each type of authentication of electronic funds transfer instructions in use in that country.

46. The requirement, or use, of authentication raises the question of the consequences for sender and receiver of an instruction that appears to have been authenticated in the proper manner but which is, in fact, false. This aspect of the question is considered below.

47. For general discussion, see UNCITRAL Legal Guide, issue 12.

B. Obligations arising out of the funds transfer

III.3 Should the receiver of an instruction be obligated to act on a funds transfer instruction it has received?

48. The receivers of funds transfer instructions are always banks. These banks can be divided into three categories: transferor banks (i.e. the bank whose customer has initiated the funds transfer), intermediary banks (i.e. banks that have received an instruction from one bank and must pass on the instruction to another bank) and transferee banks. Senders of funds transfer instructions include transferors (and especially non-bank customers), transferor banks and intermediary banks.

49. Normally, there is a pre-existing agreement between the sender and the receiver that the receiver will act on instructions received by it. In some cases a sender may send an instruction to a bank with which it has no pre-existing agreement. However, in those cases there would still normally be some reason for the sender to expect the receiver to act on the instruction.

50. Where there is a pre-existing agreement that the receiver will act on the instruction, failure to do so would be a breach of contract. The question arises whether the receiver also has an obligation arising out of receipt of the instruction itself. A negative reply would mean that a bank that received an instruction from a source with which it had no previous agreement would be free to retain the instruction and neither act in conformity with it nor notify the sender that it would not do so. While this could be expected to be a relatively rare event, the determination as to the source of a bank's obligation to act on a funds transfer instruction it has received may be of particular importance in the case of an intermediary or transferee bank, since those banks are in direct privity of contract only with the bank sending them the instruction and not with the transferor.

III.4 If the Model Rules require a receiving bank to act on an instruction, what actions would be required?

51. In the case of a credit transfer the steps that might be followed by a receiving bank would be to

- verify the authentication of the instruction;
- verify the instruction for its formal completeness and that it contained no apparent errors;
- verify whether it was satisfied that it would receive reimbursement from the sender;
- debit the account of the sender and, where the account to be credited was at the same bank, credit that account;
- where the account to be credited was at a different bank, choose an appropriate means of sending the instruction to the bank, including an appropriate means of transmission and an appropriate intermediary bank if one was necessary, send to the intermediary bank or transferee bank its own funds transfer instruction that accurately transcribes the relevant data on the instruction it had received and the additional data necessary for re-transmission; and provide the means by which the bank to which this inter-bank instruction was sent would receive reimbursement for the amount of the instruction;
- notify the debit party of the debit, and when the receiving bank is the transferee bank, notify the transferee of the credit;
- notify the sender that the instruction will not be carried out, if that is the case, and the reason why it will not be carried out.

52. It might be considered whether the Model Rules should require that any or all of these actions should be taken or whether a general statement of obligation would be sufficient.

53. Verification of the authentication of the instruction would include examination of signature or of the electronic authentication used.

54. The receiving bank may be reimbursed in a number of ways. Some may be under its complete control, such as debiting the account of the sending party. In other cases settlement may be made through a clearinghouse or by receipt of credit from a reimbursing bank on the instruction of the sender. Whatever may be the means of reimbursement, the receiving bank can normally be expected to satisfy itself that it has been or will be reimbursed before it credits the account of its credit party and forwards a new funds transfer instruction, if one is required. In some countries receiving banks explicitly or implicitly satisfy themselves as to reimbursement in regard to most or all funds transfers before acting in a way to commit themselves. In other countries reimbursement for domestic funds transfers is sufficiently secure that no special action is necessary. Even in those countries, a bank would normally first satisfy itself as to reimbursement in respect of international funds transfers.

55. In some cases banks may act on an instruction by crediting an account, sending a new funds transfer instruction to another bank or taking other similar action prior to the time they are satisfied as to the arrangements for reimbursement. In such cases the question arises whether the bank does so at its own risk or whether it can reverse its actions in case of failure to be reimbursed.

56. In some electronic funds transfers, as in paper-based funds transfers, the receiving bank may forward the instruction it has received without change. Even then, some arrangement must exist for settlement of the second inter-bank transfer. In many electronic funds transfers a new instruction must be created with the receiving bank becoming the sending bank of that instruction. The new instruction will incorporate some, but not necessarily all, the data received and some of that data will be in a different field. For instance, the name of the receiving bank becomes the name of the sending bank. Some new data may be required. The bank as sending bank must create the new instruction accurately with all the necessary data.

57. Except in rare cases, neither the transferor nor the transferor bank can choose the transferee bank. However, there is often a choice of the means for sending the instruction to that bank, e.g. paper-based credit or debit transfer, exchange of magnetic tape, telex, data transmission. There may also be a choice of routes between the two banks and of means of reimbursing the transferee bank. Often the transferor either explicitly or implicitly chooses the means by which the instruction should be forwarded to the transferee bank, or is at least aware of the choice to be made by his bank. However, it is usually the transferor bank that chooses the routing and the means of reimbursing its receiving bank. This choice may be of significance to the transferor, not only for the costs involved, but also for such matters as the speed of transmission, the time of finality (and discharge of his obligation), and the security of transmission. The usual statement of legal rule,

formulated before there was such a wide choice of means of transmission with varying characteristics, is only that whenever a correspondent bank is required in order to complete the funds transfer, the bank must choose an appropriate correspondent bank.

58. A receiving bank's obligation to act may be satisfied by notifying the sending party that the bank will not carry out the instruction, thus permitting the sending party to take appropriate action. The notice may be expected to specify the reason why the instruction will not be carried out.

III.5 Should the Model Rules provide that the duty of the transferor bank is limited to performing certain specified acts as suggested above or should the duty of the transferor bank be to see that the transferor's instruction is carried out?

59. The extent of the duty of the transferor bank is of particular importance in international funds transfers and in domestic funds transfers in those domestic systems where a funds transfer may pass through several banks, communication systems or clearinghouses between the transferor bank and the transferee bank.

For general discussion, see UNCITRAL Legal Guide, issue 16.

III.6 Should the Model Rules provide whether and to what extent the responsibility of intermediary banks and transferee banks for properly carrying out their part in the funds transfer is to the bank that sent them the funds transfer instruction, to prior parties, especially the transferor, and, in the case of the transferee bank, to the transferee?

60. The extent of the obligation of intermediary and transferee banks to the transferor is linked to the extent of the obligation of the transferor bank to the transferor. If the transferor bank's obligation is limited to its own actions, intermediary and transferee banks must have a direct obligation to the transferor, even though they are not in direct privity of contract. Otherwise the transferor would have no right to recover from anyone for losses caused by an intermediary or transferee bank. The difference in rules on this point in different legal systems is a source of danger for many international funds transfers.

61. For general discussion of the situation of the transferee bank, see UNCITRAL Legal Guide, issue 17.

III.7 Should the Model Rules specify the occasions when the receiving bank would not be required to carry out the instruction?

62. Such occasions might include that

- the authentication could not be verified;
- the instruction appeared to have an error;
- the receiving bank was not satisfied with the reimbursement offered by the sender of the instruction.

63. Such occasions might also include exonerating events such as

- computer failure, transmission system failure, power failure or the like, when the causes of the failure were beyond the control of the bank, and the consequences of the failure could neither be avoided nor overcome;
- government action, such as the imposition of exchange controls.

64. Even though the receiving bank might be excused from carrying out the instruction for any of the reasons suggested, it might still have an obligation to the sender or to the transferor to notify the sender promptly that it would not or could not carry out the instruction, unless the impeding event also made notification impossible.

65. Since it can be predicted that computer failure, transmission system failure and power failure will occur, individual banks, funds transmission systems and the banking system as a whole might be expected to plan so as to minimize the likelihood of such failure and to avoid or overcome the consequences. Some of the planning involved is common to all types of computer and data transmission activities and includes such matters as redundancy of equipment, back-up files and disaster recovery plans. Other types of planning are specific to banking, such as the possibility of adjusting settlement deadlines under certain circumstances. It may be thought that in order to determine whether the computer failure, transmission system failure or power failure would constitute an exonerating event, it should be determined whether it could have been avoided or its consequences could have been avoided or overcome by proper planning in advance.

66. See also discussion in UNCITRAL Legal Guide, issue 19.

III.8 Should the Model Rules state the periods of time within which funds transfers must be implemented?

67. Although different types of electronic funds transfers require different periods of time for each bank involved to carry out its obligations and for the entire funds transfer to be completed, they share the common characteristic of being more reliable as to the amount of time necessary than are paper-based funds transfer systems. This very reliability has been an inducement for bank customers to change their behaviour in reliance on the ability of banks to make time-sensitive funds transfers as required. The most striking examples involve large international financings where the funds must be available in a particular account at a particular hour, but more routine examples are abundant where the payment of salaries or social security allotments is to be made on fixed days.

68. The period of time for the implementation of a funds transfer that is of interest to a bank customer is the time necessary for the transferee's account to be credited after the transferor has given the instruction to the transferor bank. If the Model Rules provide that the transferor bank should be responsible for performance of the entire funds transfer, a provision on the time within which the funds transfer should be completed might also be appropriate.

69. If the transferor bank is responsible only for its own actions, a provision on the period of time within which it must complete those actions or notify its sending party that it could not or would not act might be appropriate. A similar provision in respect of the intermediary banks and the transferee bank might also be appropriate. Furthermore, it might be appropriate to consider whether additional provisions would be necessary for those cases in which transferors have been informed of the time necessary to complete time-sensitive funds transfers and wish to indicate a pay date (i.e. when the credit is to be available to the transferee) on the instruction.

70. For additional discussion, see UNCITRAL Legal Guide, issue 23.

III.9 Should the Model Rules provide for the obligations of the sender of a funds transfer instruction?

71. The principal obligation of the sender is to reimburse the receiving bank at the time and in the manner agreed between them.

72. The sender must also give the receiving bank accurate information on its funds transfer instruction. If the instruction is incorrect as to amount, including currency, name of party or indication of account to be credited, including proper branch of transferee bank, the Model Rules might provide that the consequences of the error would fall on the sender, although the receiving bank may have an obligation to aid the sender in recovering the funds.

III.8 Should the Model Rules provide for the obligations of parties to the funds transfer process other than the banks?

73. Clearinghouses of various types and dedicated carriers of funds transfer instructions are an integral part of the funds transfer process. They are often owned by or operated for the benefit of the banking industry. It may seem appropriate to include in the Model Rules a statement of their obligations to sending and receiving banks and to transferors and transferees.

74. There are other carriers of funds transfer instructions that do not offer a dedicated service. They range from public carriers that offer telex or data transmission services to value added networks that offer funds transfer instruction capability with specified message formats and protocols as one of their services. Some of these carriers may also be considered to be such an integral part of the funds transfer process that they should be included within the scope of application of the Model Rules.

75. To the extent that the obligations of clearinghouses and carriers are not set forth in the Model Rules, it may seem appropriate to provide for the allocation between banks and customers for loss occasioned by such entities.

76. For additional discussion, see UNCITRAL Legal Guide, issue 18.

C. Obligations subsequent to the funds transfer

III.11 Should the Model Rules provide that banks are required to make a detailed statement available to their customers in respect of debits and credits to their accounts and the frequency of such statements?

77. There seems to be little doubt that banks have to be ready to give a statement to their customers as to the debits and credits entered to the account. The main questions relate to the form and frequency of the statement and whether the bank must send it to the customer or whether the customer must go to the bank for it. There are often different rules for commercial customers and for other customers. The increased volume of funds transfers during the last forty years and the even greater increase in value represented by funds transfers has led towards a greater frequency of the distribution of such statements.

78. These matters are governed by legal rules in some countries and by bank custom or by contract between the parties in others.

79. For general discussion, see UNCITRAL Legal Guide, issue 24.

III.12 Should the Model Rules provide that the bank's statement as to the debits and credits it has entered to the account is final if the customer does not object within some period of time? Should this period be shorter than the limitation period for beginning legal action? If so, about how long should it be and from what event should the time be measured?

80. The distribution of a statement of account activity to the customer allows the customer to reconcile his records with those of the bank. It may also be thought that the Model Rules should include a provision that the customer, having such an opportunity, must report discrepancies within some specified period of time. If this approach is taken, it may be of less importance whether the exact period of time within which discrepancies would have to be reported was uniform.

81. It might also be considered whether the customer's failure to report a discrepancy automatically made the statement binding on both bank and customer or whether the statement should be binding only to the extent that the other party had suffered loss as a result of the delayed notification.

82. For additional discussion, see UNCITRAL Legal Guide, issue 25. Issue 26 is also relevant.

IV. ERROR, FRAUD AND LIABILITY THEREFOR

- IV.1 Should the Model Rules specify the consequences and the procedures for rectifying an error when
- the amount of the funds transfer was credited to an account at the wrong branch or at the wrong bank;
  - the amount was credited to the wrong account at the correct bank;



- an insufficient amount was credited to the transferor's account;
- an excessive amount was credited to the transferor's account?

83. The error may have been made by the transferor, the transferor bank, an intermediary bank or the transferee bank. If an error by the transferor or the transferor bank leads to a debit to the transferor's account of an incorrect amount or the information given to identify the transaction shows the wrong account was credited, the transferor may be expected to know of the mistake and to require corrective action after notice of the debit has been received (see issue III.12). In all other cases, unless the transferor requests confirmation of the credit in all of its particulars, it will know a mistake has occurred only when the transferee complains that it has not received the amount due.

84. If a bank has made an error in amount, it should discover the error in reconciling its transactions. Reconciliation procedures available for electronic funds transfers make this process faster, easier and less expensive than for paper-based transfers. An error in the identification of the transferee bank or branch may be discovered by the bank or branch that receives the instruction but cannot find the account, but if the account is identified only by number and the only error is in the bank identification, the receiving bank or branch may credit an account without knowing it was not the correct account. In both cases the error will be found only as a result of a complaint by the transferee that it has not received the funds due or as a result of the notification given by the party incorrectly credited.

85. Issue V.5 raises the question as to when an underlying obligation is discharged by a funds transfer. A related question is what is the effect on the underlying obligation when the transferee's account is not credited as required or when it is credited for less than the full amount. The rule as to the effect on the underlying obligation may have implications for the obligations of the banks in rectifying the error.

86. In the majority of cases the existence of the error will be acknowledged and all parties will co-operate in rectifying it. In these cases, the only question is to determine who should bear the transaction charges and whether interest adjustments should be made.

87. Where an incorrect account is credited or the correct account is credited for too large an amount, the party credited may not be willing to have his account debited to rectify the error. It should be clear in the law that the money must be repaid, in court action if necessary. A more difficult question is whether the bank of the person who was credited incorrectly is authorized, or might be required, to debit the account without that person's consent when the fact of error is clear. The bank should not be expected to debit the account when there is dispute as to the propriety of the credit.

88. If the bank is not authorized, or chooses not, to debit the account to rectify the error, the Model Rules might specify whether the transferor must bear the consequences of the error even when made by a bank and must bring legal action against the party improperly credited or

whether the bank that made the error must take the action. This in turn will determine the mechanism for the inter-bank adjustments. There might be a difference in result if the error was made by the transferor bank, an intermediary bank or the transferee bank.

89. For additional discussion, see UNCITRAL Legal Guide, issue 41.

IV.2 Should the Model Rules contain provisions establishing the appropriate jurisdiction in case of litigation involving an international electronic funds transfer?

90. It is common for legal texts governing international transactions to contain legal rules on the appropriate jurisdiction in which to litigate disputes arising out of those rules.

91. In the case of funds transfers, the need for or the appropriateness of such rules might depend upon decisions made as to the substantive rules on responsibility. For example, if it was decided that a transferor bank was responsible for its own actions, so that the transferor would have to determine which bank caused the error and sue that bank for recovery, it might be thought appropriate to allow the transferor to sue in its own courts as well as in those where the problem occurred.

IV.3 Should the Model Rules specify rules establishing the burden of proof as to whether the transferor had authorized a funds transfer and as to whether it had been implemented as instructed?

93. For general discussion, see UNCITRAL Legal Guide, issues 21 and 22.

IV.4 Should the Model Rules provide that either the transferor or the transferee would be able to recover interest for a delay of a funds transfer?

94. For general discussion, see UNCITRAL Legal Guide, issue 27.

95. The draft inter-bank compensation rules for cases of delayed or incorrect funds transfers that are being prepared by the International Chamber of Commerce provide that the bank that has funds by error must pay interest to the other bank, even when the error was that of the bank that was out of funds.

IV.5 Should the Model Rules provide that either the transferor or the transferee could recover exchange losses for delay or non-performance of a funds transfer?

96. For general discussion, see UNCITRAL Legal Guide, issue 28.

97. Even if the Model Rules did not contain provisions covering exchange loss to the transferor or transferee, it might be appropriate for them to contain a provision establishing the date on which exchange rates should be calculated when an international funds transfer was not executed as planned, and the funds were returned to the transferor.

IV.6 Should the Model Rules provide that a bank might be liable for consequential damages for its failure to execute a funds transfer properly?

98. For general discussion, see UNCITRAL Legal Guide, issue 29.

IV.7 Should the Model Rules contain rules as to whether the transferor is responsible for some or all fraudulent activity of family members, employees, or third persons that cause a funds transfer instruction to be sent to the transferor bank?

99. This issue assumes that the existence and nature of the fraud have been established.

100. The fraud may be perpetrated by an employee in the course of employment. It may be perpetrated by an employee or other person who, because of his employment or relationship, learned the secret code (PIN or password) and had access to any device necessary to send funds transfer instructions. The fraud may have been caused by a third person with whom the transferor had no prior relationship. In the latter case there may have been varying degrees of negligence on the part of the transferor that contributed to the loss.

## V. FINALITY

V.I Should the Model Rules contain a single rule on the finality of a customer funds transfer that would govern a number of issues or should there be separate rules as regards the time when

- the debit to the transferor's account reduces, or the credit to the transferee's account increases, the amount against which attachment can be made or which falls within the transferor's estate in insolvency proceedings;
- death of the transferor, the termination of legal existence of a corporate entity or a similar event terminates the authority of the banks to act on the funds transfer instruction;
- the transferor loses the right to withdraw or to cancel the funds transfer instruction.

101. A single rule on "finality" is easier for banks to administer than are separate rules one each of the different issues. However, not all consequences usually associated with finality of a funds transfer can necessarily be accommodated by a single rule.

102. For general discussion, see UNCITRAL Legal Guide, issue 31.

V.2 On what event or point of time should the Model Rules consider a funds transfer to be final for some or all purposes suggested above?

103. The UNCITRAL Legal Guide, chapter IV, paragraphs 4 to 19 suggested a number of different points of time when a funds transfer might be considered to be final. Most of those events related to some action of the transferee bank in regard either to the funds transfer instruction or to the transferee's account.

104. One event that is commonly considered to indicate finality of a funds transfer is the entry of a debit or credit to an appropriate account. However, using electronic funds transfer techniques, and especially when entries are made by batch processing or are made to a provisional account, it may be difficult to determine when the entry was made. Therefore, if an entry of a debit or credit to an account is to constitute finality of a funds transfer or otherwise affect legal rights and obligations, consideration might be given to determining what constitutes entry of the debit or credit using different electronic funds transfer techniques.

105. There is a further question that is stimulated by the fact that actions of the banks that might be considered as making the funds transfer final, such as entry of a debit or credit to the account or the sending of a notice, may be taken by the bank in one order or another for its administrative convenience rather than for reasons related to the funds transfer itself. In particular, batch processed funds transfers may be processed the night before the entry date or during the night following the entry date. As a result there may be as much as a 24 hour difference in the time when different items might be processed and still bear the same entry date. Consideration might be given as to how such matters should affect the rules on finality.

106. For general discussion see UNCITRAL Legal Guide, issues 32, 39 and 40.

V.3 Should the Model Rules contain provisions on the time when a funds transfer between banks is final? Should any such provision be identical to or different from the time of finality of a customer's funds transfer? What should be the effect of finality of a funds transfer between two banks on the customer's funds transfer?

107. It may not be considered appropriate in all countries to make a distinction between finality of the funds transfer between banks and the finality of the funds transfer between the non-bank transferor and transferee. However, the distinction is maintained in many countries and is probably unavoidable in international funds transfers. What is less clear in most cases is the effect on the customer funds transfer, and the rights and obligations of the parties to it, of the finality of a funds transfer between any given pair of banks.

108. For general discussion, see UNCITRAL Legal Guide, issue 33.

V.4 Should the Model Rules contain provisions on the allocation of the risk of loss between the parties to a funds transfer that a bank will become insolvent prior to the settlement for the funds transfer?

109. In respect of the amount represented by the funds transfer, prior to the commencement of the funds transfer the transferor runs the risk that the transferor bank will become insolvent. After the funds transfer is final, the transferee runs the risk that the transferee bank will become insolvent. It is not clear who bears the risk that either of these banks or that one of the intermediary banks will become insolvent during the funds transfer and before settlement.

110. A funds transfer may be made by a chain of banks as follows:

Transferor →	Transferor →	Intermediary →	Intermediary →	Transferee →	Transferee
	Bank	Bank	Bank	Bank	
	A	B	C	D	

111. There are many possible situations if one of the banks becomes insolvent. Assume that Bank A debits the transferor's account and sends the instruction to Bank B. Settlement occurs by debit to the account Bank A holds with Bank B. Before Bank B sends the instruction to Bank C, it becomes insolvent. In this case the transferor has not paid the transferee but its account with Bank A has been debited. Similarly Bank A has settled with Bank B. Should Bank A be required to find another route to Bank D? Does the transferor or Bank A bear the risk of loss from Bank B's insolvency?

112. A different problem is posed when Bank D has credited the transferee's account before Bank B has settled with Bank C and before Bank C has settled with Bank D. If Bank C then becomes insolvent, should Bank B be required to settle with Bank C. Should Bank C be required to settle with Bank D in spite of Bank C's insolvency? Alternatively, should Bank B be required to settle directly with Bank D, thereby eliminating Bank C from the settlement chain?

113. Would the rule be different if Bank C's failure was that of settlement at the clearinghouse?

114. What should be the impact of such failure to settle on the funds transfer between the transferor and the transferee?

115. Whether or not it would be necessary for every country to have special rules on the allocation of the risk of loss arising out of the insolvency of a domestic bank, it may be thought that such rules would be of particular value for international funds transfers.

116. For general discussion, see UNCITRAL Legal Guide, issue 37.

V.5 Should the Model Rules contain a provision on the time when an underlying obligation is discharged?

117. In most countries the rules on discharge of an underlying obligation by funds transfer are not contained in the law governing the funds transfer. Instead, those rules are contained in the law governing the underlying obligation. Nevertheless, the two sets of rules should be in harmony. Therefore, without prejudice to any later decision should the Model Rules be transformed into a convention, model law or other form of binding legal norm, it may be thought appropriate to consider in the context of the Model Rules the appropriate time for discharge of an underlying obligation when payment is made by means of an electronic funds transfer.

118. For general discussion, see UNCITRAL Legal Guide, issue 36.

- I.4 Should the Model Rules apply only to funds transfers where accounts at banks are to be debited and credited or should they also apply where accounts at other financial institutions are to be debited and credited?

17. It may be thought that this issue need not to be addressed in the preparation of the Model Rules, even though it may be an important issue within any given country. The word "bank" could be used throughout the preparation of the Model Rules without prejudice to the definition that the word might be given at a later time or by users of the Model Rules.

18. It may be thought that the Model Rules should apply where the account of the transferor is to be debited but cash is to be paid to the transferee or where the transferor pays in cash to a bank for credit to the account of the transferee at the same or a different bank, but that the Model Rules should not apply where funds are paid in by the transferor and are to be paid in cash to the transferee.

- I.5 Should consumer electronic funds transfers be excluded from the scope of application of the Model Rules?

19. All types of electronic funds transfers, including those that might be classified as consumer transfers, were considered in the UNCITRAL Legal Guide. In most cases the legal issues in consumer and non-consumer funds transfers were found to be the same. In those cases where different legal issues arose, or in the more frequent cases where the same legal issues arose but a different legal rule might be envisaged for consumer funds transfers, this was pointed out. For that purpose it was not necessary to define what was a consumer funds transfer.

20. If consumer funds transfers were to be excluded from the scope of the Model Rules, a definition would have to be given. It could be based on the characterization of the transferor or of the transferee of the funds, e.g. a party who was neither characterized as a commercial party nor as an agency of the State might be considered to make consumer funds transfers, but it could not be based on the purpose of the funds transfer, as it was in the United Nations Convention on Contracts for the International Sale of Goods, where sales of goods for personal, family or household use were excluded. Other bases for distinguishing consumer funds transfers could be the amount of money involved (a generally unsatisfactory distinction) or the funds transfer technique used. It can be assumed, for example, that funds transfers executed by use of plastic card technology are, at the present time, normally consumer funds transfers while certain high-value systems are normally for non-consumer purposes.

21. However, while the current technology and its uses offer some means of distinguishing between consumer and non-consumer funds transfers, the distinction between the two is not inherent in the technology. It is possible that the plastic card technology will evolve in such a way that it will serve as the basis for most electronic funds transfer authentications, both consumer and non-consumer. Similarly, facilities that are currently used for high-value on-line funds transfer instructions may also be used for batch transmission of low-value funds transfer instructions. Therefore, the criteria for distinguishing between consumer and non-consumer funds transfers on the basis of the funds transfer technology utilized may be different in the future from what it might be today.