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Commission on
International
Trade Law**

YEARBOOK

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NOTE

Symbols of United Nations documents are composed of capital letters combined with figures. Mention of such a symbol indicates a reference to a United Nations document.

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INTRODUCTION

This is the thirteenth volume in the series of Yearbooks of the United Nations Commission on International Trade Law (UNCITRAL).¹ This volume covers the actions of the Commission and its subsidiary bodies from the end of the fourteenth session up to and including the fifteenth session and the actions of the United Nations Conference on Trade and Development (UNCTAD) and the General Assembly on the report of the fifteenth session.

The present volume consists of three parts. Part one contains the Commission's report on the work of its fifteenth session, which was held in New York, from 26 July to 6 August 1982, and the action thereon by the United Nations Conference on Trade and Development (UNCTAD) and by the General Assembly.

Part two reproduces most of the documents considered at the fifteenth session of the Commission. These documents include reports of the Commission's three Working Groups dealing respectively with international contract practices, international negotiable instruments and the new international economic order, as well as reports and notes by the Secretary-General and the Secretariat. Also included in this part are selected working papers which were before the Working Groups.

Part three contains recommendations to assist arbitral institutions and other interested bodies with regard to arbitrations under the UNCITRAL Arbitration Rules, and provisions on a universal unit of account for use in international transport and liability conventions, both of which were adopted at the fifteenth session of the Commission. Also included in this part are relevant resolutions of the General Assembly, a bibliography of recent writings related to the Commission's work, prepared by the Secretariat, and a check list of UNCITRAL documents.

¹ To date the following volumes of the *Yearbook of the United Nations Commission on International Trade Law* [abbreviated herein as *Yearbook* . . . (year)] have been published:

<i>Volume</i>	<i>Years covered</i>	<i>United Nations Publication, Sales No.</i>
I	1968-1970	E.71.V.1
II	1971	E.72.V.4
III	1972	E.73.V.6
IV	1973	E.74.V.3
V	1974	E.75.V.2
VI	1975	E.76.V.5
VII	1976	E.77.V.1
VIII	1977	E.78.V.7
IX	1978	E.80.V.8
X	1979	E.81.V.2
XI	1980	E.81.V.8
XII	1981	E.82.V.6

THE FIFTEENTH SESSION (1982)

A. Report of the United Nations Commission on International Trade Law on the work of its fifteenth session (New York, 26 July-6 August 1982) (A/37/17)*

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INTRODUCTION

1. The present report of the United Nations Commission on International Trade Law covers the Commission's

fifteenth session, held in New York from 26 July to 6 August 1982.

2. Pursuant to General Assembly resolution 2205 (XXI) of 17 December 1966, this report is submitted to the General Assembly and is also submitted for comments to the United Nations Conference on Trade and Development.

* Official Records of the General Assembly, Thirty-seventh session, Supplement No. 17 (A/37/17) (19 August 1982) and corrigenda 1 and 2 (English only) (hereinafter referred to as "Report"). The Report has also been issued as document A/CN.9/230 (24 August 1982) and corrigendum 1 (English only). The text of document A/CN.9/230 and Corr.1 (English only) which incorporated corrigenda

1 and 2 to A/37/17 and which corrected the minor errors, is reproduced here.

CHAPTER I. ORGANIZATION OF THE SESSION

A. Opening

3. The United Nations Commission on International Trade Law (UNCITRAL) commenced its fifteenth session on 26 July 1982. The session was opened on behalf of the Secretary-General by Mr. Erik Suy, the Legal Counsel.

B. Membership and attendance

4. General Assembly resolution 2205 (XXI) established the Commission with a membership of 29 States, elected by the Assembly. By resolution 3108 (XXVIII), the General Assembly increased the membership of the Commission from 29 to 36 States. The present members of the Commission, elected on 15 December 1976 and 9 November 1979, are the following States.¹ Australia,* Austria,* Burundi,* Chile,* Colombia,* Cuba,** Cyprus,** Czechoslovakia,** Egypt,* Finland,* France,* German Democratic Republic,* Germany, Federal Republic of,** Ghana,* Guatemala,** Hungary,** India,** Indonesia,* Iraq,** Italy,** Japan,* Kenya,** Nigeria,* Peru,** Philippines,** Senegal,** Sierra Leone,** Singapore,* Spain,** Trinidad and Tobago,** Uganda,** Union of Soviet Socialist Republics,* United Kingdom of Great Britain and Northern Ireland,* United Republic of Tanzania,* United States of America** and Yugoslavia.**

5. With the exception of Burundi, Cyprus and Senegal, all members of the Commission were represented at the session.

6. The session was also attended by observers from the following States: Argentina, Bahamas, Belgium, Bolivia, Brazil, Bulgaria, Burma, Canada, China, El Salvador, Ireland, Israel, Jamaica, Mexico, Netherlands, Paraguay, Portugal, Republic of Korea, Sri Lanka, Sudan, Suriname, Sweden, Switzerland, Turkey, Venezuela and Zambia.

7. The following United Nations organs, specialized agency, intergovernmental organizations and international non-governmental organizations were represented by observers:

(a) *United Nations organs*

United Nations Centre on Transnational Corporations, United Nations Conference on Trade and Development, United

Nations Industrial Development Organization and United Nations Institute for Training and Research.

(b) *Specialized agency*

International Monetary Fund.

(c) *Intergovernmental organizations*

Asian-African Legal Consultative Committee, Council of Europe, Hague Conference on Private International Law, Inter-American Commercial Arbitration Commission, International Institute for the Unification of Private Law and Organization of American States.

(d) *International non-governmental organizations*

International Air Transport Association, International Bar Association, International Chamber of Commerce, International Law Association and International Maritime Committee.

C. Election of officers

8. The Commission elected the following officers:²

Chairman Mr. R. Eyzaguirre (Chile)

Vice-Chairmen Mr. A. Duchek (Austria)

Mr. F. M. Sami (Iraq)

Mr. H. M. J. Smart (Sierra Leone)

Rapporteur Mr. F. Enderlein (German Democratic Republic)

D. Agenda

9. The agenda of the session, as adopted by the Commission at its 252nd meeting, on 26 July 1982, was as follows:

1. Opening of the session.
2. Election of officers.
3. Adoption of the agenda.
4. International contract practices.
5. International payments.
6. International commercial arbitration.
7. New international economic order: industrial contracts.
8. Co-ordination of work.
9. Status of conventions.
10. Training and assistance in the field of international trade law.
11. Most-favoured-nation clauses.
12. Future work.
13. Relevant General Assembly resolutions.³
14. Other business.
15. Adoption of the report of the Commission.

E. Decisions of the Commission

10. All the decisions taken by the Commission in the course of its fifteenth session were reached by consensus.

* Term of office expires on the day before the opening of the regular session of the Commission in 1983.

** Term of office expires on the day before the opening of the regular session of the Commission in 1986.

¹ Pursuant to General Assembly resolution 2205 (XXI), the members of the Commission are elected for a term of six years. Of the current membership, 17 were elected by the General Assembly at its thirty-first session on 15 December 1976 (decision 31/310) and 19 were elected by the General Assembly at its thirty-fourth session on 9 November 1979 (decision 34/308). Pursuant to resolution 31/99 of 15 December 1976 the term of those members elected by the General Assembly at its thirty-first session will expire on the last day prior to the opening of the sixteenth regular annual session of the Commission in 1983 while the term of those members elected by the General Assembly at its thirty-fourth session will expire on the last day prior to the opening of the nineteenth regular annual session of the Commission in 1986.

² The elections took place at the 252nd meeting, on 26 July 1982, and the 257th meeting, on 28 July 1982. In accordance with a decision taken by the Commission at its first session, the Commission has three Vice-Chairmen, so that together with the Chairman and Rapporteur, each of the five groups of States listed in General Assembly resolution 2205 (XXI), sect. II, para. 1, will be represented on the bureau of the Commission (see *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16* (A/7216), para. 14 (Yearbook . . . 1968-1970, part two, I, A)).

³ It was agreed that General Assembly resolution 36/107 would be discussed in conjunction with agenda item 7.

F. Adoption of the report

11. The Commission adopted the present report at its 268th meeting, on 6 August 1982.

CHAPTER II. INTERNATIONAL CONTRACT PRACTICES: UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES⁴

Introduction

12. At its twelfth session, the Commission requested its Working Group on International Contract Practices to consider the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.⁵ At its fourteenth session, the Commission considered the draft uniform rules proposed by the Working Group and requested the Secretary-General to incorporate in the rules such supplementary provisions as might be required if the rules were to take the form of a convention or a model law, to prepare a commentary on the rules, to prepare a questionnaire addressed to Governments and international organizations seeking to elicit their views on the most appropriate form for the rules and to circulate the rules to all Governments and interested international organizations for their comments, together with the commentary and the questionnaire.⁶

13. At its present session the Commission had before it the draft uniform rules with the required supplementary provisions and the commentary (A/CN.9/218),* together with an analysis of the responses of Governments and international organizations to the questionnaire and of their comments on the draft uniform rules (A/CN.9/219 and Add. 1).**

Discussion at the session⁷

Appropriate form for the rules

14. The Commission commenced its deliberations by considering whether the rules should be embodied in a con-

vention, a model law or in general conditions. There was general agreement that a convention provided the most effective form of unification. In opposition to a convention, it was noted that in recent years several conventions had not entered into force because a sufficient number of States had not adhered to them partly due to the fact that under the constitutions of some States the procedure to be followed for adhering to a convention was time-consuming and difficult. It was also noted that a convention was not as suitable as a model law for dealing with one aspect of the law of contract closely connected with other aspects not dealt with in the convention and that the considerable cost associated with the adoption of a convention might not be justified when only the unification of a limited area was accomplished. On the other hand, it was indicated that the cost of adopting the convention might not be so great if the convention were adopted by the General Assembly on the recommendation of the Sixth Committee, that is without convening a special conference.

15. The majority view supported the form of a model law. Such a law would be useful for countries, in particular for developing countries, in revising their law on the subject. When adopting a model law, a State was free to make minor modifications necessary for adapting it to the national legal system. In opposition to a model law, it was noted that States would be as slow to change their national laws by adopting a model law as to adhere to a convention and that in the past States had not frequently adopted model laws. Furthermore, the adoption of a model law rather than a convention by the Commission would communicate a lesser sense of the need for unification.

16. There was some support for the adoption of general conditions. Such general conditions would give parties some guidance in drafting their contracts. Furthermore, general conditions could be used as soon as they were finalized by the Commission and would accordingly come into use earlier than if one of the other forms were adopted. In opposition to general conditions, it was noted that they would be ineffective where they conflicted with mandatory national laws and that the structure of the uniform rules as currently drafted would need considerable change if the form of general conditions were to be adopted.

17. After deliberation, the Commission noted that the uniform rules might be cast in a form which might enable the rules to be used for several purposes. For instance, a convention might be drafted which contained a set of uniform rules in an annex. This was the form used in the Hague Convention relating to a Uniform Law on the International Sale of Goods of 1 July 1964 (Hague Convention of 1964), to which was annexed the Uniform Law on the International Sale of Goods, and in the Benelux Convention relating to the Penalty Clause of 26 November 1973, to which was annexed uniform rules regulating penalty clauses. States might adhere to the convention, thereby obligating themselves to adopt the uniform rules. In addition, the conven-

* Reproduced in this volume, part two, I, A.

** Reproduced in this volume, part two, I, B.

⁴ The Commission considered this subject at its 256th, 257th, 258th, 259th, 260th and 263rd meetings, on 28, 29 and 30 July and 2 August 1982.

⁵ Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 31 (Yearbook . . . 1979, part one, II, A).

⁶ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth session, Supplement No. 17* (A/36/17), para. 14 (Yearbook . . . 1981, part one, A).

⁷ For the summary records of the discussion, see A/CN.9/SR.256, 257, 258, 259 and 260.

tion may permit a reservation that the uniform rules were only to apply when the parties to a contract had chosen to apply the uniform rules to the contract (e.g. as in the Hague Convention of 1964, article V). Furthermore, States not adhering to the convention could use the uniform rules as a model law and parties to a contract could use the uniform rules as general conditions which they might incorporate in the contract. Accordingly, the Commission decided to examine the substance of the uniform rules and defer a decision on the form to be adopted.

Discussion of specific articles

18. The Commission discussed the definition in article A, paragraph 1, of the type of clause to be covered in the uniform rules and articles D, E, F and G. After its discussion, the Commission referred these articles to a drafting group for consideration in the light of the discussion.

Article A, paragraph 1

"1. This law applies to contracts in which the parties have agreed [in writing] that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) is entitled to recover, or to forfeit an agreed sum of money."

19. Opinion was divided as to maintaining the requirement that the agreement of the parties should be in writing. In support of maintaining the requirement, it was noted that writing facilitated proof of the clause and contributed to certainty as to its contents. Furthermore, certain legal systems required some types of contracts to be in writing. In opposition to the requirement, it was suggested that it should be left to the applicable law to determine if writing was to be required. Under some legal systems, the requirement of writing was a condition for the validity of the contract and since the uniform rules did not deal with the issue of validity it was unnecessary for the uniform rules to deal with this requirement. The prevailing view was that, if the form of a model law were adopted for the uniform rules, the issue should be left to be determined by the State adopting the law. If the form of a convention were adopted, the solution adopted in articles 11 and 95 of the Vienna Convention on Contracts for the International Sale of Goods, 1980,* should be adopted.

20. The Commission considered whether it was necessary to retain the word "agreed" in the phrase "agreed sum of money". It was suggested that the word was misleading, as it was not necessary for the parties to specify an exact sum in a liquidated damages or penalty clause. The prevailing view was that the word should be retained, but that

consideration should be given to clarifying that a clause in which the parties only specified a method of calculating the sum payable was covered by the uniform rules.

21. There was general agreement that the uniform rules should not apply where the contract provided that the agreed sum was to be claimed by the obligee from a bank under a bank guarantee to be opened at the instance of the obligor in favour of the obligee.

22. There was agreement that the definition covered both clauses which would be characterized as liquidated damages clauses and clauses which would be characterized as penalty clauses in the common law system. However, it was noted that in its present formulation the definition might cover some clauses which should fall outside the scope of the uniform rules (e.g. a clause which provided that the price in a sales contract was to be paid in advance, and the price would be recoverable if there was no delivery of goods), and it was agreed that the definition should be reformulated to exclude such cases.

23. It was agreed that while the word "forfeit" used in the English version of the uniform rules might bear the meanings assigned in the commentary to the rules (A/CN.9/218, paragraph 20) the meanings of the equivalent words used in the other language versions were unclear and should be clarified. The possibility of using other terminology in the English version which would avoid this problem should be considered. It was also agreed that in the proposed reformulation of the definition of clauses to be covered by the rules an attempt might be made to avoid the use of the words "recover, or to forfeit".

Article D

"Unless the parties have agreed otherwise, the obligee is not entitled to recover or to forfeit the agreed sum if the obligor is not liable for the failure of performance."

24. It was noted that drafting improvements might be needed to clarify some issues, such as the relationship between article D and article G, problems of the burden of proof where the obligor alleges that he is not liable for failure of performance, and the extent to which the parties might modify article D. It was suggested that the burden of proof should be defined in a clearer manner and that an obligor who relies on an absence of liability should prove it. Under another view the liability of the obligor including the burden of proof should be settled under the applicable law and the present formulation was adequate in that regard.

25. The suggestion was made to delete the opening words of article D enabling the parties to modify the provisions of the article and to deal in a separate provision with the issue of which articles parties were free to modify. The question was raised whether the parties should have the freedom to provide that the agreed sum was payable even in

* Yearbook . . . 1980, part three, I, B.

cases when the obligor was not liable for his failure of performance. In this connection it was suggested that the issue might be linked to a modification of article G. The court or arbitral tribunal might be authorized to reduce the agreed sum not only in cases where it was shown to be grossly disproportionate in relation to the loss suffered by the obligee, but also where the payment of the agreed sum might be considered manifestly unfair due to absence of liability of the obligor for failure of performance.

26. It was agreed that article D should be maintained in its present form and that a necessary modification should be made in article G to take care of the situation where the requirement of the payment was considered manifestly unfair. There was also general agreement that the power of the parties to modify the provision of the article set forth in its opening words should be contained in a separate article, which would also include the power to modify articles E and F.

Article E

"1. Where the agreed sum is to be recoverable or forfeited on delay in performance of the obligation, the obligee is entitled to both performance of the obligation and the agreed sum.

"2. Where the agreed sum is to be recoverable or forfeited on non-performance, or defective performance other than delay, the obligee is entitled either to performance, or to recover or forfeit the agreed sum, unless the agreed sum cannot reasonably be regarded as a substitute for performance.

"3. The rules set forth above shall not prejudice any contrary agreement made by the parties."

27. It was agreed that if, under this article, the obligee was entitled to performance, a court should not be bound to enter a judgement for specific performance unless the court would do so under its own law. Subject to the recognition that the above principle was applicable, and subject to possible drafting improvements, paragraph 1 of this article was considered acceptable.

28. There was general agreement that the proviso to paragraph 2 should form a separate sentence. It was noted that in this separate sentence the proviso could be cast in a positive form ("if the agreed sum could reasonably be regarded as a substitute for performance") and that additional wording was required to clarify the consequences when the proviso was not satisfied. Clarification might also be needed as to the allocation of the burden of proof.

29. The view was expressed that paragraph 2 of this article might be clarified by providing that, upon non-performance or defective performance, the obligee is entitled to the agreed sum; however, he would not be so entitled where performance had been effected, unless the agreed

sum could not reasonably be regarded as a substitute for performance. This view was opposed as the suggested formulation would deprive the obligee of an effective choice of remedies; his choice of the agreed sum could be negated by the obligor effecting performance.

30. The view was expressed that where the obligee elected for the remedy of performance, he should also be entitled to damages caused by the non-performance or defective performance. The question was raised as to the effects of termination of the contract on the remedies given under paragraph 2. It was also noted that, in view of the power given in paragraph 3 to the parties to modify the provisions of the article, the terms of the contract drafted by the parties would to a considerable extent affect the application of the article.

Article F

"Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or forfeited occurs, the obligee is entitled, in respect of the failure, to recover or forfeit the sum, and is entitled to damages to the extent of the loss not covered by the agreed sum, but only if he can prove that his loss grossly exceeds the agreed sum."

31. There was general agreement that the article need not repeat the description contained in article A of the type of clause covered by the uniform rules, but should only define the circumstances in which the obligee would be entitled to damages in addition to the agreed sum.

32. There was some support for the view that the obligee should only be entitled to the agreed sum, as this would enhance certainty as to the monetary rights and liabilities of the parties in case of failure of performance. There was greater support for the view that the article should be reformulated to provide that the obligee should only be entitled to the agreed sum unless the contract provided that he should be entitled to additional damages in defined circumstances. There was also some support for the view that the obligee should be entitled to additional damages only if such damages are due to the fault or gross negligence of the obligor. The prevailing view, however, was that the article as currently formulated represented an acceptable compromise.

33. There was support for the view that the present formulation should be amended to clarify that the obligee should only be entitled to damages if the applicable law gave him such a right.

Article G

"1. The agreed sum shall not be reduced by a court or arbitral tribunal.

"2. However, the agreed sum may be reduced if it is shown to be grossly disproportionate in relation to the loss that has been suffered by the obligee, and if the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee."

34. There was a view that the relationship of the rule prohibiting a reduction of the agreed sum in paragraph 1 of this article, and the rule permitting a reduction in paragraph 2, should be clarified. However, it was also noted that the present form of the article as a whole could be regarded as a compromise between the civil and common law systems.

35. While there was some support for retaining the two conditions to be satisfied under paragraph 2 before the agreed sum could be reduced, the prevailing view was that retaining the two conditions might unjustifiably restrict the power to reduce; the condition that the agreed sum could not reasonably be regarded as a genuine pre-estimate of the loss should be deleted.

36. It was noted that the present formulation of paragraph 2 appeared to give a discretion to reduce or not to reduce the agreed sum even when such sum was grossly disproportionate to the loss suffered, and it was suggested that reduction should be mandatory in such circumstances.

37. It was also noted that the rule should specify a measure delimiting the extent to which an agreed sum grossly disproportionate to the loss suffered should be reduced. Under another view, the extent of reduction should be left to the discretion of the court or arbitrator. A view was also expressed that the word "grossly" should be deleted from paragraph 2.

38. The modification of article G to enable reduction of the agreed sum when parties had, under article D, agreed that the obligee was entitled to such sum even when the obligor was not liable for his failure of performance was considered. There was support for the view that article G should be modified to enable reduction when the obligee's entitlement to the agreed sum was manifestly unfair.

39. There was general agreement that the provisions of the article could not be modified by the parties.

Decision of the Commission

40. The Drafting Group was of the view that it was unable to complete its work of preparing a revised text of the draft uniform rules in the time available. Accordingly it was decided that the Secretariat should submit a revised text for consideration by the Commission at its sixteenth session, taking into account the discussion at the present session and within the Drafting Group. A decision on the form to be adopted for the uniform rules could also be taken at that session.

CHAPTER III. INTERNATIONAL PAYMENTS

A. *Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques*⁸

Introduction

41. The Commission had before it the report of the Working Group on International Negotiable Instruments on the work of its eleventh session, held in New York from 3 to 14 August 1981 (A/CN.9/210).^{*} At that session, the Working Group adopted a draft Convention on International Bills of Exchange and International Promissory Notes and a draft Convention on International Cheques, after a Drafting Group had reviewed both drafts and established corresponding language versions (in Chinese, English, French, Russian and Spanish).

42. The Commission had before it the text of both draft Conventions (A/CN.9/211 and 212)^{**} and a commentary thereon (A/CN.9/213 and 214).^{***} Also before the Commission was a note by the Secretariat setting forth suggestions for possible future courses of action concerning these draft Conventions (A/CN.9/223).^{****}

Discussion at the session

43. The Commission expressed its appreciation to the Working Group and to its Chairman, Mr. René Roblot, for the successful completion of its work in the highly technical field of negotiable instruments law.

44. The Commission considered the possible future course of action concerning the two draft Conventions. While a number of suggestions were made as to which body should next review the draft texts, the Commission was agreed that it was premature to decide this question at the present session. It was felt that a final decision could be taken only after the comments by Governments on the draft Conventions had been received and an analytical compilation had been prepared by the Secretariat.

45. In view of the importance of these comments, it was deemed essential that the comments would be presented as complete as possible in the document to be prepared by the Secretariat. In order to facilitate the analytical compilation, the Secretary-General was requested to indicate in his note verbale the desirable structure and presentation of the comments. He was also asked to convey in the note verbale the expectation of the Commission that the comments would not merely contain specific observations and

^{*} Reproduced in this volume, part two, II, A, 1.

^{**} Reproduced in this volume, part two, II, A, 3 and 5.

^{***} Reproduced in this volume, part two, II, A, 4 and 6.

^{****} Reproduced in this volume, part two, II, A, 7.

⁸ The Commission considered this subject at its 265th and 266th meetings, on 3 and 4 August 1982.

suggestions on individual draft articles but also provide some indication of a Government's general attitude towards the draft Conventions, including their acceptability and possible form.

46. In this connection, it was noted that, due to delays in translation, the commentary on the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/213) would not be received by all Governments and interested international organizations until early in August and the commentary on the draft Convention on International Cheques probably early in September 1982. In view of this situation, it was agreed that the period for submission of comments indicated in the Secretary-General's note verbale of 14 July 1982 (i.e. until 15 February 1983) should be extended. This was deemed necessary in order to give Governments sufficient time for eliciting the views of interested groups, in particular banking circles. It was also noted that in particular the Arabic version of the draft Conventions needed improvement as to the legal terms used therein.

47. Different views were expressed as to the time schedule for the submission of comments and for the final decision of the Commission on the future course of action. Under one view, the deadline for submission of comments should be extended until 31 March 1983 and the Commission should decide on the future course of action at its sixteenth session. In order to expedite matters, the further suggestion was made that between the Commission's sixteenth and seventeenth sessions the Working Group, possibly enlarged to include all member States of the Commission, should review the draft Conventions in the light of the comments.

48. The prevailing view, however, was to extend the period for submission of comments even further, e.g. until 30 September 1983, and to take a final decision on the future course of action at the seventeenth session of the Commission in 1984. It was felt that this time schedule provided the necessary time for Governments and organizations to ascertain the views of relevant circles and also for the Secretariat to prepare a detailed analytical compilation of the comments well in advance of the seventeenth session.

49. The Commission, after deliberation, adopted this latter view. However, it also decided to place this item on the agenda of its sixteenth session to allow for possible discussion in case pertinent information would then be available.

Decision of the Commission

50. At its 266th meeting, on 4 August 1982, the Commission adopted the following decision:

The United Nations Commission on International Trade Law

1. Expresses its appreciation to the Working Group

on International Negotiable Instruments for the successful completion of its work on the preparation of a draft Convention on International Bills of Exchange and International Promissory Notes and of a draft Convention on International Cheques;

2. Requests the Secretary-General to inform all Governments and interested international organizations that they may submit their comments on these draft texts until 30 September 1983, and to provide some indication as to the desirable structure and presentation of these comments;

3. Requests the Secretary-General to prepare a detailed analytical compilation of these comments and to distribute it well in advance of the seventeenth session of the Commission to be held in 1984;

4. Decides to postpone its final decision on the future course of action to its seventeenth session;

5. Decides to place this item on the agenda of its sixteenth session to allow for possible discussion in case pertinent information would then be available.

B. Universal unit of account for international conventions⁹

Introduction

51. The Commission at its eleventh session decided to study the establishment of a universal unit of account of constant value which would serve as a point of reference in international transport and liability conventions for expressing amounts in monetary terms.¹⁰ At its fourteenth session, the Commission considered a report of the Secretary-General on the subject and decided to refer the matter to the Working Group on International Negotiable Instruments.¹¹

52. The Working Group, at its twelfth session held at Vienna from 4 to 12 January 1982, recommended that a draft article be prepared for use in international conventions, which would designate the Special Drawing Right of the International Monetary Fund (SDR) as the unit of account for limitation of liability provisions.¹² It also drafted a sample text for revising the limit of liability through use of a price index and a sample text for an expedited procedure for revising limits of liability in international conventions.¹³

⁹ The Commission considered this subject at its 254th, 255th and 256th meetings, on 27 and 28 July 1982.

¹⁰ Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17* (A/33/17), para. 67 (Yearbook ... 1978, part one, II, A).

¹¹ *Ibid.*, Thirty-sixth Session, Supplement No. 17 (A/36/17), para. 32 (Yearbook ... 1981, part one, A).

¹² A/CN.9/215, para. 97 (reproduced in this volume, part two, II, B, 1).

¹³ *Ibid.*, paras. 54 and 90.

Discussion at the session¹⁴

Universal unit of account

53. There was general agreement in the Commission that a preferred unit of account for international transport and liability conventions, particularly those for global application, should be the SDR and that the Commission should prepare a text for such a provision as recommended by the Working Group.

54. It was recognized that some States which were not members of the International Monetary Fund might not be able to accept the use of the SDR as a unit of account. However, it was pointed out that any universal unit of account provision prepared by the Commission would not be mandatory but would serve as the preferred model for use by a diplomatic conference preparing or revising a convention of the type in question. Particularly if the diplomatic conference were of the judgement that the limit of liability should also be expressed in "monetary units" measured in a fixed quantity of gold for those States which were not members of the International Monetary Fund, it might adopt a provision based upon the full text of article 26 of the Hamburg Rules.

55. The Commission decided that, in conformity with the recommendation of the Working Group, the universal unit of account provision would be substantially in the form of article 26, paragraph 1, of the Hamburg Rules and of paragraph 4 as modified to the extent necessary by the deletion of paragraphs 2 and 3, both of which refer to the use of a "monetary unit".

Adjustment of the limit of liability

56. The Commission was in agreement that the problems caused by the effects of changes in monetary values on the limits of liability were serious. It was noted that a limit of liability which remained fixed over a long period of time often became seriously eroded. It was also noted that in some cases when a convention containing a limit of liability provision did not come into force fairly promptly, States might later hesitate to ratify the convention because the limit of liability would have become too low through the effects of inflation.

57. There was a general discussion as to the best method for adjusting the limit of liability so as to continue to reflect the original balance of the convention. On the one hand it was suggested that the use of a proper price index would permit an automatic adjustment of the limit of liability. On the other hand it was suggested that the use of an index would itself contribute to inflation by increasing the limit of liability, and therefore the cost to the carrier or other party held liable, as a result of past price increases reflected

in the index. It was pointed out that some States would not ratify any convention which contained an index provision. Furthermore, it was suggested that if an indexing provision was adopted, the adjustment of the limit of liability should occur only at intervals of sufficient duration so as to assure that the limit of liability would be stable.

58. Nevertheless, it was noted, there might be conventions for which an indexing provision would be the most appropriate and, therefore, the Commission should adopt a sample price index provision for optional use by any diplomatic conference which might wish to incorporate such a provision in a convention.

59. It was noted that the expedited revision procedure drafted by the Working Group was based in large measure on the procedure in the 1980 Convention concerning International Transport by Rail (COTIF). It was noted that this procedure assured that all States Party to a convention containing such a provision would be bound by the same limit of liability since paragraph 5 of the provision required any State which could not accept a new limit of liability adopted under the provision to denounce the convention. On the other hand it was stated that this requirement might raise problems relating to the principle of the sovereignty of States.

60. There was agreement that the Commission should adopt the indexing provision and the expedited revision procedure provision as two alternative means for adjustment of the limit of liability as recommended by the Working Group.

61. It was suggested that the attention of any diplomatic conference intending to use the sample price index provision as the means of adjusting the limit of liability be drawn to the need for determining the institution to be charged with preparing the index, revising it when appropriate, calculating the index figure at the agreed-upon dates and notifying the depositary of the result.

62. However, one delegation stated that it was not prepared at the present stage to determine its position with regard to adjusting limits of liability since this problem was still being considered by competent bodies of the country concerned.

63. At its 256th meeting, on 28 July 1982, the Commission adopted the following decision:

The United Nations Commission on International Trade Law

Recognizing that many international transport and liability conventions of both a global and a regional character contain limitation of liability provisions, wherein the limitation of liability is expressed in a unit of account,

Noting that the limitation of liability as fixed in these conventions may become seriously affected over time by

¹⁴ For the summary records of the discussion, see (A/CN.9/ SR.254, 255 and 256.

changes in monetary values, thereby destroying the intended balance of the convention as adopted,

Believing that a preferred unit of account for many conventions, particularly for those of global application, would be the Special Drawing Right as determined by the International Monetary Fund,

Being of the opinion that the conventions should in any event contain a provision which would facilitate the adjustment of the limit of liability to changes in monetary values,

1. *Adopts* the unit of account provision and the two alternative provisions for the adjustment of the limit of liability in international transport and liability conventions as contained in the annexes to the present decision;

2. *Recommends* that in the preparation of future international conventions containing limitation of liability provisions or in the revision of existing conventions the unit of account provision as adopted by the Commission should be used;

3. *Recommends further* that in such conventions one of the two alternative provisions for adjustment of the limitation of liability as adopted by the Commission should be used;

4. *Suggests* that, when the sample price index provision is to be used in such a convention, consideration be given to the nature of the intended price index and the institution to be charged with its preparation, revision and calculation;

5. *Requests* the General Assembly to recommend the use of these provisions in the preparation of future international conventions containing limitation of liability provisions or in the revision of existing conventions.

*Annex I**

Universal unit of account

1. The unit of account referred to in article [] of this Convention is the Special Drawing Right as defined by the International Monetary Fund. The amounts mentioned in article [] are to be expressed in the national currency of a State according to the value of such currency at the date of judgement or the date agreed upon by the parties. The equivalence between the national currency of a Contracting State which is a member of the International Monetary Fund and the Special Drawing Right is to be calculated in accordance with the method of valuation applied by the International Monetary Fund in effect at the date in question for its operations and transactions. The equivalence between the national currency of a Contracting State which is not a member of the International Monetary Fund and the Special Drawing Right is to be calculated in a manner determined by that State.

2. The calculation mentioned in the last sentence of paragraph 1 is to be made in such a manner as to express in the national currency

* In the English text of the Report (as it appeared in documents A/37/17 and A/CN.9/230), the third sentence in Annex I, paragraph 1, was erroneously omitted. Documents A/37/17/Corr.2 (English only) and A/CN.9/230/Corr.1 (English only) corrected the omission and are incorporated here.

of the Contracting State as far as possible the same real value for amounts in article [] as is expressed there in units of account. Contracting States must communicate to the Depositary the manner of calculation at the time of signature or when depositing their instrument of ratification, acceptance, approval or accession and whenever there is a change in the manner of such calculation.

Annex II

Sample price index

1. The amounts set forth in article [] shall be linked to [a specific price index which might be considered appropriate for a particular convention]. On coming into force of this [Protocol-Conven-], the amounts set forth in article [] shall be adjusted by an amount, rounded to the nearest whole number, corresponding in percentage to the increase or decrease in the index for the year ending on the last day of December prior to which this [Protocol-Conven-] came into force over its level for the year ending on the last day of December [of the year in which the Protocol or Convention was opened for signature]. Thereafter, they shall be adjusted on the first day of July of each year by an amount, rounded to the nearest whole number, corresponding in percentage to the increase or decrease in the level in the index for the year ending on the last day of the previous December over its level for the prior year.

2. The amounts set forth in article [] shall not, however, be increased or decreased if the increase or decrease in the index does not exceed [] per cent. Where no adjustment was made in the previous year because the change was less than [] per cent, the comparison shall be made with the level for the last year on the basis of which an adjustment was made.

3. By the first day of April of each year the Depositary shall notify each Contracting State and each State which has signed the [Protocol-Conven-] of the amounts to be in force as of the first day of July following. Changes in the amounts shall be registered with the Secretariat of the United Nations in accordance with General Assembly regulations to give effect to Article 102 of the Charter of the United Nations.

Annex III

Sample amendment procedure for limit of liability

1. The Depositary shall convene a meeting of a Committee composed of a representative from each Contracting State to consider increasing or decreasing the amounts in article []:

(a) Upon the request of at least [] Contracting States, or

(b) When five years have passed since the [Protocol-Conven-] was opened for signature or since the Committee last met.

2. If the present [Protocol-Conven-] comes into force more than five years after it was opened for signature, the Depositary shall convene a meeting of the Committee within the first year after it comes into force.

3. Amendments shall be adopted by the Committee by a [] majority of its members present and voting.^a

4. Any amendment adopted in accordance with paragraph 3 of this article shall be notified by the Depositary to all Contracting States. The amendment shall be deemed to have been accepted at the end of a period of [6] months after it has been notified, unless within that period not less than [one-third] of the States that were Contracting States at the time of the adoption of the amendment by the Committee have communicated to the Depositary that they do not accept the amendment. An amendment deemed to have been accepted in accordance with this paragraph shall enter into force for all Contracting States [12] months after its acceptance.

^a The Conference of Plenipotentiaries may wish to insert a list of criteria to be taken into account by the Committee.

5. A Contracting State which has not accepted an amendment shall nevertheless be bound by it, unless such State denounces the present Convention at least one month before the amendment has entered into force. Such denunciation shall take effect when the amendment enters into force.

6. When an amendment has been adopted by the Committee but the [6] month period for its acceptance has not yet expired, a State which becomes a Contracting State to this Convention during that period shall be bound by the amendment if it comes into force. A State which becomes a Contracting State to this Convention after that period shall be bound by any amendment which has been accepted in accordance with paragraph 4.

C. *Electronic funds transfer*¹⁵

Introduction

64. The Commission, at its eleventh session, included as an item in its programme of work the legal problems arising out of electronic funds transfers. At its twelfth session the Commission, recognizing the complex technical aspects of the subject, requested the Secretariat to continue the preparatory work on this subject within this framework of the UNCITRAL Study Group on International Payments, a consultative body composed of representatives of banking and trade institutions.

65. The Commission had before it at this session a report of the Secretary-General (A/CN.9/221)* which described some of the legal problems arising in this field and contained the recommendations of the Study Group as to the future work which the Commission might undertake.

66. As examples of the legal problems arising out of the payment process, the report discussed the question as to when payment becomes final and the liability for loss caused by delayed or incorrect payment instructions. As an example of the legal problems arising out of the electronic nature of the communication and record-keeping, the report discussed the legal value of computer records.

67. The report concluded that as to the legal problems associated with the payment process, it would seem to be premature to attempt to unify the law in respect of electronic funds transfers. What seemed to be needed at this stage of development was a guide to the legal problems arising out of electronic funds transfers which would identify the legal issues, describe the various approaches, point out the advantages and disadvantages of each approach and suggest alternative solutions.

68. As to the legal value of computer records, a problem which goes beyond electronic funds transfers and concerns all aspects of international trade in which computers might be used, the report suggested that guidelines might be developed so as to assure that records which had been created

and stored in one State in a manner which made them acceptable as evidence in the courts and arbitral tribunals of that State would be acceptable as evidence in the courts and arbitral tribunals of other States in which a legal dispute might arise.

Discussion at the session

69. There was general agreement in the Commission that the preparation of a guide on the legal problems arising in electronic funds transfers should be undertaken. It was pointed out that at the present time in many States these transfers took place in a total or partial legal vacuum and that there was no agreement on the governing rules for international electronic funds transfers. It was also suggested that the problems would soon become more important for developing countries with their increased participation in domestic and international funds transfers.

70. It was suggested that the legal guide would serve largely as an inventory of legal problems to be solved in the future. Several representatives expressed the view that the guide might show areas in which the Commission could in the future prepare uniform rules. It was suggested that such uniform rules might be in the nature of a model law, which would be of particular value to the developing countries, or might concentrate on certain aspects of international electronic funds transfers.

71. As to the suggestion that guidelines be prepared on the legal value of computer records, under one view the legal rules as to evidence were so closely linked to the rest of the procedural and substantive law of a State that it would be difficult to develop even general guidelines. In this respect were mentioned the difficulties encountered in the Council of Europe on this subject, even though the regional nature of that organization reduced the disparity of approaches to be reconciled from those which would have to be reconciled by a world-wide organization such as the Commission.

72. Under another view the matter was of importance and should be undertaken by the Commission even though it might be given a lower priority than the preparation of the legal guide. It was also suggested that as a first step the subject of the legal value of computer records in the context of electronic funds transfers might be one of the subjects to be considered in the legal guide, thereby helping to prepare any future action the Commission might take on this subject.

Decision of the Commission

73. The Commission decided that the Secretariat should begin the preparation of a legal guide on electronic funds transfers, in co-operation with the UNCITRAL Study Group on International Payments. In carrying out this project the Secretariat was urged to take appropriate steps to ascertain banking practice as well as the applicable legal rules from

* Reproduced in this volume, part two, II, C.

¹⁵ The Commission considered this subject at its 256th meeting, on 27 July 1982.

all regions of the world, including the circulation of a questionnaire if it were deemed advisable. In this connection it was suggested that the Study Group should be enlarged to assure adequate representation from the developing countries. The Secretariat was also requested to submit to some future session of the Commission a report on the legal value of computer records in general.

CHAPTER IV. INTERNATIONAL COMMERCIAL ARBITRATION

A. *UNCITRAL Arbitration Rules: administrative guidelines*¹⁶

Introduction

74. The Commission, at its fourteenth session, decided that it would be desirable to issue guidelines, in the form of recommendations, to arbitral institutions and other relevant bodies to assist them in adopting procedures for acting as appointing authority or for providing administrative services in cases to be conducted under the UNCITRAL Arbitration Rules.¹⁷ It also requested the Secretary-General to prepare a revised text of the draft guidelines which had been submitted to the Commission at its thirteenth session, and any explanations thereof, for submission to the fifteenth session of the Commission.

75. The Commission, at its present session, had before it a note by the Secretary-General, prepared pursuant to that decision. This note, contained in document A/CN.9/222,* sets forth in an annex the revised draft "Recommendations concerning administrative services provided in arbitrations under the UNCITRAL Arbitration Rules".

Discussion at the session

76. The Commission, after deliberation, was agreed that the revised draft, in general, reflected the views expressed during the fourteenth session and that it was in large part acceptable, in particular the section entitled "Possible contents of administrative procedures" (paragraphs 14-33). As regards the preceding paragraphs, a number of suggestions and reservations were made.

77. One such proposal was, for example, to express in the title of the recommendations more clearly that they related not only to the providing of administrative services of a technical nature but also to the performing of the functions of an appointing authority under the UNCITRAL

Arbitration Rules. Various other suggestions aimed at a clearer distinction between those cases where an arbitral institution adopted the UNCITRAL Arbitration Rules as its own institutional rules and those cases where an institution acted as appointing authority or provided administrative services in an *ad hoc* arbitration under the UNCITRAL Arbitration Rules.

78. Under one view, only this latter situation should be dealt with in the recommendations. Under another view, however, the first situation should also be covered to the extent that an institution did not merely use the UNCITRAL Arbitration Rules as a model in preparing its own institutional rules with no indication of their source, a practice which did not raise the kind of problems which had led to the preparation of the recommendations, but instead announced that it had adopted the UNCITRAL Arbitration Rules as its own institutional rules. In support of this view it was pointed out that also in these cases the recommendations could serve the purpose of inviting institutions to consider the various options available for using the UNCITRAL Arbitration Rules and to meet the parties' needs for certainty as to what procedures to expect.

79. As regards this latter aspect, different views were expressed as to whether the recommendations should call upon institutions, when adopting the UNCITRAL Arbitration Rules, not to modify these Rules. Under one view, any arbitral institution should be free to modify the Rules according to its particular needs. Under another view, no such modifications should be made, in order to avoid disparity in the application of the UNCITRAL Arbitration Rules by different institutions. The prevailing view, however, was that the approach taken in the draft recommendations (paragraphs 8-10) constituted an acceptable compromise.

80. As regards the nature of the recommendations, the Commission was agreed that they were in no way regulatory or binding but merely intended to provide information and assistance to arbitral institutions and other interested bodies. The Commission was also agreed that the recommendations should not be accorded a formal status like other texts elaborated by it such as the UNCITRAL Arbitration Rules themselves. The view was expressed that, instead, the Secretariat could be requested to transmit the recommendations in the name of the Secretary-General, under his general mandate to assist in the interpretation and application of the UNCITRAL Arbitration Rules and to promote their use.

81. Different views were expressed as to which channels of communication should be used for the distribution of the recommendations. Under one view, copies of the recommendations should be transmitted only to Governments, inviting them to forward the recommendations to all interested and relevant bodies in their respective countries. Under another view, the recommendations should be transmitted directly to all arbitral institutions and similar interested bodies known to the Secretariat. There was wide

* Reproduced in this volume, part two, III, C.

¹⁶ The Commission considered this subject at its 253rd, 254th and 266th meetings, on 26 and 27 July and 4 August 1982.

¹⁷ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 59 (Yearbook . . . 1981, part one, A).

support, however, for using both of these channels of communication.

82. The Commission concluded that it was desirable to finalize the text of the recommendations during the course of its present session. It, therefore, requested the Secretariat to redraft the recommendations taking into account the suggestions made during the discussion and to submit the revised draft for its consideration before the closure of the present session.

83. The Commission considered a revised draft text of the recommendations contained in document A/CN.9/222. It was agreed that this revised draft text reflected the views expressed during the discussion of those recommendations.

84. The Commission was agreed that the revised text was acceptable, subject to the following amendment. After paragraph 17 of the annex of A/CN.9/222 which set forth a model clause, the following paragraph should be added:

"In view of the considerations and concerns expressed above in paragraphs 12 and 15, if the administrative procedures of the institution are such as to lead to a modification in substance of the UNCITRAL Arbitration Rules, it may be advisable that this modification be reflected in the model clause."

85. The Commission requested the Secretary-General to transmit these recommendations to Governments and to arbitral institutions and other interested bodies such as chambers of commerce.¹⁸

B. Model arbitration law¹⁹

86. The Commission, at its fourteenth session, decided to proceed with work towards the preparation of a draft model law on international commercial arbitration, and to entrust this work to the Working Group on International Contract Practices.²⁰

87. The Working Group commenced this work at its third session, held in New York from 16 to 26 February 1982. The Commission, at its present session, had before it the report of the Working Group on the work of that session (A/CN.9/216).*

88. The Commission took note of the report of the Working Group on the work of its third session and expressed its appreciation to the Chairman of the Working Group, Mr. Iván Szasz. It noted that the Working Group had discussed all but three questions set forth in a working paper prepared by the Secretariat (A/CN.9/WG.II/WP.35).** It

was understood that the list of issues dealt with in that working paper, to which the Working Group had added some more issues to be possibly included in the model law, was not to be regarded as exhaustive but that the Working Group should be open to any further suggestions for inclusion of yet other issues. It was suggested in particular that the Working Group should consider such issues as the relevance of limitation of actions in the context of arbitration proceedings and the time period during which arbitral awards would be enforceable.

89. The Commission requested the Working Group to proceed with its work expeditiously.

CHAPTER V. NEW INTERNATIONAL ECONOMIC ORDER²¹

A. *Clauses related to contracts for the supply and construction of large industrial works*

Introduction

90. The Commission had before it the report of the Working Group on the New International Economic Order on the work of its third session, held in New York from 12 to 23 July 1982 (A/CN.9/217).* The report sets forth the deliberations of the Working Group on the basis of the studies by the Secretary-General entitled "Clauses related to contracts for the supply and construction of large industrial works" (A/CN.9/WG.V/WP.4 and Add. 1-8, hereinafter referred to as Study I** and A/CN.9/WG.V/WP.7 and Add. 1-6, hereinafter referred to as Study II).***

91. The report noted that the Working Group had concluded the discussion of those topics in Study I which had not been considered at the second session of the Working Group, and had also completed its discussion of Study II.

92. There was general agreement in the Working Group that the Secretariat should now commence the drafting of the legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works which the Commission, at its fourteenth session, had decided to undertake.²² The Working Group requested the Secretariat to submit a few sample draft chapters and an outline of the structure of the guide to its next session.

* Reproduced in this volume, part two, III, A.

** Reproduced in this volume, part two, III, B.

¹⁸ The complete text of the recommendations is reproduced in annex I to this report.

¹⁹ The Commission considered this subject at its 253rd meeting, on 26 July 1982.

²⁰ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 70 (Yearbook . . . 1981, part one, A).

* Reproduced in this volume, part two, IV, A.

** Yearbook . . . 1981, part two, IV, B, 1.

*** Reproduced in this volume, part two, IV, B.

²¹ The Commission considered this subject at its 267th meeting, on 4 August 1982.

²² Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 84 (Yearbook . . . 1981, part one, A).

Discussion at the session

93. The Commission expressed its appreciation to the Working Group and to its Chairman, Mr. Leif Sevón, for the expeditious manner in which the work had been conducted and for the conclusion of the consideration of the two studies prepared by the Secretariat. The report of the Working Group was approved by the Commission.

94. It was suggested that the legal guide should deal with the legal problems between the parties to the contract arising out of the failure of a Government to grant an import or export licence, the withdrawal of such a licence or out of other governmental restrictions which caused one of the parties not to be able to perform the contract as agreed. It was noted, however, that certain aspects of this issue were already covered in the Studies.

95. A view was expressed that it would be advisable to clarify in the legal guide the importance of the choice of the applicable law by the parties and to include therein a model clause in this connection.

96. A suggestion was made that the legal guide should recommend that, in case of the use of cost-reimbursable contracts, at least a preliminary estimate of the cost of the works should be indicated in the contract.

97. There was general support that the next session of the Working Group should be held at Vienna during the week immediately preceding the next session of the Commission, as suggested by the Working Group.

CHAPTER VI. CO-ORDINATION OF WORK

A. *Activities of other organizations in the field of international trade law: transport documents*²³*Introduction*

101. The General Assembly, in resolution 34/142, requested the Secretary-General to place before the Commission at each of its sessions a report on the activities of other organs and international organizations related to international trade law together with recommendations as to steps to be taken by the Commission.

102. The Commission, at its fourteenth session, decided that, to further strengthen the co-ordinating role of the Commission, the Secretariat should select a particular area of international trade law for consideration and submit a report on the work of other organizations in that area.²⁴ The subject of international transport documents was chosen for the report submitted to the present session of the Commission (A/CN.9/225).*

103. The report discussed the legal regime governing transport documentation requirements under the principal multilateral conventions and some of the current developments in this field. The report concluded that there may be a greater need in the future than there has been in the past for harmonization of the rules governing such transport documentation.

Discussion at the session

104. There was general agreement that the report was a useful means for the Commission to fulfil its role of co-ordination in the field of international trade law. Although the report did not suggest any specific action which the Commission might take at the present time, it demonstrated the need for co-ordination in this field. The suggestion contained in the report that the Secretariat would continue to monitor developments in this field was welcomed and the Secretariat was requested to keep the Commission informed of any future course of action which it might take.

105. The observer from the International Institute for the Unification of Private Law (UNIDROIT) stated that his organization was interested in co-operating with the Commission in the future work leading to the preparation of a draft Convention on the Liability of International Terminal Operators, one of the texts analysed in the report.

106. The Secretariat was also requested to prepare further reports of this nature and several topics for future re-

B. *General Assembly resolution 36/107 on international economic law*

98. The Commission took note of General Assembly resolution 36/107 of 10 December 1981 on progressive development of the principles and norms of international law relating to the new international economic order. It also took note of information given by the Secretariat on its co-operation with the United Nations Institute for Training and Research (UNITAR) which had been entrusted with a study relating to this issue.

99. A view was expressed that this study was connected with some aspects of international trade law and that the Commission should be informed regularly in the future of the progress of the study. It was further suggested that the experience of the Commission in dealing with the new international economic order might be of relevance to the study.

100. The Commission heard a statement by the observer for UNITAR, who pointed out that all relevant information on the work of the Commission needed for the study had been received from the Secretariat of the Commission and that there was a close co-operation between the Secretariats of UNITAR and the Commission.

* Reproduced in this volume, part two, VI, B.

²³ The Commission considered this subject at its 263rd and 264th meetings, on 2 and 3 August 1982.

²⁴ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 100 (Yearbook . . . 1981, part one, A).

ports were suggested, among which were transfer of technology and legal aspects of the new international economic order. There was general agreement, however, that the Secretariat should be free to choose the subject on which to report in the light of the developments in the field and the resources available to the Secretariat.

107. The Commission also repeated its desire, expressed at the fourteenth session, that a report be submitted at regular intervals on all the activities of other organizations active in the field of international trade law. It was stated that some Governments circulated the report throughout the different ministries as a means of informing those ministries of the activities being undertaken and as a means of co-ordinating the approach of the Government in the different fora. It was suggested that such a report might be submitted once every two or three years.

B. *Documentary credits*²⁵

Introduction

108. The Commission had before it a note by the Secretariat which described the progress made by the International Chamber of Commerce (ICC) in the revision of the 1974 version of the Uniform Customs and Practice for Documentary Credits (UCP) (A/CN.9/229).^{*} The Commission was informed that a draft revised text of UCP was ready for circulation by ICC to its national committees and that, at the request of ICC, the draft text would be circulated later this month by the Secretariat to all States for comment. It was expected that the final version of the revised text would be ready for adoption by ICC during the course of this year. It was suggested that the Commission might wish to consider at its sixteenth session the possibility of commending the use of the revised text of UCP, as it had in respect of the 1962 and 1974 versions of UCP.

Discussion at the session

109. A proposal was made that the Secretariat should be requested to make a study of the use of letters of credit, especially for purposes other than the sale of goods, to see whether the current law was adequate. It was pointed out that letters of credit were originally intended to be used in connection with the documentary sale of goods. Currently they are used for a number of other purposes, such as in connection with bid bonds and re-purchase agreements. It was suggested that the legal rules developed for the one situation might not be appropriate for these other uses to which letters of credit are currently put.

110. It was pointed out that such a study should not prejudice any future endorsement by the Commission at

its sixteenth session of the new revision of UCP. That revision by ICC had been undertaken largely to reflect recent changes in transport technology and banking practice as they affected the traditional function of the documentary credit in the international sale of goods. This revision of UCP was desirable in any case. Furthermore, it could be expected that the study would be a long-term project and could not be before the Commission at the time the new revision of UCP was presented for endorsement.

111. The observer from ICC stated that his organization looked forward to co-operating in the preparation of the study.

Decision of the Commission

112. After discussion the Commission decided to request the Secretary-General to submit to a future session of the Commission a study on letters of credit and their operation in order to identify legal problems arising from their use, especially in connection with contracts other than those for the sale of goods.

C. *General co-ordination of activities*²⁶

113. The Commission had before it a note by the Secretary-General which discussed the co-ordination activities of the Secretariat during the last year (A/CN.9/226).^{*}

114. The representative of the Hague Conference on Private International Law reported that invitations had been sent to all members of the Commission, whether or not they were members of the Conference, to attend the meeting of the Special Commission to consider the preparatory work for the revision of the 1955 Hague Convention on the Law Applicable to International Sale of Goods.

115. The representative of the International Institute for the Unification of Private Law (UNIDROIT) reported that all members of the Commission had been invited to a meeting of governmental experts in Rome from 2 to 13 November 1981 to revise the draft Uniform Law on Agency of an International Character in the International Sale of Goods. The draft law had been revised to make it conform better to the United Nations Convention on Contracts for the International Sale of Goods. It was also reported that the Government of Switzerland had agreed to be the host to a diplomatic conference in Geneva from 31 January to 18 February 1983 to adopt a convention on the subject.

116. The Commission noted that, at its fourteenth session, it had welcomed the decision of the Hague Conference and UNIDROIT to invite members of the Commission to participate in the preparatory work on these conventions and that it regarded them as significant steps to-

^{*} Reproduced in this volume, part two, VI, C.

²⁵ The Commission considered this subject at its 263rd meeting, on 2 August 1982.

^{*} Reproduced in this volume, part two, VI, A.

²⁶ The Commission considered this subject at its 263rd and 264th meetings, on 2 and 3 August 1982.

wards close collaboration in the work of the unification of the law related to international trade.²⁷ The Commission also noted that the General Assembly, in resolution 36/32 of 13 November 1981, had also welcomed these decisions.

117. The representative of the Council of Europe indicated the interest of his organization in co-operating with the Commission in activities of mutual interest, and in particular in respect of the legal value of computer records, a subject on which the Council of Europe adopted a Recommendation to Governments.

118. The Commission expressed its approval of the co-ordination activities of the Secretariat. It also welcomed the statements of those representatives of other organizations who had spoken. The Secretariat was urged to continue its efforts in this regard, and especially with those organizations mentioned in General Assembly resolution 34/142 on the co-ordinating role of the Commission.

CHAPTER VII. STATUS OF CONVENTIONS²⁸

119. The Commission considered the status of conventions that were the outcome of its work, i.e. Convention on the Limitation Period in the International Sale of Goods (New York, 1974); Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980); United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg); and United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). The Commission had before it a note by the Secretary-General entitled "Status of conventions" (A/CN.9/227)* which sets forth the status of signatures, ratifications and accessions to these Conventions as at 15 May 1982.

120. The Commission noted that, pursuant to paragraph 8 of General Assembly resolution 36/32 of 13 November 1981, the Secretary-General had brought these Conventions to the notice of all States which had not ratified or acceded to them, provided these States with appropriate information as to the mode of their entry into force and the current status of ratifications and accessions, and had drawn the attention of these States to the view of the Commission that an early entry into force and a wide acceptance of these Conventions would be of great value for the unification of international trade law.

121. The Commission noted with appreciation that, subsequent to 15 May 1982, Chile had ratified the United

Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg), and that ratification by France of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) had been authorized by its Parliament.

122. As regards the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980), many States indicated that the question of adhering to this Convention was under active consideration and some of these States indicated that a decision favourable to adherence was expected. Several States indicated that the procedures for adherence were taking place.

123. As regards the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg), many States indicated that the question of adhering to this Convention was under active consideration. Several States indicated their intention of adhering to the Convention. The Secretary of the Commission noted that, in connection with this Convention, the United Nations Conference on Trade and Development was also taking steps to promote adherence to it.

124. The Secretary of the Commission informed the Commission that the Secretariat intended to hold regional seminars on the three Conventions noted above in connection with the Commission's programme of training and assistance, in order to enhance wider adherence to these Conventions.

CHAPTER VIII. TRAINING AND ASSISTANCE IN THE FIELD OF INTERNATIONAL TRADE LAW²⁹

Introduction

125. The Commission, at its fourteenth session,³⁰ agreed that it should continue to sponsor symposia and seminars on international trade law and considered it desirable for these seminars to be organized on a regional basis. The Commission welcomed the possibility that these regional seminars might be sponsored jointly with regional organizations. It requested the Secretariat to make such arrangements as it found desirable in this regard.

126. By its resolution 36/32 of 13 November 1981, the General Assembly reaffirmed the importance, in particular for the developing countries, of the work of the Commission concerned with training and assistance in the field of international trade law and welcomed the initiatives being undertaken to sponsor regional seminars jointly with

* Reproduced in this volume, part two, VII.

²⁷ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 94. (Yearbook . . . 1981, part one, A).

²⁸ The Commission considered this subject at its 264th meeting, on 3 August 1982.

²⁹ The Commission considered this subject at its 267th meeting, on 4 August 1982.

³⁰ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 109 (Yearbook . . . 1981, part one, A).

regional organizations. The resolution also invited Governments, relevant United Nations organs, organizations, institutions and individuals to assist the Secretariat in financing and organizing symposia and seminars.

127. The Commission had before it a note by the Secretariat entitled "Training and assistance" (A/CN.9/228).^{*} This note reported that the Inter-American Juridical Committee of the Organization of American States had included in its 1982 annual seminar the subject of international sale of goods and that the Secretary-General of the Asian-African Legal Consultative Committee had agreed to organize, jointly with the UNCITRAL Secretariat, seminars on trade law subjects in conjunction with its annual sessions whenever feasible. The note also reported on activities of the Secretariat to promote training and assistance in the field of international trade law.

Discussion at the session

128. The Commission was informed that a contribution had been received from the Government of Yugoslavia in the amount of \$US 3,000 to be used towards the financing of the Commission's training and assistance programme. In addition, the Government of the Netherlands had made available the sum of 25,000 guilders to be used toward the financing of seminars or symposia which the Commission might organize in the future. The Commission expressed its gratitude for these contributions.

129. The Commission was informed that the Government of Australia conducted a seminar each year in the field of international trade law, including the work of the Commission. It was considering holding a future seminar in this field which would relate specifically to the countries of the Pacific region. The Commission was also informed that an institute for the unification of trade law had been established at the University of Seville and that the work of this institution would be closely related to the work of the Commission. It was reported that the Ministry of Commerce of Iraq was organizing a symposium which would deal with the United Nations Convention on Contracts for the International Sale of Goods for officials in Iraq dealing with international trade. In addition, the Commission was informed that the work of UNCITRAL was the subject of analysis and discussion at the University of Baghdad.

130. The Secretary of the Commission expressed appreciation to Governments and institutions which were arranging seminars or symposia in the field of international trade law and requested that the Secretariat be supplied with copies of papers or proceedings in connection with these seminars or symposia in order to assist the Secretariat in its further planning of regional seminars.

131. The view was expressed that initiatives such as those about which the Commission had been informed were

of particular benefit to developing countries and it was hoped that such initiatives would continue.

Decision of the Commission

132. The Commission agreed that the Secretariat should continue to explore various possibilities of collaborating with other organizations and institutions in the organization of regional seminars and also to use those occasions for the promotion of legal texts emanating from the work of the Commission.

CHAPTER IX. MOST-FAVOURLED-NATION CLAUSES³¹

Introduction

133. In resolution 36/111 of 10 December 1981 the General Assembly requested, *inter alia*, the Commission to submit any written comments and observations which it deemed appropriate on chapter II of the report of the International Law Commission on the work of its thirtieth session,³² and in particular on the draft articles on most-favoured-nation clauses adopted by the International Law Commission and those provisions relating to such clauses on which the International Law Commission was unable to take a decision.

134. The Commission had before it a note by the Secretariat entitled "Most-favoured-nation clauses" (A/CN.9/224).^{*} This note briefly set forth the background of resolution 36/111 and of the draft articles on most-favoured-nation clauses. In order to assist the Commission in its consideration of procedures for responding to the request of the General Assembly, the note discussed the purpose of the draft articles on most-favoured-nation clauses, and drew attention to certain points in connection with three issues relating to the draft articles. The note concluded by suggesting a possible procedure for formulating the Commission's response to the request of the General Assembly.

Discussion at the session

135. The Commission was divided as to whether it should proceed to formulate comments and observations upon the International Law Commission draft articles on most-favoured-nation clauses.

136. In support of the view that the Commission should formulate comments and observations in response to the request of the General Assembly, it was suggested that as a subsidiary organ of the General Assembly UNCITRAL was the most appropriate legal body to consider the Interna-

^{*} Reproduced in this volume, part two, V.

³¹ The Commission considered this subject at its 262nd meeting, on 2 August 1982.

³² *Official Records of the General Assembly, Thirty-third Session, Supplement No. 10 A/33/10 and Corr. 1 (Arabic only)*. (Yearbook of the International Law Commission 1978, vol. II, Part Two).

^{*} Reproduced in this volume, part two, VIII.

tional Law Commission draft articles. According to this view the draft articles were closely linked to international trade and the comments of the Commission on the draft articles could help remove obstacles to international trade and could assist in the development of international trade. A number of members of the Commission who spoke on this issue supported this view.

137. In support of the view that the Commission should not formulate comments and observations, it was suggested that the draft articles were outside the field of trade law, but rather dealt with questions of treaty law and trade policy, thus making them an inappropriate subject of consideration by the Commission. Concern was also expressed that the topic of most-favoured-nation clauses involved controversial political issues with which the Commission was not equipped to deal. It was suggested that the task of reconciling the divergent views concerning these issues should be left to other fora. It was further suggested that the draft articles had been considered by the Sixth Committee and the General Assembly and had already been commented on by some States, United Nations organs and international organizations. A majority of the members of the Commission who spoke on this issue supported this view.

138. The Commission noted that in the absence of a consensus no substantive comments on the draft articles could be submitted.

CHAPTER X. RELEVANT GENERAL ASSEMBLY RESOLUTIONS, FUTURE WORK AND OTHER BUSINESS³³

A. Relevant General Assembly resolutions

(i) General Assembly resolution on the work of the Commission

139. The Commission took note with appreciation of General Assembly resolution 36/32 of 13 November 1981 on the report of the United Nations Commission on International Trade Law on the work of its fourteenth session.

(ii) General Assembly resolution on international economic law

140. The Commission considered General Assembly resolution 36/107 of 10 December 1981 in connection with item 7 of the agenda.³⁴

(iii) General Assembly resolution on most-favoured-nation clauses

141. The Commission considered General Assembly resolution 36/111 of 10 December 1981 in connection with item 11 of the agenda.³⁵

B. Book on UNCITRAL

(i) Affirmation of decision

142. The Commission, at its fourteenth session, in connection with its discussion of co-ordination of work, decided to authorize the Secretariat to publish a book on UNCITRAL.³⁶ However, this decision was inadvertently not reflected in the report of the Commission at its fourteenth session.

143. The Commission decided to affirm the decision taken at its fourteenth session by including the following paragraph in the report of its present session:

"In view of the desirability of promoting further the work of the Commission and the legal texts associated with this work, the Commission decided to authorize the Secretariat to publish a book describing the activities of the Commission for the harmonization of unification of international trade law, together with legal texts emanating from the work of the Commission."

(ii) News-letter

144. The suggestion was made that an UNCITRAL news-letter might be prepared and distributed either quarterly or semi-annually. Such a news-letter might include such matters as information on ratifications or adherences to the conventions emanating from the work of the Commission, the actions of its working groups, activities of other organizations and summaries of judicial decisions relevant to the work of the Commission.

145. There was general agreement that such a news-letter would be useful. It was stated that it would be of particular value to the developing countries which often had a difficult time keeping abreast of developments. In this connection the statements previously made in respect of the co-ordination of work were recalled.³⁷ In addition, it would serve as a means of promoting the work of the Commission, including the ratification or adherence to the conventions which it had prepared.

146. It was decided to request the Secretary-General to prepare a note for the next session which would consider the format which such a news-letter might take, as well as the administrative and financial implications.

C. Date and place of the sixteenth session of the Commission

147. It was decided that the sixteenth session of the

³³ The Commission considered this subject at its 267th meeting, on 4 August 1982.

³⁴ See paras. 98-100.

³⁵ See chap. IX.

³⁶ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), paras. 85-101 (Yearbook ... 1981, part one, A).

³⁷ See para. 107.

Commission would be held from 24 May to 3 June 1983 at Vienna.

D. Sessions of the Working Groups

148. It was decided that the Working Group on International Contract Practices would hold its fourth session from 4 to 15 October 1982 at Vienna and its fifth session from 22 February to 4 March 1983 in New York.

149. It was decided that the fourth session of the Working Group on the New International Economic Order would be held from 16 to 20 May 1983 at Vienna.

ANNEX I

Recommendations to assist arbitral institutions and other interested bodies with regard to arbitration under the UNCITRAL Arbitration Rules

[Annex reproduced in part three, II, of this volume.]

ANNEX II

List of documents before the session

[Annex not reproduced; see check list of UNCITRAL documents at the end of this volume.]

B. United Nations Conference on Trade and Development (UNCTAD): extract from the report of the Trade and Development Board (twenty-fifth session) (TD/B/930)*

"B. *Progressive development of the law of international trade: fifteenth annual report of the United Nations Commission on International Trade Law (agenda item 10 (b))*

"713. For the consideration of this item the Board had before it the report of the United Nations Commission on International Trade Law on the work of its fifteenth session,³⁵ distributed under cover of TD/B/923.

"Action by the Board

"714. At its 588th meeting, on 7 September 1982, the Board took note of the report of the United Nations Commission on International Trade Law on its fifteenth session."

³⁵ For the printed text, see *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17 and Corr. 1)*."

* *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 15 (A/37/15)*, vol. II, chap. VII: Other matters in the field of trade and development.

C. General Assembly: report of the Sixth Committee (A/37/620)*

1. At its 4th plenary meeting, on 24 September 1982, the General Assembly decided to include in the agenda of its thirty-seventh session the item entitled "Report of the United Nations Commission on International Trade Law on the work of its fifteenth session" and to allocate it to the Sixth Committee.

2. The Sixth Committee considered this item at its 3rd to 8th meetings, from 28 September to 4 October, and at its 43rd meeting, on 11 November 1982. The summary records of those meetings (A/C.6/37/SR.3-8 and 43) con-

tain the views of representatives who spoke during the consideration of this item.

3. At the 3rd meeting, on 28 September, the Chairman of the United Nations Commission on International Trade Law at its fifteenth session introduced its report on the work of that session.¹

¹ *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17 and Corr. 1 English only)* (reproduced in this volume, part one, A). The presentation of the report was pursuant to a decision by the Sixth Committee at its 1,096th meeting, on 13 December 1968 (See *Official Records of the General Assembly, Twenty-third Session, Annexes*, agenda item 88, document A/7408, para. 3) (Yearbook . . . 1968-1970, part two, I, B, 2).

* 24 November 1982, *Official Records of the General Assembly, Thirty-seventh Session, annexes*, agenda item 119.

4. In addition to this report, the Committee had before it in connection with the item a note by the Secretary-General (A/C.6/37/L.6) relating to the consideration of the report by the Trade and Development Board of the United Nations Conference on Trade and Development.

5. At the 43rd meeting, on 11 November, the representative of Austria introduced a draft resolution (A/C.6/37/L.7) sponsored by Argentina, Australia, Austria, Belgium, Brazil, Canada, Chile, Egypt, Finland, France, Germany, Federal Republic of, Greece, India, Italy, Jamaica, Japan, Kenya, Morocco, the Netherlands, Nigeria, the Philippines, Senegal, Singapore, Spain, Sweden, Thailand, Trinidad and Tobago, Turkey and Yugoslavia, later joined by Cyprus and Ghana, as well as a draft resolution (A/C.6/37/L.8) sponsored by Australia, Austria, Chile, Egypt, Finland, France, Germany, Federal Republic of, Greece, Japan, Kenya, the Netherlands, Nigeria, the Philippines, Singapore, Sweden and Thailand, later joined by Cyprus.

6. The representative of Hungary spoke on behalf of a number of delegations in explanation of their positions and

requested that draft resolution (A/C.6/37/L.7) be adopted without a vote. The representative of the United Kingdom of Great Britain and Northern Ireland made a statement in the light of the statement made by the representative of Hungary.

7. At the same meeting, the Committee adopted draft resolution (A/C.6/37/L.7) without a vote (see paragraph 9, draft resolution I) and draft resolution (A/C.6/37/L.8) by consensus (see paragraph 9, draft resolution II).

8. The representative of Cuba spoke in explanation of her country's position.

RECOMMENDATIONS OF THE SIXTH COMMITTEE

9. The Sixth Committee recommends to the General Assembly the adoption of the following draft resolution:

[Texts not reproduced in this section. Draft resolution I and draft resolution II were adopted, with editorial changes, as General Assembly resolutions 37/106 and 37/107. See section D, below.]

D. General Assembly resolutions 37/106 and 37/107 of 16 December 1982

37/106. REPORT OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW*

The General Assembly,

Having considered the report of the United Nations Commission on International Trade Law on the work of its fifteenth session,¹

Recalling that the object of the United Nations Commission on International Trade Law is the promotion of the progressive harmonization and unification of international trade law,

Recalling, in this regard, its resolutions 2205 (XXI) of 17 December 1966, by which it established the United Nations Commission on International Trade Law and defined the object and terms of reference of the Commission, 3108 (XXVIII) of 12 December 1973, by which it increased the membership of the Commission, 34/142 of 17 December 1979, by which the co-ordinating function of the Commission in the field of international trade law was emphasized, and 36/32 of 13 November 1981, by which the importance of the participation of observers from all States and interested international organizations at sessions of the Commis-

sion and its Working Groups was affirmed, as well as its previous resolutions concerning the reports of the Commission on the work of its annual sessions,

Recalling also its resolutions 3201 (S-VI) and 3202 (S-VI) of 1 May 1974, 3281 (XXIX) of 12 December 1974 and 3362 (S-VII) of 16 September 1975,

Reaffirming its conviction that the progressive harmonization and unification of international trade law, in reducing or removing legal obstacles to the flow of international trade, especially those affecting the developing countries, would significantly contribute to universal economic co-operation among all States on a basis of equality, equity and common interests and to the elimination of discrimination in international trade and, thereby, to the well-being of all peoples,

Having regard for the need to take into account the different social and legal systems in harmonizing the rules of international trade law,

Bearing in mind its resolution 36/111 of 10 December 1981 concerning the draft articles on most-favoured-nation clauses,

Stressing the usefulness and importance of sponsoring symposia and seminars, including those organized on a regional basis, for promoting better knowledge and understanding of international trade law and, especially, for the training of lawyers from developing countries in this field,

1. *Takes note with appreciation of the report of the*

* Adopted on the report of the Sixth Committee (A/37/620). The Committee examined the question at its 3rd to 8th meetings, from 28 September to 4 October 1982, and at its 43rd meeting, on 11 November 1982 (A/C.6/37/SR.3-8 and 43).

¹ *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17 and Corr. 1) (reproduced in this volume, part one, A).*

I. INTERNATIONAL CONTRACT PRACTICES*

A. Report of the Secretary-General: text of draft uniform rules on liquidated damages and penalty clauses, together with a commentary thereon (A/CN.9/218)**

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Introduction

1. At its eleventh session, the Commission included in its new programme of work the subject of liquidated damages and penalty clauses as part of the study of international contract practices.¹ At its twelfth session, the Commission considered a report of the Secretary-General entitled "Liquidated damages and penalty clauses",² and requested its Working Group on International Contract Practices to consider the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.³ The Working Group held two sessions,⁴ and at its second session adopted draft uniform rules on liquidated damages and penalty clauses.⁵

2. At its fourteenth session, the Commission considered these draft rules, and *inter alia* requested the Secretary-

General to incorporate in the draft uniform rules such supplementary provisions as might be required if the rules were to take the form of a convention or a model law, and to prepare a commentary on the uniform rules.⁶ The present document has been prepared in response to this request. The draft uniform rules incorporating the supplementary provisions are hereinafter referred to as "the Rules".

3. Two previous attempts have been made at a regional level at unification in this field.⁷ An attempt made within the Council of Europe culminated in the formulation of a set of principles set forth in an appendix to resolution (78) 3 on penal clauses in civil law adopted by the Committee of Ministers on 20 January 1978. The resolution (hereinafter referred to as the "Council of Europe resolution") recommends to member Governments that they take the principles into consideration when preparing new legislation on this subject, and consider the extent to which the principles can be applied, subject to any necessary modifications, to other clauses which have the same aim or effect as penal clauses.⁸ An attempt made within the Benelux Economic Union culminated in the adoption at the Hague on 26 November 1973 of the Benelux Conven-

* For consideration by the Commission see Report, chapter II (part one, A, above).

** 11 November 1981.

¹ Report of the United Nations Commission on International Trade Law on the work of its eleventh session (1979), *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17* (A/33/17), para. 67 (c) (i) b (Yearbook ... 1978, part one, II, A).

² A/CN.9/161 (Yearbook ... 1979, part two, I, C).

³ Report of the United Nations Commission on International Trade Law on the work of its twelfth session (1979), *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 31 (Yearbook ... 1979, part one, II, A).

⁴ The report of the Working Group on the work of its first session is contained in A/CN.9/177, (Yearbook ... 1980, part two, II) and on the work of its second session in A/CN.9/197 (Yearbook ... 1981, part two, I, A). At its second session, the Working Group had before it a report of the Secretary-General entitled "Liquidated damages and penalty clauses (II)", A/CN.9/WG.2/WP.33 and Add. 1 (Yearbook ... 1981, part two, I, B).

⁵ A/CN.9/197, Annex (Yearbook ... 1981, part two, I, A).

⁶ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session (1981), *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 44 (Yearbook ... 1981, part one, A).

⁷ The General Conditions of Delivery of Goods between Organizations of the Member Countries of the Council for Mutual Economic Assistance, 1968/1975 as amended in 1979, also contain several provisions regulating liquidated damages and penalty clauses.

⁸ The resolution, the principles, and an explanatory memorandum have been published as a booklet by the Council of Europe (Strasbourg, 1978).

tion relating to the Penalty Clause (hereinafter referred to as the "Benelux Convention"). Under article 1, the Contracting States agree that they will bring their national legislation on penalty clauses into conformity with certain common provisions set forth in an annex to the Convention, at the latest by the date of entry into force of the Convention.⁹ While these attempts are directed to unifying national law, the scope of application of the uniform provisions is not restricted to domestic transactions. Accordingly, relevant provisions formulated in these two previous attempts are referred to where appropriate in the commentary set forth below.

4. Liquidated damages and penalty clauses are very widely used in international trade transactions. However, there are major differences in the way different legal systems resolve certain issues arising under such clauses. As a result, there may be considerable uncertainty as to the rights of the parties under a clause until the applicable law is determined.¹⁰ The Rules are intended to remedy this situation by unification at a global level.

5. The formulation of the Rules reflect the impact of several factors. An attempt was made, to the extent possible, to give effect to international trade practice.¹¹ An examination of such practice disclosed that, while the clauses to some extent followed a standard pattern and were used for a limited number of purposes, there was a considerable variety in their formulation. To accommodate this feature, the Rules to a large extent give autonomy to the parties. Parties are free to vary all the provisions except those defining the scope of application of the Rules, and that defining the power of a court or arbitral tribunal to reduce the agreed sum. International trade practice was also referred to in determining what should appropriately be the rights of the parties under the Rules.

6. In the course of formulating the Rules, various national laws were also examined, and an attempt was made to retain in the Rules solutions common to the different laws, and to embody therein compromise solutions which satisfy the various policies in the laws.

7. Part I of this document sets forth the Rules, i.e. the texts of the draft Convention and the draft Model Law. The Rules combine the draft provisions adopted by the Working Group with supplementary provisions prepared by the Secretariat. In preparing the supplementary provisions, in accordance with the directions of the Commission, the Secretariat took into account the relevant provisions of instruments which have emerged from the work of the Commission.¹²

⁹ The Convention, with its annex, and a commentary, have been published as a booklet by the Benelux Economic Union. The Convention has not yet entered into force.

¹⁰ For a full treatment of this issue, see A/CN.9/161, sections IV and V (Yearbook . . . 1979, part two, I, C).

¹¹ A/CN.9/WG.2/WP.33 contains the results of an investigation of international trade practice (Yearbook . . . 1981, part two, I, B).

¹² Report of the United Nations Commission on International Trade Law on the work of its fourteenth session (1981), *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 43 (Yearbook . . . 1981, part one, A).

Footnotes indicate which provisions were adopted by the Working Group and which were prepared by the Secretariat.

8. The full text of a convention must include a set of final provisions. Some of these would be provisions necessary in any convention (e.g. articles providing for methods by which States may become parties, entry into force articles, articles providing for methods by which States cease to be parties, depositary article). Others would relate more closely to the substance of a convention. Examples of issues to be regulated by such provisions would be: the relationship between the draft Convention and earlier and later Conventions which also regulate liquidated damages and penalty clauses, and the possibility of not applying the draft Convention when two or more States have closely related rules on liquidated damages and penalty clauses. A set of final provisions has not been prepared at this stage in accordance with the past practice of the Commission.

9. Where a State adopts the draft Model Law, provisions additional to those set forth below may be necessary to ensure that the adopted law is workable within the legal system of that State. The legislature of the State adopting the law would be the appropriate body to decide on what provisions are necessary.

10. The texts of the draft Convention and the draft Model Law differ only in article A, paragraph (1). Accordingly, in Part II a separate commentary is given on this paragraph in respect of each instrument and a single commentary is given in respect of the other provisions.

Part I. The rules

DRAFT CONVENTION

Article A, paragraph (1)

(1) This Convention applies to contracts in which the parties have agreed [in writing] that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) is entitled to recover, or to forfeit an agreed sum of money¹³ when, at the time of the conclusion of the contract, the parties have their places of business in different Contracting States.¹⁴

DRAFT MODEL LAW

Article A, paragraph (1)

(1) This law applies to contracts in which the parties

¹³ Working Group draft (draft rule 1, A/CN.9/197, annex) (Yearbook . . . 1981, part two, I, A).

¹⁴ Secretariat supplementary provision. This criterion has been adopted in the Convention on the Limitation Period in the International Sale of Goods (Yearbook . . . 1974, part three, I, B) (hereinafter referred to as the "Limitation Convention") article 2(a), and in the United Nations Convention on Contracts for the International Sale of Goods (Yearbook . . . 1980, part three, I, B) (hereinafter referred to as the "Sales Convention") article 1(1).

have agreed [in writing] that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) is entitled to recover, or to forfeit an agreed sum of money.¹⁵

(a) When, at the time of the conclusion of the contract, the parties have their places of business in different States, and

(b) When the rules of private international law lead to the application of the law of (the State adopting the Model Law).¹⁶

DRAFT CONVENTION AND DRAFT MODEL LAW

*Article A, paragraphs (2) and (3)*¹⁷

(2) The fact that the parties have their places of business in different States is to be disregarded whenever this fact does not appear either from the contract or from any dealings between, or from information disclosed by, the parties at any time before or at the conclusion of the contract.

(3) Neither the nationality of the parties nor the civil or commercial character of the parties or of the contract is to be taken into consideration in determining the application of this (Convention) (law).

*Article B*¹⁸

For the purposes of this (Convention) (law):

(1) If a party has more than one place of business, the place of business is that which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of the contract.

(2) If a party does not have a place of business, reference is to be made to his habitual residence.

*Article C*¹⁹

This (Convention) (law) does not apply to contracts concerning goods, other property or services which are to

¹⁵ Working Group draft (draft rule 1, A/CN.9/197, annex) (Yearbook... 1981, part two, I, A).

¹⁶ Secretariat supplementary provision. The criterion at (a) has been adopted in the Limitation Convention, article 2(a), and in the Sales Convention, article 1(1). The criterion at (b) has been adopted in the Sales Convention, article 1(b).

¹⁷ Secretariat supplementary provisions. Paragraph (2) is identical with the Limitation Convention, article 2(b), and the Sales Convention, article 1(2). Paragraph (3) is identical with the Limitation Convention, article 2(e), and the Sales Convention, article 1(3).

¹⁸ Secretariat supplementary provision. It is identical with the Sales Convention, article 10, and in substance identical with the Limitation Convention, article 2(c) and (d).

¹⁹ Secretariat supplementary provision. It is to some extent derived from the Limitation Convention, article 4(a), and the Sales Convention, article 2(a).

be supplied for the personal, family or household purposes of a party, unless the other party, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the contract was concluded for such a purpose.

*Article D*²⁰

Unless the parties have agreed otherwise, the obligee is not entitled to recover or to forfeit the agreed sum if the obligor is not liable for the failure of performance.

*Article E*²¹

(1) Where the agreed sum is to be recoverable or forfeited on delay in performance of the obligation, the obligee is entitled to both performance of the obligation and the agreed sum.

(2) Where the agreed sum is to be recoverable or forfeited on non-performance, or defective performance other than delay, the obligee is entitled either to performance, or to recover or forfeit the agreed sum, unless the agreed sum cannot reasonably be regarded as a substitute for performance.

(3) The rules set forth above shall not prejudice any contrary agreement made by the parties.

*Article F*²²

Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or forfeited occurs, the obligee is entitled, in respect of the failure, to recover or forfeit the sum, and is entitled to damages to the extent of the loss not covered by the agreed sum, but only if he can prove that his loss grossly exceeds the agreed sum.

*Article G*²³

(1) The agreed sum shall not be reduced by a court or arbitral tribunal.

(2) However, the agreed sum may be reduced if it is shown to be grossly disproportionate in relation to the loss that has been suffered by the obligee, and if the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee.

²⁰ Working Group draft (draft rule 2, A/CN.9/197, annex) (Yearbook... 1981, part two, I, A).

²¹ *Ibid.* (draft rule 3, A/CN.9/197, annex).

²² *Ibid.* (draft rule 5, A/CN.9/197, annex).

²³ Working Group draft (draft rule 6, A/CN.9/197, annex) (Yearbook... 1981, part two, I, A).

Part II. Commentary

DRAFT CONVENTION AND DRAFT MODEL LAW

Article A

Prior uniform law

Limitation Convention, article 2 and article 3, paragraph 1;
Sales Convention, article 1 (1) and (3);
Council of Europe resolution, appendix, article 1;
Benelux Convention, annex, article 1.

Commentary, draft Convention, article A, paragraph (1)

11. This paragraph determines the scope of application of the Convention, and deals with the following issues:

- (a) The international character of a contract to which the Convention applies;
- (b) The link between a Contracting State and a contract which attracts the application of the Convention; and
- (c) The nature of contractual clauses regulated by the Convention.

The international character of a contract

12. The Convention only applies to international trade contracts. A contract is regarded as international if, at the time of the conclusion of the contract, the parties have their places of business in different States. In contrast with other possible criteria (e.g. that the acts constituting the offer and acceptance have been effected in the territories of different States) the criterion adopted, taken together with the rules in article B, is convenient to apply and provides certainty in the application of the Convention.

The application of the Convention

13. Some connection must exist between an international contract and the Convention sufficient to justify the application of the latter.

14. Under this article, the necessary connection is that each party has his place of business in a State which has adhered to the Convention. When this connection exists, the Convention must be applied by the forum of a Contracting State regardless of its rules of private international law.

Nature of the contractual clauses regulated

15. The clauses regulated are those commonly known as liquidated damages or penalty clauses.²⁴ They are normally formulated as follows: upon a failure to perform an obligation (hereinafter referred to as "the main obligation") by one party, the obligor, the other party, the ob-

ligee, is entitled to recover or to forfeit an agreed sum of money.

(a) *Failure of performance*

16. In international trade such clauses are always linked to a main obligation arising out of a contract, and accordingly the application of the Convention is restricted to contracts. As the agreed sum may become due on various kinds of failure of performance (e.g. delay, non-delivery, defective workmanship) the article is given a comprehensive scope covering both total and partial failure of performance.²⁵

(b) *The agreed sum*

17. In the practice of international trade, the obligation imposed on the non-performing party (the obligor) is always the payment of a sum of money. In most cases parties agree not on a fixed sum but on a formula for determining the sum payable by the obligor (e.g. \$X payable for each day of delay, or \$Y payable for each stipulated unit of output not attained), and the article is intended to cover such an agreement.

18. The article applies irrespective of whether the function of the agreed sum is to provide compensation payable by the obligor for the loss caused by his failure to perform, or is to coerce the obligor to perform, or is to serve as a limitation of the obligor's liability.²⁶ In many cases, however, the agreed sum serves both as compensation and as a coercion to perform. Accordingly, the article has been formulated to cover clauses with this dual purpose.²⁷

(c) *Recovery or forfeiture*

19. Under a liquidated damages or penalty clause, the agreed sum may be recoverable by the obligee directly from the obligor. However, it is often provided in international trade contracts that the sum is to be recovered from a bank under a bond for proper performance opened by the bank of the obligor in favour of the obligee,²⁸ and the article is drafted to cover such cases.

20. The entitlement to forfeiture envisaged in the article might arise in the following cases:

- (i) It is agreed between the parties that a sum of money paid by the obligor to the obligee is to be retained (forfeited) by the obligee in the event of failure of performance by the obligor, but returned in the event of proper performance;
- (ii) It is agreed between the parties that a sum of money due from the obligee to the obligor is to be

²⁵ A/CN.9/WG.2/WP.33, para. 14 (Yearbook . . . 1981, part two, I, B).

²⁶ A/CN.9/161, para. 4 (Yearbook . . . 1979, part two, I, C).

²⁷ A/CN.9/WG.2/WP.33, para. 12 (Yearbook . . . 1981, part two, I, B).

²⁸ *Ibid.* para. 17.

²⁴ For a full description of the nature of these clauses, see A/CN.9/161, Sections I and II (Yearbook . . . 1979, part two, I, C).

withheld (forfeited) by the obligee in the event of failure of performance by the obligor, but paid in the event of proper performance.

(d) *Types of clauses not covered*

21. The formulation of the article excludes certain types of clauses from its scope. A clause under which the obligor has the right not to perform (e.g. to withdraw from the contract subject to paying the agreed sum), is excluded.²⁹ Such a clause is not regarded as a liquidated damages or penalty clause in most national laws. Furthermore, a limitation of liability clause which fixes a maximum amount payable if liability is proved, but not a minimum,³⁰ is excluded as no agreed sum of money is payable.

22. Whether certain other types of clauses fall within the scope of the article may depend on the wording of the clause in question. A contract may provide for the payment of a sum in instalments, and a clause may be added that, upon a single default, all outstanding instalments are immediately payable.³¹ Such an acceleration clause falls outside the article, as the contract only provides for a single main obligation. If however, upon the single default, a sum additional to the outstanding instalments becomes payable, the clause may fall within the article. Again, a clause may be formulated as providing alternative obligations, e.g. fixing the price of goods sold at \$10,000 payable on 1 January, but giving an alternative of paying on 1 October the sum of \$15,000.³² If this is a true alternative obligation, the clause falls outside the article, as the \$15,000 is not payable on a failure of performance. However, if the clause is construed to impose a main obligation to pay \$10,000 on 1 January, and an obligation to pay \$5,000 on failure of that performance, it falls within the article.

23. The words "in writing" have been provisionally included because under some legal systems certain international trade contracts are only valid if they are in writing.

Commentary, draft Model Law, article A, paragraph (1)

The international character of a contract, and the nature of the contractual clauses regulated

24. As regards these matters, the scope of application of article A is the same as that of article A of the draft Convention.

²⁹ A/CN.9/161, para. 9 (Yearbook . . . 1979, part two, I, C); A/CN.9/WG.2/WP.33, para. 19, illustration (Yearbook . . . 1981, part two, I, B).

³⁰ A/CN.9/161, para. 12 (Yearbook . . . 1979, part two, I, C).

³¹ *Ibid.* para. 10; A/CN.9/WG.2/WP.33, para. 15, illustration (Yearbook . . . 1981, part two, I, B).

³² A/CN.9/161, para. 8 (Yearbook 1979, part two, I, C).

The application of the law

25. Under paragraph (1) (b) of this article, the forum of a State which adopts the Model Law must apply the law when its rules of private international law lead to the application of its law. Since after its adoption the Model Law becomes national law, it is appropriate to make its application depend on the choice of law rules regulating the application of national law.

Commentary, article A, paragraphs (2) and (3)

Paragraph (2)

AWARENESS OF SITUATION

26. Under paragraph (2), the Rules do not apply if "the fact that the parties have their places of business in different States . . . does not appear either from the contract or from any dealings between, or from information disclosed by, the parties at any time before or at the conclusion of the contract". One example of such a situation is where the parties appeared to have their places of business in the same State but one of the parties was acting as the agent for an undisclosed foreign principal. In such a situation paragraph (2) provides that the contract, which appears to be between parties whose places of business are in the same State, is not governed by the Rules.

Paragraph (3)

NATIONALITY OF THE PARTIES, CIVIL OR COMMERCIAL CHARACTER OF THE TRANSACTION

27. The question whether the Rules are applicable to a contract is determined primarily by whether the relevant "places of business" of the parties are in different Contracting States. The relevant "place of business" of a party is determined by application of article B without reference to his nationality, place of incorporation, or place of head office. This paragraph reinforces that article by making it clear that the nationality of the parties is not to be taken into consideration.

28. In some legal systems the law relating to contracts is different depending on whether the parties or the contract are characterized as civil or commercial. In other legal systems this distinction is not known. In order to ensure that the provisions of the Rules are not interpreted to apply only to contracts characterized as "commercial" or between parties characterized as "commercial" under the law of a Contracting State or a State which has adopted the Model Law, this paragraph provides that the civil or commercial character of the parties or the contract is not to be taken into consideration.

29. It should be noted, however, that article C excludes from the sphere of application of the Rules certain contracts which are likely to be characterized

as "civil" contracts by a legal system which recognizes the distinction between civil and commercial contracts.

DRAFT CONVENTION AND DRAFT MODEL LAW

Article B

Prior uniform law

Limitation Convention, article 2 (c) and (d);
Sales Convention, article 10.

Paragraph (1)

PLACE OF BUSINESS

30. Paragraph (1) lays down the criterion for determining the relevant place of business; it is the place of business "which has the closest relationship to the contract and its performance". The phrase "the contract and its performance" refers to the transaction as a whole, including factors relating to the offer and the acceptance as well as the performance of the contract. The location of the head office or principal place of business is irrelevant for the purposes of this article unless that office or place of business becomes so involved in the transaction concerned as to be the place of business "which has the closest relationship to the contract and its performance."

31. In determining the place of business which has the "closest relationship", paragraph (1) states that regard is to be given to "the circumstances known to or contemplated by the parties at any time before or at the conclusion of the contract". Therefore, when the paragraph refers to the performance of the contract, it is referring to the performance that the parties contemplated when they were entering into the contract. If it were contemplated that a party would administer the contract at his place of business in State A, a determination that his "place of business" under this article was in State A would not be altered by his subsequent decision to transfer his place of business to State B.

32. Factors that may not be known to one of the parties at the time of entering into the contract would include supervision over the making of the contract by a head office located in another State, or the foreign origin or final destination of the goods. When these factors are not known to or contemplated by both parties at the time of entering into the contract, they are not to be taken into consideration.

Paragraph (2)

HABITUAL RESIDENCE

33. Paragraph (2) deals with the case where one of the parties does not have a place of business. Most international

contracts are entered into by businessmen who have recognized places of business. Occasionally, however, a person who does not have an established "place of business" may enter into a contract that is intended for trade purposes. The present provision provides that in this situation reference is to be made to his habitual residence.

DRAFT CONVENTION AND DRAFT MODEL LAW

Article C

Prior uniform law

Limitation Convention, article 4;
Sales Convention, article 2;
Council of Europe resolution, appendix, article 8.

Commentary

34. The Rules are intended to apply only to international trade transactions as it is in this field that uniform rules are needed. The article expresses this limitation.

35. This limitation also serves another purpose. Many national legal systems have laws which regulate liquidated damages and penalty clauses in specific types of contracts with a view to protecting the weaker party to such contracts. Such laws may be applicable only to domestic contracts, and in that event no conflict would arise with the Rules. Even where their scope is not so limited, they are often restricted to consumer contracts (i.e. transactions for personal, family or household purposes). By excluding such contracts from the scope of the Rules, possible conflict with such laws is reduced. Furthermore, if the Rules were to take the form of a Model Law, any potential conflicts between the Model Law and national laws could be expressly resolved by the legislature of the State adopting the Model Law at the time of such adoption.

36. The exclusion of application of the Rules is, however, qualified in certain cases. The parties should know by the time of the conclusion of the contract whether their rights and obligations are those under the Rules or those under the applicable national law. However, the circumstances attending a contract may in some cases be such that a party has no reason to know that the contract is a consumer contract to which the Rules do not apply. In such cases the Rules apply.

DRAFT CONVENTION AND DRAFT MODEL LAW

Article D

Prior uniform law

Council of Europe resolution, appendix, article 4;
Benelux Convention, annex, article 2, paragraph 3.

Commentary

37. Under this article, the liability of the obligor for the agreed sum is dependent on his liability for failure to perform the main obligation. It follows from the article that loss caused by the failure of performance of the obligor falls on the obligee "if the obligor is not liable for the failure of performance". Since the main purpose of the agreed sum is to provide a remedy for breach of contract, no sum is payable if there is no liability for failure of performance. Whether there is no liability, e.g. because the obligor has the defence of *force majeure*, or absence of fault, is determined under the applicable law.

38. The opening phrase of the article gives the parties the faculty of agreeing that the loss caused by the failure to perform the main obligation by the obligor lies on him even when he is not liable for such failure. Such an agreement may be justified by the circumstances attending the contract. However, where the defence of the obligor for failure to perform the main obligation is that the contract is void, the agreement may be ineffective because the liquidated damages or penalty clause is also void as forming part of the contract.

DRAFT CONVENTION AND DRAFT MODEL LAW

*Article E**Prior uniform law*

Council of Europe resolution, appendix, articles 2 and 3;
Benelux Convention, annex, article 2, paragraph 1.

Commentary

39. This article regulates the relationship of two potential rights of the obligee — performance of the main obligation, and recovery of the agreed sum.³³ In relating the two rights, the adoption of the principle that in all circumstances the obligee could only recover the agreed sum would result in his under-compensation in some instances. However, the adoption of the principle that in all circumstances the obligee could recover the agreed sum, and could also enforce the main obligation, would result in his over-compensation in some instances. Accordingly, paragraphs (1) and (2) of this article deal separately with the two cases encountered in practice, and attempt to provide results in accord with international trade practice and which are fair to both parties.

40. An agreed sum payable on delay in performance (paragraph (1)) will usually be quantified by the parties to compensate the obligee for the loss likely to be suffered by him during the delay occurring until performance takes place, and not to compensate him for non-performance. Accordingly, the obligee should be entitled to claim per-

formance of the main obligation and also to recover the agreed sum.³⁴ The position would be the same even if the delay continued for such a long period as to justify the anticipation that the obligor will not perform.³⁵ In such a case, if performance by the obligor is not enforced by the legal system, the obligee will be awarded by the court a remedy additional to the agreed sum in order to compensate for the non-performance. Whether there has been delay in a particular case will be decided under the applicable national law.

41. Paragraph (2) covers all cases other than those where the agreed sum is payable on delay.³⁶ In cases covered by this paragraph, the agreed sum is normally quantified so as fully to compensate the obligee for the failure to perform. In such cases, recovery of the agreed sum would be a monetary substitute for performance of the main obligation by the obligor. Accordingly, the obligee should not be entitled both to claim performance of the main obligation and to recover the agreed sum. On the other hand, it also follows that, where the agreed sum cannot reasonably be regarded as a substitute for performance, the reason noted above for refusing to give the obligee both remedies does not exist.

42. Paragraph (3) gives the parties the faculty to vary the principles contained in paragraphs (1) and (2) (e.g. to vary the principle in paragraph (2) by providing that the obligee is in all circumstances entitled to claim both performance of the main obligation and recovery of the agreed sum).

Relationship to articles F and G

43. It must also be noted that the rights of the parties under this article may, depending on the circumstances of the case, be affected by the succeeding articles F and G. For example, in a case falling under paragraph (1) of this article, if the loss suffered by the delay grossly exceeds the agreed sum, the obligee is entitled under article F to damages to the extent of the loss not covered by the agreed sum. As another example, where the obligee chooses to recover the agreed sum under paragraph (2) of this article, the sum may be reduced by the application of article G, paragraph (2).

DRAFT CONVENTION AND DRAFT MODEL LAW

*Article F**Prior uniform law*

Council of Europe resolution, appendix, article 5;
Benelux Convention, annex, article 2, paragraph 2.

³⁴ A/CN.WG.2/WP.33, paras. 30-32 (Yearbook . . . 1981, part two, I, B).

³⁵ Parties sometimes insert specific terms on the obligee's rights when the delay is of long duration: *Ibid.* para. 32.

³⁶ *Ibid.*, paras. 33-39.

³³ A/CN.9/161, Section V, A (Yearbook . . . 1979, part two, I, C); A/CN.9/WG.2/WP.33, Part I, Section C (Yearbook . . . 1981, part two, I, B).

Commentary

44. This provision regulates the relationship of two potential rights of the obligee — recovery of damages for failure to perform the main obligation, and recovery of the agreed sum.³⁷ Two advantages in agreeing on the sum payable for failure of performance are avoidance of the expense and uncertainty accompanying an action for the recovery of damages, and the fixing of the limits of the obligor's liability.³⁸ These advantages would be maximized by restricting the obligee to the recovery of the agreed sum. However, such a restriction would cause hardship to the obligee if his actual loss exceeds the agreed sum. The provision adopted compromises between these competing considerations by providing that the obligee is restricted to recovery of the agreed sum, except when his loss grossly exceeds that sum. Accordingly, when the obligee claims the agreed sum under article E, his rights may be supplemented by the right to damages given by this article.

45. The opening words of this article give the parties the faculty of varying the principle contained therein. Thus, where parties wish the agreed sum to be the absolute limit of the obligor's liability, they may so provide.³⁹

³⁷ A/CN.9/161, Section V, B (Yearbook . . . 1979, part two, I, C); A/CN.9/WG.2/WP.33, Part I, Section D (Yearbook . . . 1981, part two, I, B).

³⁸ A/CN.9/161, para. 4 (Yearbook . . . 1979, part two, I, C).

³⁹ A limitation clause which does not fix an agreed sum but only provides a monetary limit of liability is outside the scope of these provisions. See also para. 21 above.

DRAFT CONVENTION AND DRAFT MODEL LAW

*Article G**Prior uniform law*

Council of Europe resolution, appendix, article 7;
Benelux Convention, annex, article 4.

Commentary

46. Paragraph (1) of this article states that the agreed sum cannot be reduced. This principle is justified by the need for certainty in international trade transactions.

47. Paragraph (2) recognizes, however, that in very exceptional circumstances reduction of the agreed sum may be justified. Firstly, the agreed sum must grossly exceed the loss suffered by the obligee. Recovery of the agreed sum in such circumstances would unjustly enrich the obligee, and unfairly penalize the obligor. Secondly, the agreed sum should be such that it cannot reasonably be regarded as a genuine pre-estimate by the parties of the potential loss of the obligee. This limitation is justified by the view that agreements aiming solely at compensation for loss caused by failure to perform deserve to be encouraged.

48. As the purpose of this article is to permit a court or arbitral tribunal to vary the agreement of the parties, the article itself cannot be varied by the parties.

B. Note by the Secretary-General: draft uniform rules on liquidated damages and penalty clauses: analysis of the responses of Governments and international organizations (A/CN.9/219* and Add. 1, and Corr. 1 French only)**

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[A/CN.9/219]

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* 28 May 1982.

** 23 June 1982.

[A/CN.9/219/Add.1]

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[A/CN.9/219]

Introduction

1. At its fourteenth session, the United Nations Commission on International Trade Law considered rules on liquidated damages and penalty clauses prepared by its Working Group on International Contract Practices, and decided to request the Secretary-General:

“(a) To incorporate in the draft uniform rules on liquidated damages and penalty clauses prepared by the Working Group such supplementary provision as might be required if the rules were to take the form of a convention or a model law;

“(b) To prepare a commentary on the draft uniform rules;

“(c) To prepare a questionnaire addressed to Governments and international organizations seeking to elicit their views on the most appropriate form for the uniform rules; and

“(d) To circulate the draft uniform rules to all Governments and interested international organizations for their comments, together with the commentary and the questionnaire”.¹

2. In response to this request, the Secretariat incorporated in the draft uniform rules appropriate supplementary provisions, prepared a commentary on the draft uniform rules as so modified² and also prepared a questionnaire. Thereafter, under cover of letter dated 20 November 1981 and note verbale dated 14 December 1981, the draft uniform rules were circulated to interested international organizations and all Governments for their comments, together with the questionnaire and commentary. The present document analyses the responses received as of 31 May 1982. Part I analyses the answers to the questionnaire, while Part II analyses the comments on the draft uniform rules.

¹ Report of the United Nations Commission on the work of its fourteenth session (1981), *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 44 (Yearbook ... 1981, part one, A).

² The modified draft uniform rules and the commentary are contained in A/CN.9/218 (reproduced in this volume, part two, I, A).

3. Responses were received from the following Governments and international organizations:

Governments: Austria, Argentina, Canada, Chile, Cyprus, Japan, Philippines, Poland, Republic of Korea, Spain, Sweden, Turkey, Venezuela and the Union of Soviet Socialist Republics (USSR).

International organizations: United Nations Conference on Trade and Development (UNCTAD), and United Nations Industrial Development Organization (UNIDO).

Part I. Appropriate form for the uniform rules

A. CONVENTION

4. Some States (Austria, Argentina, Chile, Cyprus, Philippines, USSR) consider a convention to be the most appropriate form for the uniform rules. A convention will generate considerable interest and be widely acceptable because it has been negotiated among a large number of States, and the rules embodied in a convention may also form a model for national legislation (Chile, Philippines). A convention provides the greatest certainty of unifying the conflicting common law and civil law rules on the subject (Austria). A State which adheres to a convention must apply the rules as formulated therein as long as it remains a party to the convention (Austria, Chile, Philippines). The rules in a convention take precedence over, and are not affected by changes in, national law (Argentina, Cyprus), and this consideration makes a convention preferable despite the high cost of adopting one (Argentina).

5. As regards the procedure for adopting a convention, Argentina and Chile prefer a convention to be adopted by a conference of plenipotentiaries, although Chile proposes adoption by the General Assembly on the recommendation of the Sixth Committee if the convening of a conference of plenipotentiaries will be very costly. Argentina, however, notes that adoption by the General Assembly would also entail considerable costs, and further would delay the work of the Sixth Committee. The Philippines and the USSR

prefer a convention to be adopted by the General Assembly, the Philippines for the reason that this procedure is less costly.

6. Some States which support a form other than a convention give reasons for opposing a convention. Only a limited number of States would adhere to a convention (Poland, Sweden, Turkey). The need for unification in this field is limited (Sweden, Venezuela), and the developing countries do not give priority to unification in this field (Venezuela). The small number of articles in the draft makes a convention inappropriate (Poland).

7. Japan is not opposed to a convention if a majority in the Commission prefers this form, while Canada notes that, if a convention were to be chosen, it should only apply when specifically invoked by the parties in writing.

B. MODEL LAW

8. Some States (Japan, Poland, Republic of Korea, Spain) consider a model law to be the most effective form of unification.

9. The Commission, or the General Assembly, could recommend to States that they incorporate the model law in their national legislation (Philippines, Poland).

10. Some States which support a form other than a model law give reasons for opposing a model law. A model law may only provide limited unification because States are free to adopt a model law with modifications, and different States may make different modifications (Austria, Philippines).

C. UNCITRAL RULES (GENERAL CONDITIONS)

11. Some States (Canada, Sweden, Turkey, Venezuela) consider general conditions to be the most appropriate form. The adoption of this form furthers the principle of giving parties freedom as to the terms to be included in the contract (Canada, Turkey), and general conditions would give parties some guidance in drafting their contracts (Sweden). Furthermore, general conditions could be used by parties as soon as they are finalized by the Commission, and the uniform rules would thus be applied earlier than if one of the other forms were adopted (Canada). As general conditions the uniform rules may also have a wide application to many types of contracts (Turkey). Because unification in this field is not a matter of priority, the formulation of general conditions is the most practical and realistic approach, despite the limited unification achieved thereby (Venezuela).

12. Some States which support a form other than general conditions give reasons for opposing general conditions. General conditions forming part of a contract are invalid when they conflict with mandatory provisions of the applicable law regulating a liquidated damages or penal-

ty clause (Argentina, Japan, Philippines, Poland). Parties might not choose to incorporate the general conditions in their contracts (Argentina).

Part II. Comments on specific articles

A. DRAFT CONVENTION, ARTICLE A, PARAGRAPH (1)

13. Austria proposes that the draft Convention should apply in the same circumstances that the United Nations Convention on Contracts for the International Sale of Goods* (hereinafter referred to as the "Sales Convention") and the Convention on the Limitation Period in the International Sale of Goods** as amended by the Protocol of 1980*** apply i.e. when, at the time of the conclusion of the contract the parties have their places of business in different Contracting States, or when the rules of private international law lead to the application of the law of a Contracting State. Liquidated damages and penalty clauses are often contained in international sales contracts, and such harmonization would prevent disparity in the application of the three instruments to such contracts. Furthermore, if this draft article were so modified, the draft Convention would have a wider application.

B. DRAFT MODEL LAW, ARTICLE A, PARAGRAPH (1)

14. Austria notes that the application of the draft Model Law needs clarification in the following case: when the forum State has adopted the draft Model Law, but its rules of private international law lead, not to the application of its national law, but to the application of the law of another State which has adopted the draft Model Law. Austria proposes that the draft Model Law should apply in such a case, and that to achieve this purpose paragraph (1) (b) should be modified to read: "when the rules of private international law lead to the application of the law of a State adopting the model law".

15. Spain draws attention to the possibility that the parties may have their places of business in different States, only one of which has adopted the draft Model Law. It notes that the draft article does not clarify if the draft Model Law is to apply when the forum is in the State which has not adopted the draft Model Law.

16. Spain also notes that clarification is needed in that the present drafting of paragraph (1) might suggest that the mere fact that at the time of the conclusion of the contract the parties have their places of business in different States (i.e. only the conditions in subparagraph (a) are satisfied) makes the draft Model Law applicable. However,

* Yearbook . . . 1980, part three, I, B.

** Yearbook . . . 1974, part three, I, B.

*** Yearbook . . . 1980, part three, I, C.

the draft Model Law would not apply in such circumstances if neither of the States had adopted it.

17. Spain accordingly proposes the following text, which would resolve its concerns set forth in the preceding two paragraphs:

"(1) This law applies to contracts in which the parties have agreed in writing that, upon a total or partial failure of performance by one of them (the obligor), another party (the obligee) is entitled to recover, or to withhold and appropriate, an agreed sum of money, provided that:

"(a) The contract in question is an international one, in the sense that the parties have their places of business in different States at the time of conclusion of the contract, and

"(b) The Model Law has been adopted by both the States, or if by only one, the rules of private international law impose its application to the contract in any event."³

C. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE A, PARAGRAPH (1)

18. Some States (Republic of Korea, Spain,⁴ USSR) support retention of the requirement that the agreement of the parties should be in writing. Spain notes that writing appears to be required by its commercial code for the validity of international trade contracts. The Republic of Korea notes that the term writing should cover a clause in the contract itself, or a separate agreement signed by the parties, or an exchange of letters or telegrams. Austria supports the solution adopted in articles 11 and 96 of the Sales Convention in regard to the requirement of writing if the form of a convention is adopted.⁵

19. Spain notes that the term "forfeit"⁶ does not appear to be very appropriate in the context of this article, because of the associations of this word with public law. More appropriate are the following words or phrases: "retain", "appropriate", "possess himself of" or "withhold payment of reimbursement."⁷

³ This text submitted by Spain also incorporates certain suggestions by Spain on other issues: see paras. 18 and 19 below.

⁴ See text set forth in para. 17 above.

⁵ Article 11 is as follows:

"A contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirement as to form. It may be proved by any means, including witnesses."

Article 96 is as follows:

"A Contracting State whose legislation requires contracts of sale to be concluded in or evidenced by writing may at any time make a declaration in accordance with article 12 that any provision of article 11, article 29, or Part II of this Convention, that allows a contract of sale or its modification or termination by agreement or any offer, acceptance, or other indication of intention to be made in any form other than in writing, does not apply where any party has his place of business in that State."

⁶ In Spanish "confiscar". This term is also used in articles D, E and F.

⁷ In Spanish, "retener", "apropiarse", "hacer suya" or "dejar de pagar o reembolsar". See text set forth in para. 17 above.

20. The Republic of Korea notes that when a sum additional to the agreed sum becomes payable under an acceleration clause,⁸ such additional sum should be regarded as an agreed sum under this article.

21. UNIDO notes that the uniform rules do not deal with clauses providing an incentive (agreed sum as bonus) for performance before the due date. UNIDO also notes that a liquidated damages or penalty clause may not in all circumstances be an adequate remedy for physical or non-physical damage caused by breach of contract.

D. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE A, PARAGRAPH (3), AND ARTICLE C

22. Spain notes that although article A, paragraph (3) states, *inter alia*, that neither the civil nor commercial character of the contract is to be taken into consideration in determining the application of the Convention or model law, yet article C excludes non-commercial contracts from their application. Accordingly, Spain suggests that, while article C can remain unchanged, article A, paragraph (3) should be modified to read as follows:

"(3) Neither the nationality of the parties nor the civil or commercial character of the parties or of the contract is to be taken into consideration in determining the application of this law, except as provided in article C."⁹

23. UNCTAD notes that it may be advisable to clarify in the uniform rules that they do not apply to maritime transport contracts in view of the special nature of maritime transport. However, if it is felt desirable to cover maritime transport contracts, then careful consideration would have to be given to ensure consonance of the uniform rules with maritime law and practice e.g. in matters of demurrage under charterparties. Furthermore, UNCTAD submits that, in the latter case, before any uniform rules are finalized by UNCITRAL the subject should be co-ordinated with UNCTAD with a view to appropriate future action.

E. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE D

24. Sweden suggests that because of this article, there may be difficulty in applying the uniform rules to cases where the agreed sum is to be claimed from a bank under a first demand guarantee. Under such a guarantee the bank is bound to pay on demand of the obligee without inquiry as to the obligor's liability. The mere fact that the parties agree that that sum is to be claimed under a first demand guarantee may not amount to

⁸ See A/CN.9/218, para. 22 (reproduced in this volume, part two, I, A).

⁹ This proposal is drafted with reference to a model law, which Spain supports.

an agreement that the obligee is entitled to recover the agreed sum even if the obligor is not liable for his failure of performance. Accordingly, the question whether the uniform rules should cover such cases requires consideration.

25. Spain notes that this article may be superfluous, as the principle embodied therein is found in its civil code.¹⁰ It also notes that, under its civil code,¹¹ the nullity of the main obligation entails the nullity of the liquidated damages or penalty clause.¹²

F. DRAFT CONVENTION AND DRAFT MODEL LAW ARTICLE E, PARAGRAPHS (1) AND (2)

26. Sweden notes that the remedies of the obligee differ depending on whether the breach of contract by the obligor is delay in performance (paragraph (1)) or non-performance (paragraph (2)). However, it may be impossible to determine whether the breach is delay or non-performance until the delay has lasted so long that it is evident that performance will never take place.

27. The Republic of Korea observes that there is no justification for making the rights of the obligee differ depending on whether the breach of contract by the obligor is delay in performance on the one hand (paragraph (1)), or non-performance or defective performance other than delay on the other (paragraph (2)). In all cases the obligee should be entitled to select his remedy.

28. As regards an agreed sum to be recoverable or forfeited on defective performance other than delay (paragraph (2)) the USSR suggests that it will be useful to specify that when the obligee elects to require performance (rather than claim the agreed sum), he retains the right to the recovery of losses sustained as a result of the defective performance.

29. Spain notes that paragraph (2) must deal with the following four cases:

(a) When the agreed sum is fixed with a view to covering non-performance, and non-performance occurs;

(b) When the agreed sum is fixed with a view to covering defective performance, and defective performance occurs;

(c) When the agreed sum is fixed with a view to covering non-performance, but defective performance occurs; and

(d) When the agreed sum is fixed with a view to covering defective performance, but non-performance occurs.

¹⁰ Article 1.105

¹¹ Article 1.155

¹² See A/CN.9/218, para. 38 (reproduced in this volume, part two, I, A).

30. As regards case (a), Spain approves of the solution adopted in paragraph (2). As regards case (b), it observes that the proper solution (although not explicitly stated in the paragraph) is that the obligee should be entitled to recover or forfeit the agreed sum as a supplement to the defective performance he has received. As regards case (c), it notes that it is logical to suppose that the agreed amount would exceed the losses suffered by the obligee from the defective performance. To permit recovery of the agreed sum in full in such a case would be contrary to "economic public order", and accordingly Spain proposes an amendment to article G to deal with this case.¹³ As regards case (d), article F would apply, as contemplated in the commentary,¹⁴ and the obligee's rights would be supplemented by the right to damages given by that article.

G. DRAFT CONVENTION AND DRAFT MODEL LAW ARTICLE F

31. Sweden notes that in this article the principle that it is justifiable in certain circumstances to recover damages in addition to the agreed sum is accepted. However, such recovery of damages deprives the agreement of certainty as to the recoverable sum. Assuming, however, that this principle is to be accepted, Sweden observes that the circumstances specified in the article as justifying such recovery are too restricted. Other circumstances (e.g. gross negligence on the part of the obligor) should also be relevant.

32. The Republic of Korea notes that, while under article G, paragraph (2), only a court or arbitral tribunal can vary the agreement of the parties on the amount recoverable, article F might be construed as giving the obligee the power to vary the amount recoverable. If this construction is correct, article F should be modified, as the obligee should not have the power of unilateral variation.

H. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE C

33. Sweden notes that in paragraph (2) of this article the principle that it is justifiable to reduce the agreed sum in certain circumstances is accepted. However, the circumstances regarded therein as justifying a reduction are too restricted. All the circumstances relating to the contract, including both the circumstances at the time of conclusion of the contract and at a later stage, should be taken into consideration.

34. Argentina observes that the principle contained in paragraph (1) is important for preserving certainty in international trade transactions. Accordingly, paragraph (2), which contains an exception to that principle, should be construed restrictively. Reduction of the agreed sum should

¹³ See para. 35 below.

¹⁴ See A/CN.9/218, para. 44 (reproduced in this volume, part two, I, A).

only be permitted when the disproportion between the loss suffered by the obligee and the agreed sum is such that by recovering the agreed sum the obligee will obtain an obvious, unequivocal and clearly disproportionate advantage without any justifying cause.

35. In order to give effect to its suggestion in regard to article E,¹⁵ Spain suggests that article G should be re-drafted as follows:

"(1) The agreed sum shall not be reduced by a court or arbitral tribunal except as provided in the following paragraph.

"(2) The agreed sum may be reduced if it is shown to be grossly disproportionate in relation to the loss that has been suffered by the obligee, and if the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee. Specifically, it can be reduced when, after it has been fixed in contemplation of (total) non-performance, defective performance other than delay occurs."

[A/CN.9/219/Add. 1]*

Introduction

1. Subsequent to the issuance of the analysis of responses of Governments and international organizations (A/CN.9/219),** responses were received from the Governments of the Federal Republic of Germany, Hungary, the Netherlands and Norway. These responses are analysed below.

Part I. Appropriate form for the uniform rules

A. CONVENTION

2. The Netherlands considers a convention to be the most appropriate form for the uniform rules, as this form would be the most effective for unification. The Federal Republic of Germany is of the view, however, that a convention is not an appropriate form. Many States, including the Federal Republic of Germany, have national legislation which creates a fair balance between the rights of obligors and obligees under liquidated damages and penalty clauses, taking into account the circumstances prevailing in the particular States (e.g. the need for consumer protection). It would be very difficult for States to displace this national legislation by the uniform rules, and accordingly the Federal Republic of Germany is doubtful if a convention would be ratified by a sufficiently large number of States.

* 23 June 1982.

** 28 May 1982.

¹⁵ See para. 30 above.

B. MODEL LAW

3. Hungary considers a model law to be the most appropriate form for the uniform rules. A model law is best suited to the nature of the uniform rules, and it can be incorporated in the national legislation in harmony with such legislation. The Federal Republic of Germany is of the view, however, that if this form were adopted, the uniform rules would be embodied in the national legislation only very incompletely and with substantial alterations, and no effective unification would result.

C. UNCITRAL RULES (GENERAL CONDITIONS)

4. The Federal Republic of Germany and Norway consider general conditions to be the most appropriate form. The Federal Republic of Germany notes that in this form the uniform rules would help the parties in drafting their contracts by giving uniform criteria according to which, in the case of total or partial failure to perform the contract, the relation of claims for performance on the one hand and claims for penalties or damages on the other can be adjusted. Norway notes that the form of general conditions will make it possible to simplify the text, in particular regarding its scope of application. This form will also facilitate a clearer text for article F (because the rule therein can be linked to the intention of the parties) and for article G (because questions of modification based on the validity of the contract can be left to the applicable law).

Part II. Comments on specific articles

A. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE A, PARAGRAPH (1)

5. The Netherlands proposes the deletion of the term "agreed" appearing before the phrase "sum of money" as it is not necessary that the parties specify an exact sum in a liquidated damages or penalty clause. It is sufficient that it should be possible to determine the sum on the basis of the agreement.

6. Norway proposes clarification that the uniform rules do not apply to any guarantee by a third party (e.g. bank or other credit institution).

B. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE E, PARAGRAPH (2)

7. The Netherlands and Norway propose the modification of this paragraph to clarify that when the last clause of this paragraph¹ applies, the effect is not to impose a restriction on the obligee's choice between recovery of per-

¹ "... unless the agreed sum cannot reasonably be regarded as a substitute for performance."

formance, or recovery or forfeiture of the agreed sum, but to remove the restriction on concurrent recovery of performance and recovery or forfeiture of the agreed sum. To secure this clarification, Norway suggests the following re-drafting:

"(2) Where the agreed sum is to be recoverable or forfeited on non-performance, or defective performance other than delay, the obligee is entitled to recover or forfeit the agreed sum. However, he is not so entitled where performance has been effected, unless the agreed sum cannot reasonably be regarded as a substitute for performance."²

C. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE F

8. The Netherlands notes that it is unnecessary for this article to state that the obligee is entitled, in respect of a failure of performance, to recover the agreed sum. The article should only state that, in the circumstances specified therein,³ the obligee is entitled to damages to the extent of the loss not covered by the agreed sum.

9. Norway notes that liquidated damages or penalty clauses may be formulated for different purposes:

(a) As a clause exclusively providing a penalty, independent of damages; or

(b) As a clause providing for liquidated damages, limiting the damages to a maximum amount; or

(c) As a clause providing minimum damages, but not preventing the recovery of excess damages.

10. Norway notes that the article as presently drafted attempts to provide a single rule in respect of clauses with these different purposes, and that this leads to unsatisfactory results. Norway proposes that the rule to be applied under the article should be made to depend on the intention of the parties in formulating the clause. The fact that the need for additional damages may differ according to whether the breach of contract consists of delay, non-performance or defective performance should also be taken into account.

11. Norway accordingly makes the following suggestions:

(a) That the last sentence of the article⁴ be deleted; or

(b) That the article should be re-drafted as follows:

"Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or for-

feited occurs, the obligee is entitled, in respect of the failure, to recover or forfeit the sum, and is entitled to damages for loss not intended to be covered by the agreed sum (e.g. where the sum is not to be regarded only as a penalty independent of any loss or as liquidated maximum damages)."⁵

The following sentence may also be added if considered necessary:

"However, where the agreed sum must be regarded as part of the damages, the obligee may claim damages to the extent of the loss not actually covered by the sum."⁶

D. DRAFT CONVENTION AND DRAFT MODEL LAW, ARTICLE G

12. The Federal Republic of Germany notes that, if the form of general conditions is adopted for the uniform rules, the present drafting of this article may be inappropriate. The national legislation of many States, including that of the Federal Republic of Germany, contains mandatory provisions providing for review by the courts of liquidated damages and penalty clauses in certain cases. Such legislation would, to some degree at least, conflict with the provisions of article G. Accordingly, the Federal Republic of Germany suggests that it should be expressly provided, either in article G or elsewhere in the uniform rules, that when such mandatory provisions are inconsistent with the uniform rules, the former is to prevail.

13. Norway notes that the difficulties encountered in article G will be reduced if the uniform rules are given the form of general conditions, which will be subject to mandatory law e.g. rules on validity or on unconscionable contracts. Norway proposes that, if this form is to be chosen, paragraph (1) of this article should be re-drafted as follows:

"(1) The agreed sum shall not be reduced by a court or arbitral tribunal, unless to the extent that the agreement may be modified according to the rules on validity of contracts or on unconscionable contracts under the law applicable"⁷

14. The Netherlands proposes that the uniform rules should state that parties cannot by agreement vary the provisions of this article. This might be done in a new paragraph added to this article, or in a new article specifying which articles the parties can vary (articles D to F) and which they cannot (articles A to C and G). If a new article is formulated, the provisions in articles D to F enabling the parties to modify those articles could be deleted.

15. The Netherlands notes that the provisions in this article defining the conditions under which an agreed sum can be reduced may be inappropriate for cases where the

² New wording in italics.

³ "... but only if he can prove that his loss grossly exceeds the agreed sum."

⁴ "... but only if he can prove that his loss greatly exceeds the agreed sum."

⁵ New wording in italics.

⁶ *Idem*.

⁷ *Idem*.

function of the agreed sum is not to compensate the obligee for loss he might suffer by the obligor's non-performance, but to coerce the obligor to perform. For instance, where the agreed sum was stipulated to coerce the obligor to perform an obligation, non-performance of which would not result in appreciable financial loss to the obligee, the obligor may be able to obtain a reduction, which in the circumstances would be inappropriate.

16. The Netherlands suggests that, before an agreed sum can be reduced under paragraph (2) of this article, both conditions specified in the paragraph⁸ must be satisfied, and that the paragraph should clearly state this require-

⁸ "If it is shown to be grossly disproportionate in relation to the loss that has been suffered by the obligee, and if the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee."

ment. The Federal Republic of Germany and Norway, however, are of the view that paragraph (2) should be modified to enable reduction of the agreed sum if only one of the conditions is satisfied. The Federal Republic of Germany notes that to require both conditions to be satisfied excessively restricts the scope of application of the article to a few cases which in practice rarely occur. Norway suggests the following re-drafting of the paragraph:

"(2) However, the agreed sum may be reduced if it is shown to be *unreasonably* disproportionate in relation to the loss suffered by the obligee, *or* if the agreed sum cannot reasonably be regarded *to reflect* a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee."⁹

⁹ New wording in italics.

II. INTERNATIONAL PAYMENTS

A. International negotiable instruments*

1. REPORT OF THE WORKING GROUP ON INTERNATIONAL NEGOTIABLE INSTRUMENTS ON THE WORK OF ITS ELEVENTH SESSION (NEW YORK, 3-14 AUGUST) (A/CN.9/210)**

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Introduction

1. In response to decisions by the United Nations Commission on International Trade Law (UNCITRAL), the Secretary-General prepared a draft Uniform Law on International Bills of Exchange and International Promissory Notes, with commentary (A/CN.9/WG.IV/WP.2).¹ At its fifth session (1972), the Commission established a Working Group on International Negotiable Instruments. The Commission requested that the above draft Uniform Law be submitted to the Working Group and entrusted the Working Group with the preparation of a final draft.²

2. The Working Group held its first session in Geneva in January 1973. At the session the Working Group con-

sidered articles of the draft Uniform Law relating to transfer and negotiation (articles 12-22), the rights and liabilities of signatories (articles 27-40), and the definition and rights of a "holder" and a "protected holder" (articles 5-6 and 23-36).³

3. The second session of the Working Group was held in New York in January 1974. At that session the Working Group continued consideration of articles of the draft Uniform Law relating to the rights and liabilities of signatories (articles 41-45) and considered articles in respect of presentment, dishonour and recourse, including the legal effects of protest and notice of dishonour (articles 46-62).⁴

4. The third session was held in Geneva in January 1975. At that session the Working Group continued its consideration of the articles concerning notice of dishonour (articles 63-66). The Group also considered provisions regarding the sum due to a holder and to a party secondarily liable who takes up and pays the instrument (articles 67-68) and

* For consideration by the Commission see Report, chapter III, A (part one, A, above).

** 16 February 1981.

¹ Report of the United Nations Commission on International Trade Law on the work of its fourth session, *Official Records of the General Assembly, Twenty-sixth Session, Supplement No. 17* (A/8417), para. 35 (Yearbook . . . 1971, part one, II, A). For a brief history of the subject up to the fourth session of the Commission, see A/CN.9/53, paras. 1 to 7. See also Report of the United Nations Commission on International Trade Law on the work of its fifth session, *Official Records of the General Assembly, Twenty-seventh Session, Supplement No. 17* (A/8717), para. 61 (2) (c) (Yearbook . . . 1972, part one, II, A).

² *Ibid.*, para. 61 (1) (a).

³ Report of the Working Group on International Negotiable Instruments on the work of its first session (Geneva, 8-19 January 1973), A/CN.9/77 (Yearbook . . . 1973, part two, II, 1).

⁴ Report of the Working Group on International Negotiable Instruments on the work of its second session (New York, 7-18 January 1974), A/CN.9/86 (Yearbook . . . 1974, part two, II, 1).

provisions regarding the circumstances in which a party is discharged of his liability (articles 69-78).⁵

5. The fourth session of the Working Group was held in New York in February 1976. At that session the Working Group considered articles 79 to 86 and articles 1 to 11 of the draft Uniform Law, thereby completing its first reading of the draft text of the law.⁶

6. At the fifth session of the Working Group, held in New York in July 1977, the Working Group commenced its second reading of the draft Uniform Law (retitled at that session "draft Convention on International Bills of Exchange and International Promissory Notes") and considered articles 1 to 24.⁷

7. The sixth session of the Working Group was held in Geneva in January 1978. At that session the Working Group, continuing its second reading of the text of the draft Convention on International Bills of Exchange and International Promissory Notes, considered articles 5 and 6 and articles 24 to 53.⁸

8. The seventh session of the Working Group was held in New York in January 1979. At that session the Working Group, continuing its second reading of the text of the draft Convention on International Bills of Exchange and International Promissory Notes, considered articles 24 and 53 to 70.⁹

9. The eighth session of the Working Group was held in Geneva in September 1979. At that session the Working Group, continuing its second reading of the text of the draft Convention on International Bills of Exchange and International Promissory Notes, considered articles 1, 5, 9, 11 and 70 to 86.¹⁰ In response to a decision by the Commission at its twelfth session,¹¹ the Working Group, at its eighth session, requested the Secretariat to commence preparatory work in respect of uniform rules applicable to international cheques.

10. The ninth session of the Working Group was held in New York in January 1980. At that session the Working Group, continuing its third reading of the text of the draft

Convention on International Bills of Exchange and International Promissory Notes, considered articles 13 to 85 and articles 5 (10) in connection with article 22.¹² The Working Group also considered articles 1 to 30 of the uniform rules applicable to international cheques as drafted by the Secretariat (A/CN.9/WG.IV/WP.15).

11. The tenth session of the Working Group was held at Vienna from 5 to 16 January 1981. At that session the Working Group continued its consideration of the Uniform Rules applicable to International Cheques as drafted by the Secretariat, and considered draft articles 34, X, 41 to 45, 53 to 66 bis, 67 to 68, 70, 70 bis, 71 and 72, 74, 74 bis, 74 ter, 74 quater, 78 to 85 and A to F (crossed cheques). It also considered legal issues arising outside the cheque, post-dated cheques and certain other issues.¹³

12. The Working Group held its eleventh session in New York from 3 to 14 August 1981. The Working Group consists of the following eight members of the Commission: Chile, Egypt, France, India, Nigeria, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America. All members of the Working Group were represented at the eleventh session. The session was also attended by observers of the following States: Argentina, Australia, Austria, Brazil, China, Colombia, Cuba, Czechoslovakia, El Salvador, Gabon, Italy, Japan, Kenya, Malaysia, Philippines, Portugal, Republic of Korea, Romania, Suriname, Sweden, Switzerland, Trinidad and Tobago, Turkey and Venezuela, and by observers from the following international organizations: International Monetary Fund, Hague Conference on Private International Law, European Banking Federation and International Chamber of Commerce.

13. The Working Group elected the following officers:

Chairman: Mr. René Roblot (France)
Rapporteur: Mr. Ibrahim Youssri (Egypt)

14. The Working Group had before it the following documents: * provisional agenda (A/CN.9/WG.IV/WP.20), two notes by the Secretariat setting forth draft articles of the Uniform Rules applicable to International Cheques (A/CN.9/WG.IV/WP.15 and 19), a note by the Secretariat setting forth certain revised draft articles of the Uniform Rules applicable to International Cheques (A/CN.9/WG.IV/WP.21), a note by the Secretariat setting forth certain revised draft articles of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/WG.IV/WP.22), a note by the observer of the Hague Conference on Private International Law on

⁵ Report of the Working Group on International Negotiable Instruments on the work of its third session (Geneva, 6-17 January 1975), A/CN.9/99 (Yearbook ... 1975, part two, II, 1).

⁶ Report of the Working Group on International Negotiable Instruments on the work of its fourth session (New York, 2-12 February 1976), A/CN.9/117 (Yearbook ... 1976, part two, II, 1).

⁷ Report of the Working Group on International Negotiable Instruments on the work of its fifth session (New York, 18-29 July 1977), A/CN.9/141 (Yearbook ... 1978, part two, II, A).

⁸ Report of the Working Group on International Negotiable Instruments on the work of its sixth session (Geneva, 3-13 January 1978), A/CN.9/147 (Yearbook ... 1978, part two, II, B).

⁹ Report of the Working Group on International Negotiable Instruments on the work of its seventh session (New York, 3-12 January 1979), A/CN.9/157 (Yearbook ... 1979, part two, II, A).

¹⁰ Report of the Working Group on International Negotiable Instruments on the work of its eighth session (Geneva, 3-14 September 1979), A/CN.9/178 (Yearbook ... 1980, part two, III, A).

¹¹ Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 44 (Yearbook ... 1979, part one, II, A).

* The documents are reproduced in this volume, part two, II, A, 2, (a) to (h).

¹² Report of the Working Group on International Negotiable Instruments on the work of its ninth session (New York, 2-11 January 1980), A/CN.9/181 (Yearbook ... 1980, part two, III, B).

¹³ Report of the Working Group on International Negotiable Instruments on the work of its tenth session (Vienna, 5-16 January 1981), A/CN.9/196 (Yearbook ... 1981, part two, II, A).

questions not dealt with in the draft Convention (A/CN.9/WG.IV/WP.23), the text of draft articles of the draft Convention on International Bills of Exchange and International Promissory Notes as prepared by a Drafting Group convened by the Secretariat (A/CN.9/WG.IV/WP.24 and Add. 1-2), the text of draft articles of the Uniform Rules applicable to International Cheques as prepared by the same Drafting Group (A/CN.9/WG.IV/WP.25 and Add. 1), and the reports of the ninth and tenth sessions of the Working Group (A/CN.9/181 and 196).

Deliberations and Decisions

15. The Working Group continued its consideration of the draft Uniform Rules applicable to International Cheques as set forth in documents A/CN.9/WG.IV/WP.15, 19 and 21. The Group decided to change the title of the draft text to "Draft Convention on International Cheques". At the present session the Working Group also considered certain articles of the draft Convention on International Bills of Exchange and International Promissory Notes.

16. The Working Group considered and adopted with some modifications the complete text of the draft Convention on International Cheques and of the draft Convention on International Bills of Exchange and International Promissory Notes, as revised by the Drafting Group (A/CN.9/WG.IV/WP.24 and Add. 1-2 and WP.25 and Add. 1).^{*} The final text of the draft Convention on International Cheques is set forth in document A/CN.9/212** and of the draft Convention on International Bills of Exchange and International Promissory Notes in A/CN.9/211.***

17. The Working Group thereby completed the task entrusted to it by the Commission to prepare a draft Convention on International Bills of Exchange and International Promissory Notes, and a draft Convention on International Cheques. The Working Group took note of the decision of the Commission, at its fourteenth session, to request the Secretary-General to circulate the texts, together with a commentary, to all Governments and interested international organizations for their comments.¹⁴

18. The Working Group took note of the decision of the Commission, at its fourteenth session, to request the Working Group to consider various possibilities in regard to the formulation of a unit of account of constant value, which would serve as a point of reference in international conventions for expressing amounts in monetary terms, and to prepare a text if possible.¹⁵

19. The Working Group decided to hold its next session (the twelfth session) at Vienna from 4 to 15 January 1982.

20. At the close of its session, the Working Group expressed its appreciation to the observers of States and to representatives of international organizations who attended the session.

I. DRAFT CONVENTION ON INTERNATIONAL CHEQUES

Draft articles 1 to 85, A to F, a and β ¹⁶

21. The Working Group decided to examine in second reading draft articles 1 to 85, A to F, a and β of the draft Convention on International Cheques.

Article 1, paragraph (1)

22. The text of article 1, paragraph (1), as considered by the Working Group, is as follows:

"This Convention applies to international cheques."

23. The Working Group adopted this paragraph.

Article 1, paragraph (2)

24. The text of article 1, paragraph (2), as considered by the Working Group, is as follows:

"An international cheque is a written instrument which

"(a) Contains, in the text thereof, the words 'international cheque (Convention of . . .)';

"(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order or to bearer;

"(c) Is drawn on a banker or on a person or institution assimilated by the applicable law to a banker;

"(d) Is payable on demand;

"(e) Is dated;

"(f) Shows that at least two of the following places are situated in different States:

"(i) The place where the cheque is drawn;

"(ii) The place indicated next to the name or the signature of the drawer;

"(iii) The place indicated next to the name of the drawee;

¹⁶ Each draft article is numbered to correspond to the draft article in the draft Convention on International Bills of Exchange and International Promissory Notes which relates to the same or a similar issue. Accordingly, when a draft article in that draft Convention has no relation to cheques, there is an interruption in the numbering sequence of the draft articles set forth here and when a draft article here has no relation to bills of exchange or promissory notes, it is identified by a letter (e.g. articles A to F on crossed cheques).

^{*} Reproduced in this volume, part two, II, A, 2, (d), (e), (f).

^{**} Reproduced in this volume, part two, II, A, 5.

^{***} Reproduced in this volume, part two, II, A, 3.

¹⁴ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 22.

¹⁵ *Ibid.*, para. 32.

"(iv) The place indicated next to the name of the payee;

"(v) The place of payment;

"(g) Is signed by the drawer."

25. The Working Group adopted subparagraphs (a) and (b).

26. As regards subparagraph (c), it was observed that the words "by the applicable law" introduced an element of uncertainty, in that it was not immediately clear which test should be used to determine that law. The Working Group decided to delete these words since they were superfluous.

27. As regards subparagraph (d), the Working Group reconsidered whether the requirement should be retained. After deliberation, the Group decided to maintain its decision taken at its ninth session (A/CN.9/181, paragraphs 162-163),* and therefore to delete as a formal requisite the reference to a cheque being payable on demand. Instead, the Group decided that the rule that a cheque be payable on demand should be dealt with in article 9 of the draft Convention on International Cheques.

28. The Working Group adopted subparagraphs (e), (f) and (g).

Article 1, paragraph (3)

29. The text of article 1, paragraph (3), as considered by the Working Group, is as follows:

"Proof that the statements referred to in paragraph (2) (f) of this article are incorrect does not affect the application of this Convention."

30. The Working Group adopted this paragraph.

Article 3

31. The text of article 3, as considered by the Working Group, is as follows:

"This Convention applies without regard to whether the places indicated on an international cheque pursuant to paragraph (2) (f) of article 1 are situated in Contracting States."

32. The Observer of the Hague Conference on Private International Law expressed the view that the Convention should apply only when the place of payment was situated in a Contracting State. The Working Group, after discussion, adopted article 3 without change.

Article 4

33. The text of article 4, as considered by the Working Group, is as follows:

"In the interpretation and application of this Convention, regard is to be had to its international character and to the need to promote uniformity."

34. The Working Group adopted this article.

Article 5, paragraphs (1), (2), (3), (4) and (5)

35. The text of article 5, paragraphs (1), (2), (3), (4) and (5), as considered by the Working Group, is as follows:

"(1) 'Cheque' means an international cheque governed by this Convention;

"(2) 'Drawee' means the banker on whom a cheque is drawn;

"(3) 'Payee' means the person in whose favour the drawer directs payment to be made;

"(4) 'Bearer' means a person in possession of a cheque payable to bearer or endorsed in blank;

"(5) 'Holder' means the person referred to in article 13 bis."

36. The Working Group adopted these paragraphs.

Article 5, paragraph (6)

37. The text of article 5, paragraph (6), as considered by the Working Group, is as follows:

"'Protected holder' means a holder of a cheque which, when he became a holder, was complete and regular on its face and not overdue [in accordance with article 53 (f)], provided that, at that time, he was without knowledge of any claim to or defence upon the cheque referred to in article 24 or of the fact that it was dishonoured by non-payment."

38. The Working Group noted that the Drafting Group had prepared a modified draft text of the definition of the term "protected holder" for the draft Convention on International Bills of Exchange and International Promissory Notes. This text was as follows:

"'Protected holder' means the holder of an instrument which, when he became a holder, was completed and regular on its face, provided that:

"(a) He was, at that time, without knowledge of circumstances giving rise to a claim to or defence upon the instrument referred to in article 24 or of the fact that it was dishonoured by non-acceptance or non-payment;

"(b) The time-limit provided by article 53 for presentment of that instrument for payment had not then expired."

39. It was observed that the words "without knowledge of circumstances giving rise to a claim to or defence upon the instrument" might be interpreted too widely. It was suggested that mere knowledge of such circumstances should not necessarily prevent a holder from being a protected

* Yearbook ... 1980, part two, III, B.

holder. The Working Group, after discussion, agreed with this observation, and decided to replace the above-quoted words by the words "without knowledge of a claim to or defence upon the instrument."

40. As a result of this decision, the Working Group adopted the following text of paragraph (6) of the draft Convention on International Cheques:

"'Protected holder' means the holder of a cheque which, when he became a holder, was complete and regular on its face, provided that:

"(a) He was, at that time, without knowledge of a claim to or defence upon the cheque referred to in article 24 or of the fact that it was dishonoured by non-payment;

"(b) The time-limit provided by article 53 for presentment of the cheque for payment had not then expired."

Article 5, paragraph (7)

41. The text of article 5, paragraph (7), as considered by the Working Group, is as follows:

"'Party' means a person who has signed a cheque."

42. The Working Group noted that the Drafting Group had proposed a modified draft text of the definition of the term "party" for the draft Convention on International Bills of Exchange and International Promissory Notes, which reads as follows:

"'Party' means any person who has signed an instrument [as drawer, maker, acceptor, endorser or guarantor].

43. The Working Group decided to use a similar approach to the definition of the term "party" in the draft Convention on International Cheques and adopted the following text:

"'Party' means any person who has signed a cheque as drawer, endorser or guarantor."

Article 5, paragraph (8)

44. The text of article 5, paragraph (8), as considered by the Working Group, is as follows:

"'Forged signature' includes a signature which is forged by the wrongful or unauthorized use of a stamp, symbol, facsimile, perforation or other means by which a signature may be made in accordance with article 27."

45. The Working Group adopted this paragraph.¹⁷

Article 6

46. The text of article 6, as considered by the Working Group, is as follows:

¹⁷ As to new paragraph (9) of article 5, see discussion and decision below, paras. 222-229.

"For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence."

47. The Working Group adopted this article.

Article 7

48. The text of article 7, as considered by the Working Group, is as follows:

"The sum payable by a cheque is deemed to be a definite sum although the cheque states that it is to be paid

"(a) With interest;

"(b) According to a rate of exchange indicated on the cheque or to be determined as directed by the cheque; or

"(c) In a currency other than the currency in which the amount of the cheque is expressed."

49. The Working Group re-affirmed its view that a stipulation on a cheque that it is to be paid with interest should be without any legal effect on the cheque. Accordingly, the Working Group decided to delete paragraph (a), and to add a new article 7 *bis* worded as follows:

"Any stipulation on a cheque that it is to be paid with interest is deemed not to have been written on the cheque."

Article 8

50. The text of article 8, as considered by the Working Group, is as follows:

"(1) If there is a discrepancy between the amount of the cheque expressed in words and the amount expressed in figures, the sum payable is the amount expressed in words.

"(2) If the amount of the cheque is expressed in a currency having the same description as that of at least one other State than the State where payment is to be made as indicated on the cheque and the specified currency is not identified as the currency of any State, the currency is to be considered as the currency of the State where payment is to be made.

"(3) If a cheque states that it is to be paid with interest, without specifying the date from which interest is to run, interest runs [from the date of the cheque] [from the date on which the cheque is issued].

"(4) A stipulation on a cheque stating that it is to be paid with interest is to be disregarded unless it indicates the rate at which interest is to be paid."

51. As a consequence of the decision reached under article 7, the Working Group decided to delete paragraphs (3) and (4), and to adopt paragraphs (1) and (2).

Article 9

52. The text of article 9, as considered by the Working Group, is as follows:

"A cheque is payable on demand:

"(a) If it states that it is payable on demand or at sight or on presentment or if it contains words of similar import, or

"(b) If no time of payment is expressed."

53. Pursuant to its decision taken in respect of article 1 (2) (d), deleting the reference to the requirement that a cheque "is payable on demand", the Working Group decided to revise article 9 to read as follows:

"A cheque is always payable on demand. It is so payable:

"(a) If it states that it is payable on demand or at sight or on presentment or if it contains words of similar import, or

"(b) If no time of payment is expressed, or

"(c) Even though it is stated on the cheque that it is payable at a definite time."

Articles 10, 11, 13, new article, 13 bis and 15

54. The text of articles 10, 11, 13, new article, 13 bis and 15, as considered by the Working Group, is as follows:

"Article 10

"(1) A cheque may

"(a) Be drawn by the drawer on himself or be drawn payable to his order;

"(b) Be drawn by two or more drawers;

"(c) Be payable to two or more payees.

"(2) If a cheque is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the cheque may exercise the rights of a holder. In any other case the cheque is payable to all of them and the rights of a holder can only be exercised by all of them."

"Article 11

"(1) An incomplete cheque which satisfies the requirements set out in subparagraphs (a) and (g) of paragraph (2) but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) of article 1 may be completed and the cheque so completed is effective as a cheque.

"(2) When such a cheque is completed otherwise than in accordance with agreements entered into

"(a) A party who signed the cheque before the completion may invoke the non-observance of the agree-

ment as a defence against a holder, provided the holder had knowledge of the non-observance of the agreement when he became a holder;

"(b) A party who signed the cheque after the completion is liable according to the terms of the cheque so completed."

"Article 13

"A cheque is transferred

"(a) By endorsement and delivery of the cheque by the endorser to the endorsee; or

"(b) By mere delivery of the cheque if it is drawn payable to bearer or if the last endorsement is in blank."

"New article

"(1) An endorsement must be written on the cheque or on a slip affixed thereto (*allonge*). It must be signed.

"(2) An endorsement may be made

"(a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the cheque is payable to any person in possession thereof;

"(b) Special, by a signature accompanied by an indication of the person to whom the cheque is payable."

"Article 13 bis

"(1) A person is a holder if he is

"(a) The bearer of a cheque; or

"(b) The payee in possession of the cheque; or

"(c) In possession of a cheque

"(i) Which has been endorsed to him; or

"(ii) On which the last endorsement is in blank; and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

"(2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.

"(3) A person is not prevented from being a holder by the fact that the cheque was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon, the cheque."

"Article 15

"The holder of a cheque on which the last endorsement is in blank may

"(a) Further endorse the cheque either in blank or to a specified person; or

"(b) Convert the blank endorsement into a special endorsement by indicating therein that the cheque is payable to himself or to some other specified person; or

"(c) Transfer the cheque in accordance with paragraph (b) of article 13."

55. The Working Group adopted these articles.

Article 16

56. The text of article 16, as considered by the Working Group, is as follows:

"[When the drawer or an endorser has inserted in the cheque or in the endorsement such words as 'not negotiable', 'not transferable', 'not to order', 'pay (X) only', or words of similar import, the transferee does not become a holder except for purposes of collection.]"

57. After deliberation, the Working Group decided to insert after the words "the drawer" the words "of a cheque payable to a payee or his order", in order to make clear that this provision did not apply to a cheque payable to bearer.

58. The Working Group noted that the Drafting Group had proposed the following draft text of article 16 of the draft Convention on International Bills of Exchange and International Promissory Notes:

"When the drawer, or the maker has inserted in the instrument, or an endorser in his endorsement, such words as 'not negotiable', 'not transferable', 'not to order', 'pay (X) only', or words of similar import, the transferee does not become a holder except for purposes of collection."

59. The Working Group decided to use similar wording for the draft Convention on International Cheques, and adopted the following text:

"When the drawer of a cheque payable to a payee or to his order has inserted in the cheque, or an endorser in his endorsement, such words as 'not negotiable', 'not transferable', 'not to order', 'pay (X) only', or words of similar import, the transferee does not become a holder except for purposes of collection."

Articles 17, 18, 19 and 20

60. The text of articles 17, 18, 19 and 20, as considered by the Working Group, is as follows:

"Article 17

"(1) A conditional endorsement transfers the cheque irrespective of whether the condition is fulfilled.

"(2) A claim to or a defence upon the cheque based on the fact that the condition was not fulfilled may not be raised except by the party who endorsed conditionally against his immediate transferee."

"Article 18

"An endorsement in respect of a part of the sum due under the cheque is ineffective as an endorsement."

"Article 19

"Where there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the cheque."

"Article 20

"(1) When an endorsement contains the words 'for collection', 'for deposit', 'value in collection', 'by procuration', 'pay any bank', or words of similar import, authorizing the endorsee to collect the cheque (endorsement for collection), the endorsee

"(a) May only endorse the cheque for purposes of collection;

"(b) May exercise all the rights arising out of the cheque;

"(c) Is subject to all claims and defences which may be set up against the endorser;

"(2) The endorser for collection is not liable upon the cheque to any subsequent holder."

61. The Working Group adopted these articles.¹⁸

Article 21

62. The text of article 21, as considered by the Working Group, is as follows:

"(1) The holder of a cheque may transfer it to a prior party in accordance with article 13; nevertheless, in the case where the transferee was a prior holder of the cheque, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

"(2) The endorsement to the drawee operates only as an acknowledgement that the endorser has received from the drawee the sum payable by the cheque [except in the case where the drawee has several establishments and the endorsement is made in favour of an establishment other than that on which the cheque has been drawn]."

63. The Working Group decided to delete the square brackets from paragraph (2) and adopted this article.

Article 21 bis, paragraph (1)

64. The text of article 21 bis, paragraph (1), as considered by the Working Group, is as follows:

¹⁸ See, however, later amendment of article 17 (3) below, paras. 189-192.

"[(1) A cheque may be transferred in accordance with article 13 after the expiration of the period of time for presentment.]"

65. The Working Group noted that one justification for the rule contained in this paragraph was that under article 34 (1 *bis*) the drawer of a cheque remained liable on the cheque though the time-limit for due presentment had expired. The Working Group adopted paragraph (1).

Article 21 bis, paragraph (2)

66. The text of article 21 *bis*, paragraph (2), as considered by the Working Group is as follows:

"[(2) The transfer of a cheque in accordance with article 13 after the expiration of the period of time for presentment or after protest operates only as an assignment.]"

67. The Working Group considered that the transferee under paragraph (1) of this article was a holder, and for this reason paragraph (2) should not be retained.

Article 22, paragraph (1)

68. The Working Group had before it two variant texts of this paragraph which had been drafted by the Secretariat in response to a decision taken by the Working Group at its tenth session (A/CN.9/196, paragraph 118).^{*} The texts were directed towards the question whether article 22 should impose upon the drawee of a cheque who had paid the cheque to a forger a liability for damages to the person who had suffered loss because of the forged endorsement. These variant texts are as follows:

Variant A

"If an endorsement is forged, any person has against the forger, against the person who took the cheque directly from the forger and against the drawee who paid the cheque to the forger the right to recover compensation for any damage that he may have suffered because of the forgery."

Variant B

"If an endorsement is forged, any party has against the forger, against the person who took the cheque directly from the forger and against the drawee who paid the cheque to the forger with knowledge of the forgery the right to recover compensation for any damage that he may have suffered because of the forgery."

69. Opinions were divided on this issue. Under one view, the drawee should be subject to such liability whether he paid with or without knowledge of such forgery (variant A). Under another view, such liability should exist only where the drawee had paid with knowledge of the forged endorsement (variant B). The Working Group, after deliberation,

decided that the article should not deal with the liability of the payor bank, and that the article should expressly state that this liability did not fall within the coverage of the draft Convention.

70. The question was raised whether any liability should be imposed upon an endorsee to whom the cheque had been transferred by the forger for collection. The prevailing view was that article 22 should not deal with this aspect but that the person who had suffered loss because of the forgery could rely on such rights or remedies as he was entitled to under national law.

71. As a result of these decisions, the Working Group adopted the following text:

"(1) If an endorsement is forged, any party has against the forger, and against the person to whom the cheque was directly transferred by the forger, the right to recover compensation for any damage that he may have suffered because of the forgery.

"(1 *bis*) Except to the extent provided in articles C and F, the liability of a drawee who pays, or of an endorsee for collection who collects, a cheque on which there is a forged endorsement is not regulated by this Convention."¹⁹

Article 22, paragraph (2)

72. The text of article 22, paragraph (2), as considered by the Working Group, is as follows:

"[The drawer of the cheque has a similar right to compensation in circumstances where damage is caused to him by forgery of the signature of the payee.]"

73. The Working Group deleted the square brackets from this paragraph and adopted it.

Article 22, new paragraph (3)

74. In accordance with a decision taken at its ninth session (A/CN.9/181* paragraph 40), the Working Group decided to add the following paragraph, to be numbered as paragraph (3):

"For the purposes of this article, an endorsement placed on a cheque by a person in a representative capacity without authority has the same effects as a forged endorsement."

Article 23

75. The text of article 23, as considered by the Working Group, is as follows:

"(1) The holder of a cheque has all the rights conferred on him by this Convention against the parties to the cheque.

^{*} Yearbook . . . 1981, part two, II, A.

^{*} Yearbook . . . 1980, part two, III, B.

¹⁹ See, however, later amendment below, para. 239.

"(2) The holder is entitled to transfer the cheque in accordance with article 13."

76. The Working Group adopted this article.

Articles 24 and 25

77. The text of articles 24 and 25, as considered by the Working Group, is as follows:

"Article 24

"(1) A party may set up against a holder who is not a protected holder:

"(a) Any defence available under this Convention;

"(b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

"(c) Any defence to contractual liability based on a transaction between himself and the holder;

"(d) Any defence based on incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque, provided that such absence of knowledge was not due to negligence.

"(2) The rights to a cheque of a holder who is not a protected holder are subject to any valid claim to the cheque on the part of any person.

"(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the cheque unless:

"(a) Such third person asserted a valid claim to the cheque; or

"(b) Such holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft."

"Article 25

"(1) A party may not set up against a protected holder any defence except:

"(a) Defences under articles 27 (1), 28, 29 (1), 30 (2) (3), 34 (2), 41 (1) (2), 43 (4), 54, [55], [58], [60] and 79 of this Convention;

"(b) Defences based on the incapacity of such party to incur liability on the cheque;

"(c) Defences based on the fact that such party signed without knowledge that his signature made him a party to the cheque, provided that such absence of knowledge was not due to his negligence.

"(2) Except as provided in paragraph (3), the rights to a cheque of a protected holder are not subject to any claim to the cheque on the part of any person.

"(3) The rights of a protected holder are not free from any valid claim to, or any defence to liability upon, the cheque arising from the underlying transaction between himself and the party by whom the claim or defence is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that party.

"(4) The transfer of a cheque by a protected holder vests in any subsequent holder the rights to and upon the cheque which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to or a defence upon the cheque."

78. The Working Group decided to delete the reference to articles 58 and 60 in article 25 (1) (a). The reason for this deletion was that where a cheque had been presented for payment within the period of 120 days provided for in article 53 (f) and had not been protested upon dishonour, the defence of failure to protest which under article 60 discharges the drawer, the endorsers and their guarantors could not be raised against a protected holder to whom the instrument had been transferred after the dishonour.

79. The Working Group noted that the Drafting Group had proposed a modified draft text of articles 24 and 25 of the draft Convention on International Bills of Exchange and International Promissory Notes, which is as follows:

"Article 24

"(1) A party may set up against a holder who is not a protected holder:

"(a) Any defence available under this Convention;

"(b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

"(c) Any defence to contractual liability based on a transaction between himself and the holder;

"(d) Any defence based on incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

"(2) The rights to an instrument of a holder who is not a protected holder are subject to any valid claim to the instrument on the part of any person.

"(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

"(a) Such third person asserted a valid claim to the instrument; or

"(b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft."

"Article 25

"(1) A party may not set up against a protected holder any defence except:

"(a) Defences under articles 27 (1), 28, 29 (1), 30 (2, 3), 50, 55, 57, 60 and 79 of this Convention;

"(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;

"(c) Defences based on the incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

"(2) The rights to an instrument of a protected holder are not subject to any claim to the instrument on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that person."

"Article 25 bis

"(1) The transfer of an instrument by a protected holder vests in any subsequent holder the rights to and upon the instrument which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to or a defence upon the instrument.

"(2) If a party pays the instrument in accordance with article 67 and the instrument is transferred to him, such transfer does not vest in that party the rights to and upon the instrument which any previous protected holder had."²⁰

80. The Working Group decided to follow a similar approach, and adopted the following text:

"Article 24

"(1) A party may set up against a holder who is not a protected holder:

"(a) Any defence available under this Convention;

"(b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

"(c) Any defence to contractual liability based on a transaction between himself and the holder;

"(d) Any defence based on incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque, provided that such absence of knowledge was not due to his negligence.

"(2) The rights to a cheque of a holder who is not a protected holder are subject to any valid claim to the cheque on the part of any person.

"(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the cheque unless:

"(a) Such third person asserted a valid claim to the cheque; or

"(b) Such holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft."

"Article 25

"(1) A party may not set up against a protected holder any defence except:

"(a) Defences under articles 27 (1), 28, 29 (1), 30 (2, 3), 41 (1) (2), 43 (4), 54, 55 and 79 of this Convention;

"(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that party;

"(c) Defences based on the incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque provided that such absence of knowledge was not due to his negligence.

"(2) The rights to a cheque of a protected holder are not subject to any claim to the cheque on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that person."

"Article 25 bis

"(1) The transfer of a cheque by a protected holder vests in any subsequent holder the rights to and upon the cheque which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to or a defence upon the cheque.

"(2) If a party pays the cheque in accordance with article 67 and the cheque is transferred to him, such trans-

²⁰ Paragraph (2) sets forth a provision previously contained in article 68 (2).

fer does not vest in that party the rights to and upon the cheque which any previous protected holder had."

Article 26

81. The text of article 26, as considered by the Working Group, is as follows:

"Every holder is presumed to be a protected holder, unless the contrary is proved."

82. The Working Group adopted this article.

Article 27 and the article appended thereto

83. The text of article 27 and the article appended thereto, as considered by the Working Group, reads as follows:

"(1) Subject to the provisions of articles 28 and 30, a person is not liable on a cheque unless he signs it."

"(2) A person who signs in a name which is not his own is liable as if he had signed it in his own name."

"(3) A signature may be in handwriting or by facsimile, perforations, symbols or any other mechanical means."

"*"

Article . . .

"A Contracting State whose legislation requires that a signature on a cheque be handwritten may, at the time of signature, ratification or accession make a declaration to the effect that a signature placed on a cheque in its territory must be executed in handwriting."

84. The Working Group adopted article 27.

85. As regards the article appended to article 27, the principal question raised was the effect of a non-handwritten signature, made in the territory of a State having made the declaration, in the territory of a State in which article 27, paragraph (3) applied. The Working Group was agreed that in actions brought in the courts of the State having made the declaration, signatures on a cheque that were not in handwriting should not be given legal effect. On the other hand, there was no unanimity as to whether the courts of a State not having made the declaration would have to give effect to such signatures. Accordingly, the Working Group decided to retain the article, but to place it between square brackets.

Articles 28 and 29

86. The text of articles 28 and 29, as considered by the Working Group, is as follows:

"Article 28

"A forged signature on a cheque does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed

the cheque himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own."

"Article 29

"(1) If a cheque has been materially altered:

"(a) Parties who have signed the cheque subsequent to the material alteration are liable thereon according to the terms of the altered text;

"(b) Parties who have signed the cheque before the material alteration are liable thereon according to the terms of the original text. Nevertheless a party who has himself made, authorized, or assented to, the material alteration is liable on the cheque according to the terms of the altered text."

"(2) Failing proof to the contrary, a signature is deemed to have been placed on the cheque after the material alteration."

"(3) Any alteration is material which modifies the written undertaking on the cheque of any party in any respect."

87. The Working Group adopted these articles.

Article 30

88. The text of article 30, as considered by the Working Group, is as follows:

"(1) A cheque may be signed by an agent."

"(2) The name or signature of a principal placed on the cheque by an agent with his authority imposes liability on the principal and not on the agent."

"(3) The signature of an agent placed by him on a cheque without authority, or with authority to sign but not showing on the cheque that he is signing in a representative capacity for a named person, or showing on the cheque that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on such agent and not on the person whom the agent purports to represent."

"(4) The question whether a signature was placed on the cheque in a representative capacity may be determined only by reference to what appears on the cheque."

"(5) An agent who is liable pursuant to paragraph (3) and who pays the cheque has the same rights as the person for whom he purported to act would have had if that person had paid the cheque."

89. The Working Group noted that the Drafting Group had proposed a modified draft text of article 30 of the draft Convention on International Bills of Exchange and International Promissory Notes, which is as follows:

"(1) An instrument may be signed by an agent."

"(2) The signature of an agent placed by him on an instrument in a representative capacity for a named principal and with the authority of that principal, or the signature of a principal placed on the instrument by an agent with his authority, imposes liability on the principal and not on the agent.

"(3) A signature placed on an instrument by a person as agent but without authority to sign or exceeding his authority or by an agent with authority to sign but not showing on the instrument that he is signing in a representative capacity for a named person, or showing on the instrument that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.

"(4) The question whether a signature was placed on the instrument in a representative capacity may be determined only by reference to what appears on the instrument.

"(5) A person who is liable pursuant to paragraph (3) and who pays the instrument has the same rights as the person for whom he purported to act would have had if that person had paid the instrument."

90. The Working Group decided to follow a similar approach in the present article and adopted the following text:

"Article 30

"(1) A cheque may be signed by an agent.

"(2) The signature of an agent placed by him on a cheque in a representative capacity for a named principal and with the authority of that principal, or the signature of a principal placed on the cheque by an agent with his authority, imposes liability on the principal and not on the agent.

"(3) A signature placed on a cheque by a person as agent but without authority to sign or exceeding his authority or by an agent with authority to sign but not showing on the cheque that he is signing in a representative capacity for a named person, or showing on the cheque that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.

"(4) The question whether a signature was placed on the cheque in a representative capacity may be determined only by reference to what appears on the cheque.

"(5) A person who is liable pursuant to paragraph (3) and who pays the cheque has the same rights as the person for whom he purported to act would have had if that person had paid the cheque."

Article 30 bis

91. The text of article 30 *bis*, as considered by the Working Group, is as follows:

"The order to pay contained in a cheque does not of itself operate as an assignment of a right to payment existing outside the cheque."

92. The Working Group noted that the Drafting Group had proposed a modified draft text of article 30 *bis* of the draft Convention on International Bills of Exchange and International Cheques, which is as follows:

"The order to pay contained in a bill does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee outside the bill."

93. The Working Group decided to follow a similar approach in the present article subject to the deletion of the last three words of that text, and adopted the following text:

"The order to pay contained in a cheque does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee."

Article 34, paragraphs (1), (1 bis) and (1 ter)

94. The text of article 34, paragraphs (1), (1 *bis*) and (1 *ter*), as considered by the Working Group, is as follows:

"(1) The drawer engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder the amount of the cheque, and any interest and expenses which may be recovered under article 67 or 68.

"(1 *bis*) Delay in making presentment does not discharge the drawer of liability except to the extent of the loss suffered because of the delay.

"(1 *ter*) Delay in protesting a cheque for dishonour does not discharge the drawer of liability except to the extent of the loss suffered because of the delay."

95. The Working Group was agreed that it was inherent in paragraphs (1 *bis*) and (1 *ter*) that the liability of a drawer on a cheque would be liability for the amount of the cheque less the amount which he suffered as a loss because of delay in presentment. Thus, a drawer, whose liability on a cheque is for, say, SwF 1,000 and who, because of the delay in presentment, suffers a loss of say SwF 250 would be liable for SwF 750. The Working Group adopted these paragraphs.²¹

Article 34, paragraph (2)

96. The text of article 34, paragraph (2), as considered by the Working Group, is as follows:

²¹ See, however, later decision to delete paragraphs (1 *bis*) and (1 *ter*) below, para. 201.

"(2) The drawer may not exclude or limit his own liability by a stipulation on the cheque. Any such stipulation is without effect."

97. The Working Group adopted this paragraph.

Article X, paragraph (1)

98. The text of article X, paragraph (1), as considered by the Working Group, is as follows:

"(1) Any statement written on a cheque indicating certification, confirmation, acceptance, visa or any other equivalent expression has only the effect to ascertain the existence of funds and prevents the withdrawal of such funds by the drawer, or the use of such funds by the drawee for purposes other than payment of the cheque bearing such a statement, before the expiration of the time-limit for presentment."

99. The Working Group adopted this paragraph.

Article X, paragraphs (2) and (3)

100. The text of article X, paragraphs (2) and (3), as considered by the Working Group, is as follows:

"(2) However, a Contracting State may:

"(a) Provide that a drawee may accept a cheque; and

"(b) Determine the legal effects thereof.

"(3) An acceptance must be effected by the signature of the drawee accompanied by the word 'accepted' or words of similar import."

101. The Working Group adopted these paragraphs subject to redrafting them to form a single paragraph (2) as follows:

"(2) However, a Contracting State may provide that a drawee may accept a cheque and determine the legal effects thereof. Such acceptance must be effected by the signature of the drawee accompanied by the word 'accepted' or words of similar import."²²

102. The Working Group was of the view that the provisions of article X (2) should eventually be placed in that part of the Convention dealing with declarations and reservations and be drafted in the form of a declaration which a State upon ratifying or acceding to the Convention was permitted to make.

Articles 41, 42, 43, 44, 45 and 53

103. The text of articles 41, 42, 43, 44, 45 and 53, as considered by the Working Group, is as follows:

"Article 41

"(1) The endorser engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder the amount of the cheque, and any interest and expenses which may be recovered under article 67 or 68.

"(2) The endorser may exclude or limit his own liability by an express stipulation on the cheque. Such stipulation has effect only with respect to that endorser."

"Article 42

"(1) Any person who transfers a cheque by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer:

"(a) A signature on the cheque was forged or unauthorized; or

"(b) The cheque was materially altered; or

"(c) A party has a valid claim or defence against him; or

"(d) The cheque is dishonoured by non-payment.

"(2) The damages according to paragraph (1) may not exceed the amount referred to in article 67 or 68.

"(3) Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the cheque without knowledge of such defect."

"Article 43

"(1) Payment of a cheque may be guaranteed, as to the whole or part of its amount, for the account of a party by any person, who may or may not have become a party.

"(2) A guarantee must be written on the cheque or on a slip affixed thereto ('*allonge*').

"(3) A guarantee is expressed by the words: 'guaranteed', '*aval*', 'good as *aval*' or words of similar import, accompanied by the signature of the guarantor.

"(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires

"(a) The signature alone on the front of the cheque, other than that of the drawer, is a guarantee,

"(b) A signature alone on the back of a cheque is an endorsement. A special endorsement of a cheque made payable to bearer does not convert the cheque into an order instrument.

"(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the drawer."

²² See, however, later decision concerning paragraph (2) below, para. 239.

"Article 44"

"A guarantor is liable on the cheque to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the cheque."

"Article 45"

"The guarantor who pays the cheque has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party."

"Article 53"

"A cheque is duly presented for payment if it is presented in accordance with the following rules:

"(a) The holder must present the cheque to the drawee on a business day at a reasonable hour;

"(f) A cheque must be presented for payment within 120 days of its stated date;

"(g) A cheque must be presented for payment:

"(i) At the place of payment specified on the cheque; or

"(ii) If no place of payment is specified, at the address of the drawee indicated on the cheque; or

"(iii) If no place of payment is specified and the address of the drawee is not indicated, at the principal place of business of the drawee.

"(h) A cheque may be presented for payment at a clearing-house of which the drawee is a member."

104. The Working Group adopted these articles.²³

Article 54

105. The text of article 54, as considered by the Working Group, is as follows:

"(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

"(2) Presentment for payment is dispensed with

"{(a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:

"(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

"(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

"(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.]

"(c) If the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment."

106. The Working Group deleted the square brackets from paragraph (2), subparagraph (a), and, subject to this deletion, adopted the article.

Articles 55 and 56

107. The text of articles 55 and 56, as considered by the Working Group, is as follows:

"Article 55"

"(1) If a cheque is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

"(2) Delay in making [due] presentment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered because of the delay."

"Article 56"

"(1) A cheque is considered to be dishonoured by non-payment

"(a) When payment is refused upon due presentment or when the holder cannot obtain the payment to which he is entitled under this Convention;

"(c) If presentment for payment is dispensed with pursuant to article 54 (2) and the cheque is unpaid.

"(2) If a cheque is dishonoured by non-payment, the holder may, subject to the provisions of article 57, exercise a right of recourse against the drawer, the endorsers and their guarantors."

108. It was noted that one of the requirements for there to be due presentment was that the cheque must be presented within 120 days of its stated date. It was also noted that in the absence of due presentment the drawer, endorsees and their guarantors were not liable on the cheque. However, under article 34 (1 *bis*) a late presentment of the cheque for payment did not discharge the drawer. Consequently, article 55 (1) as currently drafted was incorrect in that it did not reflect the provisions of article 34 (1 *bis*).

109. Furthermore, under article 56 (1) (a) a cheque was considered to be dishonoured when payment was refused upon due presentment, although as a result of article 34 (1 *bis*) a cheque should also be considered dishonoured by

²³ See, however, later amendment of article 53 (h) below, para. 206.

non-payment in respect of the drawer if payment was refused upon late presentment.

110. Accordingly, the Working Group decided: to retain paragraphs (1) and (2) of article 55, but to amalgamate their provisions, to delete the word "due" in paragraph (2), and to modify article 56 to make clear that non-payment of a cheque on a delayed presentment constituted dishonour by the drawee in respect of the drawer.

111. The text of articles 55 and 56 as adopted by the Working Group is as follows:

"Article 55

"If a cheque is not duly presented for payment, the drawer, the endorser and their guarantors are not liable thereon. However, if a cheque is not duly presented because of delay in making presentment, the drawer is not discharged of liability except to the extent of the loss suffered because of the delay."

"Article 56

"(1) A cheque is considered to be dishonoured by non-payment:

"(a) When payment is refused upon due presentment, or when the holder cannot obtain the payment to which he is entitled under this Convention, or, as regards the drawer only, if presentment of the cheque, otherwise duly made, is delayed and payment is refused;

"(c) If presentment for payment is dispensed with pursuant to article 54 (2) and the cheque is unpaid.

"(2) If a cheque is dishonoured by non-payment, the holder may, subject to the provisions of article 57, exercise a right of recourse against the drawer, the endorser and their guarantors."

Article 57

112. The text of article 57, as considered by the Working Group, is as follows:

"If a cheque has been dishonoured by non-payment, the holder may exercise a right of recourse only after the cheque has been duly protested for dishonour in accordance with the provisions of articles 58 to 61."

113. The Working Group adopted this article.

Article 58, paragraphs (1), (2) and (3)

114. The text of article 58, paragraphs (1), (2) and (3), as considered by the Working Group, is as follows:

"(1) A protest is a statement of dishonour drawn up at the place where the cheque has been dishonoured and signed and dated by a person authorized to certify dishonour of a negotiable instrument by the law of that place. The statement must specify:

"(a) The person at whose request the cheque is protested;

"(b) The place of protest; and

"(c) The demand made and the answer given, if any, or the fact that the drawee could not be found.

"(2) A protest may be made

"(a) On the cheque itself or on a slip affixed thereto (*allonge*); or

"(b) As a separate document, in which case it must clearly identify the cheque that has been dishonoured.

"(3) Unless the cheque stipulates that protest must be made, a protest may be replaced by a declaration written on the cheque and signed and dated by the drawee; the declaration must be to the effect that payment is refused."

115. The Working Group adopted these paragraphs.

Article 58, paragraph (3 bis)

116. The text of article 58, paragraph (3 bis), as considered by the Working Group, is as follows:

"Where a cheque is presented to a clearing-house, protest may be replaced by a dated declaration by the clearing-house to the effect that the cheque had been presented to it and has not been paid."

117. The Working Group decided to delete this paragraph on the ground that it had no practical application.

Article 58, paragraph (4)

118. The text of article 58, paragraph (4), as considered by the Working Group, is as follows:

"A declaration made in accordance with paragraph (3) or (3 bis) is deemed to be a protest for the purposes of this Convention."

119. Consequent upon the deletion of paragraph (3 bis) of the article, the Working Group deleted the words "or (3 bis)" in paragraph (4), and adopted the paragraph subject to this deletion.

Articles 59, 60, 61, 62, 63, 64 and 65

120. The text of articles 59, 60, 61, 62, 63, 64 and 65, as considered by the Working Group, is as follows:

"Article 59

"Protest for dishonour of a cheque by non-payment must be made on the day on which the cheque is dishonoured or on one of the two business days which follow."

"Article 60"

"(1) If a cheque which must be protested for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.

"(2) Delay in protesting a cheque for non-payment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered by the delay."

"Article 61"

"(1) Delay in protesting a cheque for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

"(2) Protest for dishonour by non-payment is dispensed with:

"(a) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;

"(b) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

"(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

"(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

"(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made;

"(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person;

"(e) If presentment for payment is dispensed with in accordance with article 54 (2)."

"Article 62"

"(1) The holder, upon dishonour of a cheque by non-payment, must give due notice of such dishonour to the drawer, the endorsers and their guarantors.

"(3) An endorser or a guarantor who received notice must give notice of dishonour to the party immediately preceding him and liable on the cheque.

"(4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the cheque against the party notified."

"Article 63"

"(1) Notice of dishonour may be given in any form whatever and in any terms which identify the cheque and state that it has been dishonoured. The return of the dis-

honoured cheque is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.

"(2) Notice of dishonour is deemed to have been duly given if it is communicated or sent to the person to be notified by means appropriate in the circumstances, whether or not it is received by that person.

"(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice."

"Article 64"

"Notice of dishonour must be given within the two business days which follow

"(a) The day of protest, or, if protest is dispensed with, the day of dishonour; or

"(b) The receipt of notice given by another party."

"Article 65"

"(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

"(2) Notice of dishonour is dispensed with

"(a) If after the exercise of reasonable diligence notice cannot be given;

"(b) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:

"(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

"(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

"(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.

"(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person."

121. The Working Group adopted these articles.

Article 66

122. The text of article 66, as considered by the Working Group, is as follows:

"Failure to give due notice of dishonour renders a person who is required to give such notice under article 62 to a party who is entitled to receive such notice liable

for any damages which that party may suffer directly from such failure, provided that such damages do not exceed the amount due under article 67 or 68."

123. The Working Group deleted the word "directly" appearing in the article in order to align the text with that of articles 22 and 42 and, subject to this deletion, adopted the article.

Article 66 bis

124. The text of article 66 *bis*, as considered by the Working Group, is as follows:

"The holder may exercise his rights on the cheque against any one party or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound."

125. The Working Group adopted this article.

Article 67, paragraphs (1) and (2)

126. The text of article 67, paragraphs (1) and (2), as considered by the Working Group, is as follows:

"(1) The holder may recover from any party liable the amount of the cheque.

"(2) When payment is made after the cheque has been dishonoured, the holder may recover from any party liable the amount of the cheque with interest at the rate specified in paragraph (4) calculated from the date of presentment to the date of payment and any expenses of protest and of the notices given by him."

127. The Working Group adopted these paragraphs.

Article 67, paragraph (4)

128. The text of article 67, paragraph (4), as considered by the Working Group, is as follows:

"(4) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main domestic centre of the country where the cheque was payable, or if there is no such rate, then at the rate of [] per cent per annum, to be calculated on the basis of the number of days in accordance with the custom of that centre."

129. There was no unanimity in the Working Group as to an acceptable formulation of the rate at which interest should be calculated in the case of dishonour. Nevertheless, the Working Group decided to maintain the present text, and expressed the hope that an acceptable formulation might be agreed upon during the deliberations in the Commission. However, the Working Group deleted the word "domestic" in the phrase "main domestic centre" as it was unnecessary.

Article 68

130. The text of article 68, as considered by the Working Group, is as follows:

"(1) A party who takes up and pays a cheque in accordance with article 67 may recover from the parties liable to him

"(a) The entire sum which he was obliged to pay in accordance with article 67 and has paid;

"(b) Interest on that sum at the rate specified in article 67, paragraph (4) from the date on which he made payment;

"(c) Any expenses of the notices given by him.

"(2) Notwithstanding article 25 (4), if a party takes up and pays the cheque in accordance with article 67 and the cheque is transferred to him such transfer does not vest in that party the rights to and upon the cheque which any previous protected holder had."

131. The Working Group adopted this article.²⁴

Article 70, paragraph (1)

132. The text of article 70, paragraph (1), as considered by the Working Group, is as follows:

"A party is discharged of liability on the cheque when he pays the holder or a party subsequent to himself who has taken up and paid the cheque and is in possession thereof the amount due pursuant to articles 67 and 68."

133. It was noted that article 70 did not deal with the discharge of the liability of parties on a cheque as a result of payment by the drawee. While it was true that article 78, paragraph (2), provided that payment by the drawee discharged all parties to the cheque, it was considered whether such payment should discharge in all cases. Under one view, as regards payment by the drawee, the draft Convention should not make a distinction between proper and improper payment. Under another view, payment by the drawee under circumstances where a third party had asserted a valid claim to the cheque, or where the holder had acquired the cheque by theft or had forged the signature of a payee or endorsee, or where the holder had participated in the theft, should not lead to a discharge of liability of parties to the instrument. Under this view, the same conditions would apply where payment was made by a party. Under a third view, payment by the drawee with knowledge that an endorsement was forged was not proper payment and therefore should not discharge the drawer irrespective of whether the payment was to the forger, to the person who took it from the forger or to a remote person.

134. The Working Group, after deliberation, adopted the view that payment, even with knowledge of the forged

²⁴ The provision contained in paragraph (2) has subsequently been incorporated in article 25 *bis* (as new paragraph (2)).

endorsement, and even if payment was made to the forger himself, was a proper payment and discharged the drawer. Consequently this rule imposed the risk of forgery on the person whose signature was forged. However, that person had, under article 22, a statutory right for damages suffered by him because of the forgery against the person who forged his signature and the person to whom the instrument was transferred by the forger. Furthermore, under article 22, paragraph (2), he may, under national law, have such a right against the drawee.

135. The Working Group accordingly decided not to supplement the provisions of this paragraph, since the desired result already obtained under article 78, paragraph (2), which provides that payment by the drawee discharges all parties, whether or not the drawee paid to the forger, and whether or not the drawee paid with knowledge of the forgery.

136. The Working Group was of the view that the provisions of article 78, paragraph (2), should apply also to payment by the drawee of a bearer instrument which was stolen from the owner.

Article 70, paragraph (3)

137. The text of article 70, paragraph (3), as considered by the Working Group, is as follows:

"A party is not discharged of his liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the cheque or that the holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery."

138. The Working Group adopted this paragraph.

Article 70, paragraph (4)

139. The text of article 70, paragraph (4), as considered by the Working Group, is as follows:

"(a) A person receiving payment of a cheque must, unless agreed otherwise, deliver:

- "(i) To the drawee making such payment the cheque [and a receipted account];
- "(ii) To any other person making such payment, the cheque, a receipted account and any protest.

"(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the cheque to him. Withholding payment in these circumstances does not constitute dishonour by non-payment.

"(c) If payment is made but the person paying, other than the drawee, fails to obtain the cheque, such person is discharged but the discharge cannot be set up as a defence against a protected holder."

140. The Working Group deleted the words in square brackets appearing in subparagraph (a) (i) and, subject to this deletion, adopted this paragraph.

New article 70 bis

141. The text of new article 70 bis, as considered by the Working Group, is as follows:

"If the drawee without knowledge that an endorsement is forged or is made by a person in a representative capacity without authority [or that a third person had asserted a valid claim to the cheque] pays a cheque drawn on him to the holder, he does not, in doing so, incur any liability by reason only of such forged or unauthorized endorsement [or the assertion of such claim]."

142. The Working Group decided to delete this article, as it was unnecessary because the rule contained therein was already covered by articles 22, 70 and 78 (2).

Article 71

143. The text of article 71, as considered by the Working Group, is as follows:

"(1) The holder is not obliged to take partial payment.

"(2) If the holder who is offered partial payment does not take it, the cheque is dishonoured by non-payment.

"(3) If the holder takes partial payment from the drawee, the cheque is to be considered as dishonoured by non-payment as to the amount unpaid.

"(4) If the holder takes partial payment from a party to the cheque.

"(a) The party making payment is discharged of his liability on the cheque to the extent of the amount paid; and

"(b) The holder must give such party a certified copy of the cheque, and of any authenticated protest, in order to enable subsequent recourse to be exercised.

"(5) The drawee or a party making partial payment may require that mention of such payment be made on the cheque and that a receipt therefor be given to him.

"(6) The person receiving the unpaid amount who is in possession of the cheque must deliver to the payer the receipted cheque and any authenticated protest."

144. The Working Group adopted this article.

Article 72

145. The text of article 72, as considered by the Working Group, is as follows:

"(1) The holder may refuse to take payment in a place other than the place where the cheque was duly presented for payment in accordance with article 53 (g).

"(2) If payment is not then made in the place where the cheque was duly presented for payment in accordance with article 53 (g), the cheque is considered as dishonoured by non-payment."

146. The Working Group decided that it was more appropriate that the reference in paragraphs (1) and (2) of this article to article 53 should not be restricted to subparagraph (g) of article 53. It accordingly deleted the reference to subparagraph (g). The Group, as a consequence of its decision on articles 55 and 56 (above paragraphs 107-111), deleted the word "duly" in paragraphs (1) and (2) and, subject to these deletions, adopted the article.

Article 74, paragraph (1)

147. The text of article 74, paragraph (1), as considered by the Working Group, is as follows:

"(1) A cheque must be paid in the currency in which the amount of the cheque is expressed."

148. The Working Group adopted this paragraph.

Article 74, paragraph (2)

149. The text of article 74, paragraph (2), as considered by the Working Group, is as follows:

"(2) The drawer may indicate on the cheque that it must be paid in a specified currency other than the currency in which the amount of the cheque is expressed. In that case:

"(a) The cheque must be paid in the currency so specified;

"(b) The amount payable is to be calculated according to the rate of exchange indicated on the cheque. Failing such an indication, the amount payable is to be calculated according to the rate of exchange for sight drafts on the date of presentment:

"(i) Ruling at the place where the cheque must be presented for payment in accordance with article 53 (g), if the specified currency is that of the place (local currency); or

"(ii) If the specified currency is not that of that place, according to the usages of the place where the cheque must be presented for payment in accordance with article 53 (g);

"(c) If such a cheque is dishonoured by non-payment, the amount is to be calculated:

"(i) If the rate of exchange is indicated on the cheque, according to that rate;

"(ii) If no rate of exchange is indicated on the cheque, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment."

150. The Working Group adopted subparagraph (a).

151. As regards subparagraph (b), it was observed that not every country made provision for a rate of exchange for sight drafts. It was suggested that this subparagraph should state according to which rate of exchange the amount payable was to be calculated in the absence of a rate for sight drafts. The Working Group, after deliberation, accepted the suggestion, and adopted the following words for the opening words of this subparagraph:

"(b) The amount payable is to be calculated according to the rate of exchange indicated on the cheque. Failing such an indication, the amount payable is to be calculated according to the rate of exchange for sight drafts, or if there is no such rate, according to the appropriate established rate of exchange on the date of presentment."

152. The Working Group adopted the opening words of subparagraph (c), and the text of subparagraph (c) (i).

153. As regards subparagraph (c) (ii), the Working Group accepted a suggestion that the provisions of paragraph (4) of this article should be incorporated in the subparagraph, and adopted the following text of the subparagraph:

"(ii) If no rate of exchange is indicated on the cheque, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment at the place where the cheque must be presented for payment in accordance with article 53 (g) or at the place of actual payment."

Article 74, paragraph (3)

154. The text of article 74, paragraph (3) as considered by the Working Group, is as follows:

"Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-payment."

155. The Working Group adopted this paragraph.

Article 74, paragraph (4)

156. The text of article 74, paragraph (4), as considered by the Working Group, is as follows:

"The rate of exchange ruling at a certain date is the rate of exchange ruling, at the option of the holder, at the place where the cheque must be presented for payment in accordance with article 53 (g) or at the place of actual payment."

157. Pursuant to its decision to incorporate the provisions of this paragraph in paragraph (2), subparagraph (c) (ii), of this article, the Working Group deleted this paragraph.

Article 74 bis, paragraph (1)

158. The text of article 74 *bis*, paragraph (1), as considered by the Working Group, is as follows:

"Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party."

159. The Working Group adopted this paragraph.

Article 74 bis, paragraph (2)

160. The text of article 74 *bis*, paragraph (2), as considered by the Working Group, is as follows:

"(a) If, by virtue of the application of paragraph (1) of this article, a cheque drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts on the date of presentment ruling at the place where the cheque must be presented for payment in accordance with article 53 (g);

"(b) If such a cheque is dishonoured by non-payment:

"(i) The amount is to be calculated, at the option of the holder, according to the rate of exchange ruling at the date of presentment or at the date of actual payment;

"(ii) Paragraphs (3) and (4) article 74 are applicable where appropriate.

161. The Working Group decided to align subparagraph (a) of this paragraph with the new wording of the opening words of subparagraph (b) of paragraph (2) of article 74, and adopted the following text:

"(a) If, by virtue of the application of paragraph (1) of this article, a cheque drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts or, if there is no such rate, according to the appropriate established rate of exchange on the date of presentment ruling at the place where the cheque must be presented for payment in accordance with article 53 (g);"

162. Pursuant to its decision to delete paragraph (4) of article 74, the Working Group adopted the following text of subparagraph (b) (ii) of this paragraph:

"(ii) Paragraph (3) of article 74 is applicable where appropriate."

Article 74 ter

163. The text of article 74 *ter*, as considered by the Working Group, is as follows:

"If the drawer countermands the order to the drawee to pay a cheque drawn on him, the drawee is under a duty not to pay."

164. The Working Group adopted this paragraph.

165. One observer was of the view that the provisions of this article would not always be commercially acceptable and gave the following example: A buys goods from B, and receives them from the carrier against delivery to the carrier of a bank cheque. The issuing bank has issued the cheque on the instructions of A, with whom it has an agency relationship. Afterwards, A requests the bank to stop payment on the cheque pretending that the goods are defective, and the bank has to comply with this request because of the agency relationship. The drawee bank must not pay the cheque. Recourse is possible against the issuing bank. Because of alleged knowledge of defects of goods when receiving the cheque, B is not a protected holder. The bank can, in accordance with article 24 (3), rely on non-conformity of goods. In order to avoid long litigation, B (who would be the plaintiff) agrees to a reduction of the price. There would be no danger of such an occurrence if the drawee bank would, within a certain limited time (e.g. 8 days), be allowed to pay, since then A would be the plaintiff.

Article 78

166. The text of article 78, as considered by the Working Group, is as follows:

"(1) When a party is discharged wholly or partly of his liability on the cheque, any party who has a right of recourse against him is discharged to the same extent.

"(2) Payment of a cheque by the drawee to the holder of the amount due in whole or in part discharges all parties to the cheque to the same extent."

167. The Working Group noted that the Drafting Group had proposed a modified draft text of article 78 of the draft Convention on International Bills of Exchange and International Promissory Notes, which is as follows:

"(1) When a party is discharged wholly or partly of his liability on the instrument, any party who has a right of recourse against him is discharged to the same extent.

"(2) Payment by the drawee of the whole or a part of the amount of a bill to the holder, or to any party who has paid the bill in accordance with article 67, discharges all parties of their liability to the same extent."

168. The Working Group decided to follow a similar approach, and adopted the following text:

"(1) When a party is discharged wholly or partly of his liability on the cheque, any party who has a right of recourse against him is discharged to the same extent.

"(2) Payment by the drawee of the whole or a part of the amount of the cheque to the holder, or to any party who has paid the cheque in accordance with article

67, discharges all parties of their liability to the same extent."

Article 79

169. The text of article 79, as considered by the Working Group, is as follows:

"(1) A right of action arising on a cheque can no longer be exercised after four years have elapsed:

"(a) Against the drawer or his guarantor, after the date of the cheque;

"(b) Against an endorser or his guarantor, after the date of protest for dishonour or, where protest is dispensed with, the date of dishonour.

"(2) If a party has taken up and paid the cheque in accordance with article 67 or 68 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year after the date on which he took up and paid the cheque."

170. The Working Group adopted this article.

Articles 80, 81, 82, 83, 84 and 85

171. The text of articles 80, 81, 82, 83, 84 and 85, as considered by the Working Group, is as follows:

"Article 80

"(1) When a cheque is lost, whether by destruction, theft or otherwise, the person who lost the cheque has, subject to the provisions of paragraphs (2) and (3) of this article, the same right to payment which he would have had if he had been in possession of the cheque. The party from whom payment is claimed cannot set up as a defence against liability on the cheque the fact that the person claiming payment is not in possession thereof.

"(2) (a) The person claiming payment of a lost cheque must state in writing to the party from whom he claims payment:

"(i) The elements of the lost cheque pertaining to the requirements set forth in article 1 (2); these elements may be satisfied by presenting to that party a copy of that cheque;

"(ii) The facts showing that, if he had been in possession of the cheque, he would have had a right to payment from the party from whom payment is claimed;

"(iii) The facts which prevent production of the cheque.

"(b) The party from whom payment of a lost cheque is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost cheque.

"(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the Court may determine whether security is called for and, if so, the nature of the security and its terms.

"(d) If the security cannot be given, the Court may order the party from whom payment is claimed to deposit the amount of the lost cheque, and any interest and expenses which may be claimed under articles 67 and 68, with the Court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

"New (3) The person claiming payment of a lost cheque in accordance with the provisions of this article need not give security to the drawer who has inserted in the cheque, or to an endorser who has inserted in his endorsement, such words as 'not negotiable', 'not transferable', 'not to order', 'pay (X) only', or words of similar import."

"Article 81

"(1) A party who has paid a lost cheque and to whom the cheque is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

"(2) Such notification must be given on the day the cheque is presented for payment or on one of the two business days which follow and must state the name of the person presenting the cheque and the date and place of presentment.

"(3) Failure to notify renders the party who has paid the lost cheque liable for any damages which the person whom he paid may suffer from such failure, provided that the total amount of the damages does not exceed the amount of the cheque and any interest and expenses which may be claimed under article 67 or 68.

"(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost cheque and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

"(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given."

"Article 82

"(1) A party who has paid a lost cheque in accordance with the provisions of article 80 and who is subsequently required to, and does, pay the cheque, or who

then loses his right to recover from any party liable to him and such loss of right was due to the fact that the cheque was lost, has the right:

"(a) If security was given, to realize the security; or

"(b) If the amount was desposited with the Court or other competent authority, to reclaim the amount so deposited.

"(2) The person who has given security in accordance with the provisions of paragraph (2) (b) of article 80 is entitled to reclaim the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the cheque is lost."

"Article 83

"A person claiming payment of a lost cheque duly effects protest for dishonour by non-payment by the use of a writing that satisfies the requirements of article 80, paragraph (2) (a)."

"Article 84

"A person receiving payment of a lost cheque in accordance with article 80 must deliver to the party paying the writing required under paragraph (2) (a) of article 80 receipted by him and any protest and a receipted account."

"Article 85

"(a) A party who paid a lost cheque in accordance with article 80 has the same rights which he would have had if he had been in possession of the cheque.

"(b) Such party may exercise his rights only if he is in possession of the receipted writing referred to in article 84."

172. The Working Group adopted these articles.

Articles A and B

173. The text of articles A and B, as considered by the Working Group, is as follows:

"Article A

"(a) A cheque is crossed when it bears across its face two parallel transverse lines.

"(b) A crossing is general if it consists of the two lines only or if between the two lines the word 'banker' or an equivalent term or the words 'and Company' or any abbreviation thereof is inserted; it is special if the name of a banker is so inserted.

"(c) A cheque may be crossed generally or specially by the drawer or the holder.

"(d) The holder may convert a general crossing into a special crossing.

"(e) A special crossing may not be converted into a general crossing.

"(f) The banker to whom a cheque is crossed specially may again cross it specially to another banker for collection."

"Article B

"If a cheque shows on its face the obliteration either of a crossing or of the name of the banker to whom it is crossed, the obliteration is regarded as not having taken place."

174. The Working Group adopted these articles.

Article C

175. The text of article C, as considered by the Working Group, is as follows:

"(1) (a) A cheque which is crossed generally is payable only to a banker or to a customer of the drawee.

"(b) A cheque which is crossed specially is payable only to the banker to whom it is crossed or, if such banker is the drawee, to his customer.

"(c) A banker may take a crossed cheque only from his customer or from another banker.

"(2) The drawee who pays or the banker who takes a crossed cheque in violation of the provisions of paragraph (1) of this article incurs liability for any damages which a person may have suffered as a result of such violation, provided that such damages do not exceed the amount of the cheque."

176. It was suggested that the word "take" used in paragraphs (1) (c) and (2) did not make it immediately clear whether the provision covered the situations where a banker takes a cheque for payment and also where he takes it for collection. The Working Group agreed with the suggestion, and decided to modify these paragraphs and adopted the following text:

"(1) (c) A banker may not take a crossed cheque except from his customer or from another banker and may not collect such a cheque except for such a person.

"(2) The drawee who pays or the banker who takes or collects a crossed cheque in violation of the provisions of paragraph (1) of this article incurs liability for any damages which a person may have suffered as a result of such violation, provided that such damages do not exceed the amount of the cheque."

Article D

177. The text of article D, as considered by the Working Group, is as follows:

"[If a banker without knowledge that an endorsement is forged or is made by a person in a representative capacity without authority [or that a third person has asserted a valid claim to the cheque] takes a crossed cheque, he does not, in doing so, incur any liability by reason only of such forged or unauthorized endorsement [or the assertion of such claim].]"

178. As a consequence of its decision relating to article 70 *bis*, the Working Group decided not to retain this article.

Articles E, F, and a

179. The text of articles E, F, and a, as considered by the Working Group, is as follows:

"Article E"

"If the crossing on a cheque contains the words 'not negotiable' the transferee becomes a holder but cannot become a protected holder in his own right."

"Article F"

"(1) (a) The drawer or the holder of a cheque may prohibit its payment in cash by writing transversally across the face of the cheque the words 'payable in account' or words of similar import.

"(b) In such a case the cheque can only be paid by the drawee by means of a book-entry.

"(2) The drawee who pays such a cheque other than by means of a book-entry incurs liability for any damages which a person may have suffered as a result thereof, provided that such damages do not exceed the amount of the cheque.

"(3) If a cheque shows on its face the obliteration of the words 'payable in account', the obliteration is regarded as not having taken place."

"Article a"

"If a cheque is drawn against insufficient funds, it is nevertheless valid as a cheque."

180. The Working Group adopted these articles.

Article β , paragraph (1)

181. The text of article β , paragraph (1), as considered by the Working Group, is as follows:

"A cheque which bears a date other than the date on which it was drawn is nevertheless valid as a cheque."

182. The Working Group adopted this paragraph.

Article β , paragraph (2)

183. The text of article β , paragraph (2), as considered by the Working Group, is as follows:

"If a cheque is presented before its stated date:

Variant A

"(a) Payment discharges parties liable on the cheque;

"(b) Refusal by the drawee to pay constitutes dishonour.

Variant B

"(a) Payment does not discharge parties liable on the cheque;

"(b) Refusal by the drawee to pay does not constitute dishonour."

184. The Working Group considered the two variants prepared by the Secretariat. The Working Group favoured variant B, but was of the view that it was not necessary to retain subparagraph (a), as the result achieved by this subparagraph already followed from other provisions in the draft Convention. The Working Group adopted the following text:

"If a cheque is presented before its stated date, refusal by the drawee to pay does not constitute dishonour."

II. DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES

Draft articles 1, 5(7), 17(3), 22(1) and new (1 bis), 25, X appended to 27(3), 30 bis, 34 bis (1), 36(2), 44, 49, 53 (h), 58 (3 bis) and (4), 61(2)(f), 66, 67(1)(b) and (2), 70(4), 71(2) and (6), 74(2)(b), 74 bis new (2), 79 and 82(1)

185. The Working Group reconsidered certain articles of the draft Convention on International Bills of Exchange and International Promissory Notes (as set forth in the annex to document A/CN.9/181)* in the light of the following:

(a) Modifications made by it to draft articles of the draft Convention on International Cheques;

(b) Revised draft articles prepared by the Secretariat and set forth in document A/CN.9/WG.IV/WP.22;**

(c) Issues of substance which arose during the deliberations of the Drafting Group.

Article 1

186. One observer expressed the view that the Convention, in particular its article 1, did not make it sufficiently clear that the use of the international instrument governed by this Convention was optional and that parties in international transactions were free to choose an instrument governed by another legal regime. It was observed in reply that

* Yearbook . . . 1980, part two, III, B.

** Reproduced in this volume, part two, II, A, 1, (b).

the optional nature could be inferred, for example in the case of a bill of exchange, from article 1, paragraph (2) (a), which required, for the Convention to apply, that the instrument used by the parties contain in its text the words "International Bill of Exchange (Convention of . . .)".

187. The Group, after deliberation, was agreed that the Secretariat should consider expressing this optional nature in the draft articles on final clauses of the draft Convention to be prepared by the Secretariat for submission to a diplomatic conference.

Article 5, paragraph (7)²⁵

188. The Working Group decided to align this paragraph with article 5, paragraph (6), of the draft Convention on International Cheques (above, paragraph 40), and adopted the following text:

"'Protected holder' means the holder of an instrument which, when he became a holder, was complete and regular on its face, provided that:

"(a) He was, at that time, without knowledge of a claim to or defence upon the instrument referred to in article 24 or of the fact that it was dishonoured by non-acceptance or non-payment;

"(b) The time-limit provided by article 53 for presentment of that instrument for payment had not then expired."

Article 17, paragraph (3)

189. It was noted that there was a certain contradiction between the provisions of article 17, paragraph (3) and article 24, paragraph (1) (b), in that, under article 17, paragraph (3), the non-fulfilment of a condition could not be raised as a defence against a remote holder, while in the same circumstances non-fulfilment of a condition could be raised as a defence under article 24, paragraph (1 bis).

190. The Working Group was agreed that a party to the instrument should be entitled to raise the non-fulfilment of his condition against a remote holder who is not a protected holder. Consequently, the Working Group decided to delete paragraph (3) of article 17.

191. In this context, the Working Group reconsidered its position as regards conditional endorsements, and was agreed that an endorsement should be unconditional, but that if, none the less, a conditional endorsement was made, such endorsement transfers the instrument whether or not such condition is fulfilled. Accordingly, the Working Group decided to retain paragraph (2) of this article, and to adopt the following new paragraph (1) to read as follows:

"(1) An endorsement must be unconditional."

192. The Working Group decided to adopt the same text for article 17 of the draft Convention on International Cheques.

Article 22, paragraph (1) and new paragraph (1 bis)

193. The Working Group considered the two variants of paragraph (1) set forth in document A/CN.9/WG.IV/WP.22* in the light of its decisions taken in regard to article 22 of the draft Convention on International Cheques (above, paragraphs 68-71). The Group, while recognizing that different considerations might apply to international bills of exchange and notes on the one hand, and international cheques on the other, decided to adopt the same rule for both draft Conventions.

194. Consequently, the Working Group adopted the following text:

"(1) If an endorsement is forged, any party has against the forger and against the person to whom the instrument was directly transferred by the forger, the right to recover compensation for any damage that he may have suffered because of the forgery;

"(1 bis) The liability of an acceptor, drawee, or maker who pays, or of an endorsee for collection who collects, an instrument on which there is a forged endorsement is not regulated by this Convention."²⁶

195. It was understood that the provisions of paragraph (1 bis) did not set forth an exhaustive list of persons paying the instrument whose liability was not governed by this Convention and that therefore, for example, the liability of a bank at which an instrument was domiciled would also be left to national law.

Article 25

196. The Working Group decided to align article 25, paragraph (1) (a), with the corresponding provision in the draft Convention on International Cheques, and to delete the reference to articles 57 and 60 in that paragraph.

Article X appended to article 27, paragraph (3)

197. The Working Group, in accordance with its decision relating to the corresponding article in the draft Convention on International Cheques (above, paragraph 85), decided to place the appended article between square brackets.

Article 30 bis

198. The Working Group decided to align article 30 bis with the corresponding article in the draft Convention on International Cheques (above, paragraph 93).

* Reproduced in this volume, part two, II, A, 1, (b).

²⁶ See, however, later amendment of paragraph (1 bis) below, para. 235.

²⁵ As to a new paragraph (11) of article 5, see discussion and decision below, paras. 222-229.

Article 34 bis, paragraph (1)

199. It was noted that the article did not state at what time the maker was to pay the note. The Working Group agreed with this observation and decided that the provision should specify that the maker engaged to pay the amount of the note in accordance with the terms of the note. The Group adopted the following text:

"(1) The maker engages that he will pay to the holder, or to any party who takes up and pays the note in accordance with article 67, the amount of the note in accordance with the terms of that note, and any interest and expenses which may be recovered under article 67 or 68."

200. The question was raised whether, in the case of a delay in making presentment of a domiciled note, the liability of the maker be reduced by the extent of the loss he suffered because of such delay. The Working Group, after deliberation, was agreed that the maker, as a party primarily liable, should not be discharged in such a case. However, it was understood that he may, under national law, have a right to recover any damages which he may have suffered because of the delay.

201. In this connection, the Working Group reconsidered the provisions of article 34, paragraphs (1 *bis*) and (1 *ter*) of the draft Convention on International Cheques and decided to delete these two paragraphs in the light of the fact that the rule contained therein was already stated in article 55, paragraph (2), and article 60, paragraph (2).

Article 36, paragraph (2)

202. The Working Group adopted a similar modification as made in article 34 *bis*, paragraph (1) (see above, paragraph 199), and adopted the following text of paragraph (2):

"(2) The acceptor engages that he will pay to the holder, or to any party who takes up and pays the bill in accordance with article 67, or the drawer who has paid the bill, the amount of the bill in accordance with the terms of his acceptance, and any interest and expenses which may be recovered under article 67 or 68."

Article 44

203. As regards paragraph (1) of this article, the question was raised whether the term "to the same extent" referred only to the amount of the instrument or also to other matters, and if it referred only to the amount, whether the words "unless the guarantor has stipulated otherwise on the instrument" would apply only to a stipulation to reduce the amount, or whether it also covered a stipulation to increase the amount. The Group, after deliberation, was agreed that the provision was not limited to the question of amount but covered other elements as well (e.g., time or place of payment) and that a stipulation by the guarantor could re-

late to any possible element of the guarantor's liability in any possible way, including reduction and increase of the amount. The Group requested the Secretariat to reflect this understanding in the commentary.

204. As regards paragraph (2) of article 44, the Working Group decided to replace the words "when due" by the words "at maturity".

Article 49

205. It was observed that the opening words of article 49 ("Presentment for acceptance is dispensed with") did not make it immediately clear whether this article applied only to cases where presentment for acceptance was mandatory, or whether it would also cover those cases where presentment was optional. The Working Group concurred with this observation and considered the substantive question whether article 49 should also cover the cases of optional presentment. The Group, after deliberation, decided in the affirmative for the reason that the provision on dispensation was also appropriate in cases of optional presentment which constituted the large majority of cases which occurred in practice. For example, in the circumstances envisaged in paragraph (a), where the drawee was dead, no acceptance by him could be obtained, and it would be futile to require the holder to present the instrument for acceptance. Consequently the Group decided, in order to make the scope of application of article 49 abundantly clear, to modify the opening words of article 49 as follows:

"A necessary or optional presentment for acceptance is dispensed with."

Article 53, paragraph (h)

206. It was noted that article 53, paragraph (h), only covered the case of presentment to a clearing-house of which the drawee was a member but did not include presentment to a clearing-house in the case of a domiciled instrument. The Working Group concurred with this observation and, in order to enlarge the scope of this provision, decided to delete the words "of which the drawee is a member". The Group adopted the same change for the corresponding article in the draft Convention on International Cheques.

Article 58, paragraphs (3 bis) and (4)

207. The Working Group considered paragraphs (3 *bis*) and (4), as set forth in document A/CN.9/WG.IV/WP.22,* in the light of its decision on article 58, paragraphs (3 *bis*) and (4), of the draft Convention on International Cheques (above, paras. 116-119). The Group decided to delete paragraph (3 *bis*) and, in paragraph (4), to delete the reference to article (3 *bis*).

* Reproduced in this volume, part two, II, A, 1, (b).

Article 61, paragraph (2) (f)

208. The Working Group reaffirmed its decision to delete this subparagraph (A/CN.9/196, para. 159).*

Article 66

209. The Working Group made the same change in article 66 as in the corresponding article of the draft Convention on International Cheques (above, paras. 122-123) and deleted the word "directly".

Article 67, paragraph (1) (b)

210. The Working Group considered the draft text of paragraph (1)(b) which reads as follows:

- "(1) The holder may recover from any party liable
- "(a) ...
- "(b) After maturity:
 - "(i) The amount of the instrument with interest, if interest has been stipulated for, from the date of presentment;
 - "(ii) If interest has been stipulated for after maturity, interest at the rate stipulated, or in the absence of such stipulation interest at the rate specified in paragraph (2), calculated from the date of maturity on the sum specified in paragraph 1(b)(i);
 - "(iii) Any expenses of protest and of the notices given by him;"

211. The Working Group, after deliberation, was agreed that under subparagraph (b) (i) the interest to be paid should be on the amount of the instrument to the date of maturity and that the interest to be paid under subparagraph (b)(ii) should be calculated from the date of presentment. Accordingly, the Group adopted the following text.

- "(b) After maturity:
 - "(i) The amount of the instrument with interest, if interest has been stipulated for, to the date of maturity;
 - "(ii) If interest has been stipulated for after maturity, interest at the rate stipulated, or in the absence of such stipulation, interest at the rate specified in paragraph (2), calculated from the date of presentment on the sum specified in paragraph 1(b)(i);
 - "(iii) Any expenses of protest and of the notices given by him;"

Article 67, paragraphs (2) and (3)

212. It was noted that paragraph (2) of article 67 referred to the official rate (bank rate) or other similar appro-

priate rate effective in the main centre of the country where the instrument was payable, and that in some countries no such rate existed. The suggestion was made, therefore, in such instances, to apply the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the instrument was payable.

213. The Working Group, after deliberation, adopted this suggestion and decided to modify paragraph (2) as follows:

- "(2) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the instrument is payable, or if there is no such rate, then in the main centre of the country in the currency of which the instrument is payable. In the absence of any such rate, the rate of interest shall be [] per cent per annum."

214. The Working Group decided to delete the words "to be calculated on the basis of the number of days and in accordance with the custom of that place" at the end of paragraph (3).

Article 70, paragraph (4)

215. The Working Group considered article 70, paragraph (4) (a) and (c) as redrafted by the Secretariat:

- "(4) (a) A person receiving payment of an instrument must, unless agreed otherwise, deliver:
 - "(i) to the drawee making such payment the instrument [and a receipted account];
 - "(ii) to any other person making such payment, the instrument, a receipted account and any protest.
 - "(b) ...
 - "(c) If payment is made but the person paying, other than the drawee, fails to obtain the instrument, such person is discharged but the discharge cannot be set up as a defence against a protected holder."

216. The Group adopted the text, subject to the deletion of the words "[and a receipted account]" in subparagraph (i).

Article 71, paragraphs (2) and (6)

217. The Working Group considered and adopted paragraphs (2) and (6) of article 71 as redrafted by the Secretariat:

- "(2) If the holder who is offered partial payment does not take it, the instrument is dishonoured by non-payment.
- "(6) The person receiving the unpaid amount who is in possession of the instrument must deliver to the

* Yearbook ... 1981, part two, II, A.

payor the receipted instrument and any authenticated protest."

Article 74, paragraph (2)(b)

218. The Working Group decided to align the opening words of paragraph (2)(b) with the revised wording of the corresponding subparagraph in the draft Convention on International Cheques (above, paragraph 151) and adopted the following text:

"(b) The amount payable is to be calculated according to the rate of exchange indicated on the instrument. Failing such indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate rate of exchange) on the date of maturity:"

Article 74 bis, new paragraph (2)

219. The Working Group decided to align subparagraph (a) of this paragraph with the revised wording of paragraph (2)(b) of article 74 (above, paragraph 218) and, subject to this modification, adopted paragraph (2) as follows:

"(a) If, by virtue of the application of paragraph (1) of this article, an instrument drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts or, if there is no such rate, according to the appropriate established rate of exchange on the date of presentment ruling at the place where the instrument must be presented for payment in accordance with article 53 (g);

"(b)(i) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated, at the option of the holder, at the rate of exchange ruling at the date of dishonour, or at the date of actual payment;

"(ii) If such an instrument is dishonoured by non-payment, the amount is to be calculated, at the option of the holder, according to the rate of exchange ruling at the date of presentment or at the date of actual payment;

"(iii) Paragraphs (3) and (4) of article 74 are applicable where appropriate."

Article 79

220. The Working Group considered article 79, paragraphs (1)(a) to (d) and (2), as redrafted by the Secretariat, and adopted this text without change:

"(1) A right of action arising on an instrument can no longer be exercised after four years have elapsed

"(a) Against the maker, or his guarantor, of a note payable on demand, after the date of the note;

"(b) Against the acceptor or the maker or their guarantor of an instrument payable at a definite time, after the date of maturity;

"(c) Against the acceptor of a bill payable on demand, after the date on which it was accepted;

"(d) Against the drawer or an endorser or their guarantor, after the date of protest for dishonour, or where protest is dispensed with, the date of dishonour.

"(2) If a party has taken up and paid the instrument in accordance with article 67 or 68 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year after the date on which he took up and paid the instrument."

Article 82, paragraph (1)

221. The Working Group considered, and adopted, the opening words of article 82, paragraph (1), as redrafted by the Secretariat:

"(1) A party who has paid a lost instrument in accordance with the provisions of article 80 and who is subsequently required to, and does, pay the instrument, or who then loses his right to recover from any party liable to him and such loss of right was due to the fact that the instrument was lost, has the right:"

III. CONSIDERATION OF TWO MATTERS RELEVANT TO BOTH CONVENTIONS

A. Instruments and cheques payable in, or denominated in, units of account

222. The observer of the International Monetary Fund (IMF) made a statement on this issue, with particular reference to the special drawing right (SDR) of IMF. He noted that the SDR was an international reserve asset created by IMF and allocated by it to its members as a supplement to existing reserve assets. Only a limited class could hold SDRs. All 141 States members of IMF were participants in its SDR Department and were eligible to hold SDRs. These member States could use SDRs in transactions with other member States, with certain other authorized holders of SDRs, and with the General Resources Account of IMF, which also held SDRs. The SDR was also the IMF unit of account.

223. The SDR was being increasingly used for a variety of transactions. Members with a balance-of-payments need may use SDRs to acquire foreign exchange in a transaction in which another member designated by IMF provided currency in exchange for SDRs. Members may also use SDRs in a variety of voluntary transactions and operations by agreement with other members. They may engage

in "swap" arrangements and forward operations involving SDRs. They may make loans of SDRs, and settle financial obligations in SDRs. They may use SDRs as security for the performance of financial obligations and in donations. Authorized holders who were not members also engaged in certain financial transactions with SDRs. In some instances the transactions might not be subject to a particular governing law.

224. As regards coverage by the draft Conventions of relevant transactions involving SDRs, the observer noted that two questions arose: (a) whether an instrument covered by the Conventions could call for payment in SDRs, or another unit of account, and (b) whether an instrument covered by the Conventions might call for payment in a particular currency but be denominated in SDRs or another unit of account. As regards the first issue, he noted that there would appear to be no special reason not to permit the Conventions to apply to an instrument payable in SDRs should the maker or drawer (which must belong to the limited class) decide to opt at its inception to make the instrument subject to the rules of the Conventions. While it was not possible to estimate the frequency of use that might develop in respect of such instruments, permitting an official holder to utilize the rules of the draft Conventions could only serve to extend the usefulness of the Conventions. Similar considerations applied as regards the second issue. The denomination in SDRs could be used by private parties as a safeguard against currency fluctuations. He noted that the valuation of an SDR against a national currency would be provided by IMF in regard to the currencies of member States, and could also be determined for other currencies.

225. Various methods might be used to extent the coverage of the draft Conventions to instruments payable in, or denominating a currency in, units of account. The method favoured by the UNCITRAL Study Group on International Payments, which had considered this question, was to add a definition of "money" to the draft Conventions, which might cover monetary units such as the SDR, the ECU and the transferable rouble. This definition was as follows:

"Money" means a medium of exchange:

"(a) Which is authorized or adopted by a Government (or several Governments) as its (or their) official currency or part thereof; or

"(b) Which is established by an intergovernmental institution and intended by it to be transferable in its records and only between it and among persons designated by it."

Consideration by the Working Group

226. The views expressed in the Working Group showed that there was little doubt that if the draft Conventions were to offer the possibility of drawing an instrument in a unit

of account which was a monetary unit, and payable in that unit, the usefulness of the Conventions would in principle be increased. However, such an extension of the application of the Conventions would, in the last resort, depend on the desire of Governments to use the Conventions for that purpose. Consequently, the Working Group concluded that it would suffice to draw the attention of Governments to this issue through a definition of money to be inserted in article 5 of the draft Conventions, and to be placed between square brackets. The commentary should make clear that the definition was of a tentative nature, and solely for the purpose of eliciting the views of Governments. The commentary should also indicate that, if the views of Governments were of a positive nature, certain provisions of the draft Conventions would have to be amended accordingly.

227. As regards denominating the sum payable in a unit of account, the Working Group was of the view that using a unit of account as a point of reference for the purpose of calculating the amount payable in an instrument in money was already implicit in the provisions of articles 7 and 74. However this possibility could, if need be, be made more explicit.

228. The tentative definition of money adopted by the Working Group is as follows:

["Money" or "currency" include a monetary unit of account which is established by an intergovernmental institution, and includes such unit of account even if intended by it to be transferable in its records and only between it and among persons designated by it."]

229. The Working Group decided to add this tentative definition to the definitions set forth in article 5, as a new paragraph (9) in the draft Convention on International Cheques and as a new paragraph (11) in the draft Convention on International Bills of Exchange and International Promissory Notes.

B. Provision on rules applicable to questions governed by the Conventions but not expressly settled therein

230. The Working Group considered a note submitted by the observer of the Hague Conference on Private International Law (Hague Conference). In this note (A/CN.9/WG.IV/WP.23),* the observer of the Hague Conference suggested to the Working Group to adopt, in both draft Conventions, an article X which might be placed in the chapter on General Provisions and which would read as follows:

"Article X"

"Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the law applicable by virtue of the rules of private international law."

* Reproduced in this volume, part two, II, A, 1, (c).

"If the State, the law of which is found to be applicable under the rules of private international law, has, independently of its general rules of law, provisions which are specific [to cheques] [to bills of exchange and promissory notes] for the settlement of the questions referred to in the preceding paragraph, these provisions will be applied with priority over those general rules."

231. Different views were expressed about the desirability of including in the draft Conventions provisions regarding the application of municipal law to questions concerning matters covered by the draft Convention but not expressly settled in it. Under one view, it was stated that such provisions were not strictly necessary. Under another view, while it was true that the provisions might state the obvious, it would be useful if the draft Convention would indicate to the courts the proper direction to be taken. Under yet another view, the implications of the proposal by the observer should be carefully considered, since it was by no means immediately clear whether the authors of the draft Convention wished to settle a question by not dealing with it, or whether the fact that the question was not regulated was by oversight.

232. It was observed that in the latter case, the proposed solution of the observer of the Hague Conference would lead to the result that, since the question was not expressly settled in the Convention, a court would have to apply rules of the conflict of laws determining the applicable law, which would prevent a court from deciding the question by analogy to a provision of the draft Convention.

233. The Working Group, after deliberation, was agreed that a provision as suggested by the observer of the Hague Conference was not necessary.

IV. ADOPTION OF DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES AS REVISED BY DRAFTING GROUP

234. The Working Group considered the articles of the draft Convention on International Bills of Exchange and International Promissory Notes as revised by the Drafting Group and set forth in document A/CN.9/WG.IV/WP.24 and Add. 1-2.*

235. The Working Group approved this text subject to the following modifications:

Article 9, paragraph (6): Delete the square brackets

Article 22, paragraph (1 bis): Replace the words "an acceptor, drawee, or maker" by the words "a party or of the drawee"

* Reproduced in this volume, part two, II, A, 2, (d), (e), (f).

236. The Working Group also considered, and adopted with minor modifications, the suggestions of the Drafting Group relating to headings, subheadings and structure of the draft Convention (A/CN.9/WG.IV/WP.24 and Add. 1-2).*

237. The Working Group noted that the Drafting Group had continued its work until the last but one day of the session of the Working Group and that, therefore, lack of time had prevented the establishment of a complete text in final form. For example, a number of changes had been expressed only in the form of corrigenda, the headings and subheadings had not been inserted at their proper place, and the draft articles had not been renumbered consecutively. It was understood that the Secretariat would compile the complete text.²⁷

V. ADOPTION OF DRAFT CONVENTION ON INTERNATIONAL CHEQUES AS REVISED BY DRAFTING GROUP

238. The Working Group considered the articles of the draft Convention on International Cheques as revised by the Drafting Group and set forth in document A/CN.9/WG.IV/WP.25 and Add. 1.**

239. The Working Group approved this text subject to the following modifications:

Article 22, paragraph (1 bis): Replace the words "the liability of a drawee" by the words "the liability of a party or of the drawee"

Article X (following article 34): Place the text of paragraph (2) between square brackets

Article 78: Insert (erroneously omitted) text:

"(1) When a party is discharged wholly or partly of his liability on the cheque, any party who has a right of recourse against him is discharged to the same extent.

"(2) Payment by the drawee of the whole or a part of the amount of the cheque to the holder, or to any party who has paid the cheque in accordance with article 67, discharges all parties of their liability to the same extent."

240. The Working Group also considered, and adopted with minor modifications, the suggestions of the Drafting Group relating to headings, subheadings and structure of the draft Convention (A/CN.9/WG.IV/WP.25/Add. 1).***

241. The Working Group noted that the Drafting Group had continued its work until the last but one day of the ses-

* Reproduced in this volume, part two, II, A, 2, (d), (e), (f).

** *Ibid.*, (g), (h).

*** Reproduced in this volume, part two, II, A, 2, (h).

²⁷ The complete text of the draft Convention is contained in A/CN.9/211 (reproduced in this volume, part two, A, 3). A commentary on this draft Convention will be published as document A/CN.9/213 (reproduced in this volume, part two, A, 4).

sion of the Working Group and that, therefore, lack of time had prevented the establishment of a complete text in final form. For example, a number of changes had been expressed only in the form of corrigenda, the headings and subheadings had not been inserted at their proper place, and the draft articles had not been renumbered consecutively. It was

understood that the Secretariat would compile the complete text.²⁸

²⁸ The complete text of the draft Convention is contained in A/CN.9/212 (reproduced in this volume, part two, A, 5). A commentary on this draft Convention will be published as document A/CN.9/214 (reproduced in this volume, part two, A, 6).

2. WORKING PAPERS SUBMITTED TO THE WORKING GROUP ON INTERNATIONAL NEGOTIABLE INSTRUMENTS AT ITS ELEVENTH SESSION (NEW YORK, 3-14 AUGUST):

(a) *Note by the Secretariat: uniform rules applicable to international cheques: text of articles as redrafted by consultants to the Secretariat and by the Working Group at its ninth and tenth sessions (A/CN.9/WG.IV/WP.21)**

Article 1

- (1) ...
- (2) ...
- (a) ...
- (b) ...
- (c) Is drawn on a banker or on a person or institution assimilated by the applicable law to a banker;¹
- (d) ...
- (e) ...
- (f) ...
- (i) ...
- (ii) The place indicated next to the name or the signature of the drawer;²
- (iii) ...
- (iv) ...
- (v) ...
- (g) ...
- (3) ...

Article 5

- ...
- (1) ...
- (2) ...
- (3) ...
- (4) ...
- (5) ...
- (6) "Protected holder" means a holder of a cheque which, when he became a holder, was complete and regular on its face and not overdue [in accordance with article 53 (f)], provided that, at that time, he was without knowledge of any claim to or defence upon the cheque referred to in article 24 or of the fact that it was dishonoured by non-payment;³
- (7) ...
- (8) ...

Article 8⁴

- (1) ...
- (2) ...
- [(3) ...]
- (4) ...]

Article 9⁵

A cheque is payable on demand:

* 12 June 1981. The text of the articles set forth herein is of the following kinds: (a) text as re-drafted by Professors A. Barak and W. Vis, consultants to the Secretariat, in accordance with requests of the Working Group made at its ninth and tenth sessions, and (b) text as amended by the Working Group at its ninth and tenth sessions. References are given to relevant paragraphs in the reports of the ninth session of the Working Group (A/CN.9/181) (Yearbook ... 1980, part two, III, B) and the tenth session of the Working Group (A/CN.9/196) (Yearbook ... 1981, part two, II, A) and to the articles of the draft Convention on International Bills of Exchange and International Promissory Notes as re-drafted or amended (A/CN.9/WG.IV/WP.22) (reproduced in this volume, part two, II, A, 2, (b)). Points of ellipsis against a paragraph or subparagraph indicate that no change has been made to the text of that paragraph or subparagraph. (Footnote in original).

¹ The Working Group's request for amendment related to article 5 (A/CN.9/181, para. 161) (Yearbook ... 1980, part two, III, B). However, it was considered that the amendment in question could more appropriately be made in this article.

² *Ibid.*, para. 165.

³ Although the term "overdue" was objected to (*ibid.*, para. 172) it was considered difficult to avoid the use of this term. In response to the view contained, *ibid.*, at para. 173, the square brackets around the last phrase have been deleted.

⁴ The only amendment is the placing of paragraphs (3) and (4) between square brackets. *Ibid.*, para. 181.

⁵ The Working Group was of the opinion that the requirement that a cheque be payable on demand should not be retained among the formal requisites set forth in paragraph (2) of article 1 but should be included among the rules applicable to presentment and payment (*ibid.*, para. 163). However it was considered more appropriate to retain paragraph (2) (d) of article 1, and add the present article.

(a) If it states that it is payable on demand or at sight or on presentment or if it contains words of similar import, or

(b) If no time of payment is expressed.

Article 21

(1) ...

(2) The endorsement to the drawee operates only as an acknowledgment that the endorser has received from the drawee the sum payable by the cheque [except in the case where the drawee has several establishments and the endorsement is made in favour of an establishment other than that on which the cheque has been drawn].⁶

Article 22

Variant A

(1) If an endorsement is forged, any person has against the forger, against the person who took the cheque directly from the forger and against the drawee who paid the cheque to the forger the right to recover compensation for any damage that he may have suffered because of the forgery.⁷

(2) ...

Note. The effect of the above rule would be that, for purposes of the drawee's liability to pay compensation to the person who suffered loss because of a forged endorsement, it is immaterial whether the drawee paid with or without knowledge of the forgery.

Variant B

(1) If an endorsement is forged, any party has against the forger, against the person who took the cheque directly from the forger and against the drawee who paid the cheque to the forger with knowledge of the forgery the right to recover compensation for any damage that he may have suffered because of the forgery.⁸

(2) ...

Note. The effect of the above rule would be that an action for damages would not lie against a drawee who paid without knowledge of the forgery.⁹

⁶ *Ibid.*, paras. 188-189.

⁷ A/CN.9/196, paras. 113-118 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.22, article 22, Variant A (reproduced in this volume, part two, II, A, 2, (b)).

⁸ A/CN.9/196, paras. 113-118; (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.22, article 22, Variant B (reproduced in this volume, part two, II, A, 2, (b)).

⁹ One of these Variants could be adopted in both the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Uniform Rules applicable to International Cheques. A further possibility would be that Variant A is adopted in the draft Convention and Variant B in the draft Uniform Rules. If one of these Variants were to be adopted, article 70 *bis* would not be required.

Article 34

(1) The drawer engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder the amount of the cheque, and any interest and expenses which may be recovered under article 67 or 68.

(1 *bis*) Delay in making presentment does not discharge the drawer of liability except to the extent of the loss suffered because of the delay.

(1 *ter*) Delay in protesting a cheque for dishonour does not discharge the drawer of liability except to the extent of the loss suffered because of the delay.

(2) ...

Note 1. The Working Group decided that the drawer would be discharged of liability upon failure of the holder to make presentment or protest. However, delay in making presentment or protest would not discharge the drawer except to the extent of the loss suffered because of the delay (A/CN.9/196, paras. 17 and 18).

2. One question which arises in this respect is to determine when there is failure to present and when there is delay. Under article 53, a cheque is duly presented if, *inter alia*, it is presented within 120 days of its stated date. Therefore, it would follow that there is no delay in presentment if the holder presented the cheque, say, within 119 days of its stated date.

Query: if the cheque is not presented within 120 days, does this constitute failure to present or delay?

3. A second question is whether the drawer whose liability on the cheque is for, say, SwF 1000 and who, because of the delay in presentment, suffers a loss of, say, SwF 250, should now be liable on the cheque for SwF 750, or whether he should be liable for SwF 1000 (the amount of the cheque) but have an action for damages outside the cheque for SwF 250?

Article X¹⁰

(1) Any statement written on a cheque indicating certification, confirmation, acceptance, visa or any other equivalent expression has only the effect to ascertain the existence of funds and prevents the withdrawal of such funds by the drawer, or the use of such funds by the drawee for purposes other than payment of the cheque bearing such a statement, before the expiration of the time limit for presentment.

(2) However, a Contracting State may:

(a) Provide that a drawee may accept a cheque; and

(b) Determine the legal effects thereof.

¹⁰ A/CN.9/181, para. 174 (Yearbook ... 1980, part two, II, B), and A/CN.9/196, paras. 23-25 and 38 (Yearbook ... 1981, part two, II, A).

(3) An acceptance must be effected by the signature of the drawee accompanied by the word "accepted" or words of similar import.

Article 43

(1) Payment of a cheque may be guaranteed, as to the whole or part of its amount, for the account of a party by any person, who may or may not have become a party.¹¹

(2) ...

(3) ...

(4) ...

(a) ...

(c) A signature alone on the back of a cheque is an endorsement. A special endorsement of a cheque made payable to bearer does not convert the cheque into an order instrument.¹²

(5) ...

Article 53

...

(a) The holder must present the cheque to the drawee on a business day at a reasonable hour;¹³

(f) A cheque must be presented for payment within 120 days of its stated date;¹⁴

(g) ...

(i) ...

(ii) ...

(iii) ...

(h) A cheque may be presented for payment at a clearing-house of which the drawee is a member.¹⁵

Article 54

(1) ...

(2) ...

[(a) ...

(i) ...

(ii) ...

(iii) ...]

(c) If the cause of delay continues to operate beyond 30 days after the expiration of the time limit for presentment for payment.¹⁶

¹¹ A/CN.9/196, para. 34 (Yearbook ... 1981, part two, II, A).

¹² *Ibid.*, para. 39.

¹³ *Ibid.*, para. 47.

¹⁴ *Ibid.*, para. 49.

¹⁵ This is a re-draft of subparagraph (h) adopted by the Working Group to accord with the style of the preceding subparagraphs. *Ibid.*, para. 47, and A/CN.9/WG.IV/WP.22, article 53 (h) (reproduced in this volume, part two, II, A, 2, (b)).

¹⁶ A/CN.9/196, para. 56 (Yearbook ... 1981, part two, II, A).

Article 55¹⁷

(1) If a cheque is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

(2) Delay in making [due] presentment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered because of the delay.

Note. The rule stated in paragraph (2) is already stated in article 34 (1 *bis*) (see above). Rules as to failure or delay in protest are also stated in article 34.

Article 57

If a cheque has been dishonoured by non-payment, the holder may exercise a right of recourse only after the cheque has been duly protested for dishonour in accordance with the provisions of articles 58 to 61.¹⁸

Article 58

(1) ...

(a) ...

(b) ...

(c) ...

(2) ...

(a) ...

(b) ...

(3) ...

(3 *bis*) Where a cheque is presented to a clearing-house, protest may be replaced by a dated declaration by the clearing-house to the effect that the cheque had been presented to it and has not been paid.¹⁹

(4) A declaration made in accordance with paragraph (3) or (3 *bis*) is deemed to be a protest for the purposes of this Convention.²⁰

Article 60²¹

(1) If a cheque which must be protested for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.

(2) Delay in protesting a cheque for non-payment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered by the delay.

¹⁷ *Ibid.*, paras. 58-62.

¹⁸ *Ibid.*, para. 66. Alignment of the provisions relating to protest for dishonour with the decisions taken in respect of article 55 has been done in the re-drafting of article 34.

¹⁹ *Ibid.*, para. 70; A/CN.9/WG.IV/WP.22, article 58 (3 *bis*) (reproduced in this volume, part two, II, A, 2, (b)).

²⁰ A/CN.9/196, para. 72 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.22, article 58 (4) (reproduced in this volume, part two, II, A, 2 (b)).

²¹ A/CN.9/196, para. 76 (Yearbook ... 1981, part two, II, A).

Note. The rule stated in paragraph (2) is already stated as to the drawer in article 34 (1 *ter*) (see above).

Article 61²²

(1) ...

(2) ...

(a) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;

(b) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made;

(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person;

(e) If presentment for payment is dispensed with in accordance with article 54 (2).

Article 65²³

(1) ...

(2) ...

(a) If after the exercise of reasonable diligence notice cannot be given;

(b) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:

(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.

(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person.

Article 67

(1) The holder may recover from any party liable the amount of the cheque.²⁴

(2) When payment is made after the cheque has been dishonoured, the holder may recover from any party liable the amount of the cheque with interest at the rate specified in paragraph (4) calculated from the date of presentment to the date of payment and any expenses of protest and of the notices given by him.²⁵

(4) ...

Article 68

(1) ...

(a) ...

(b) ...

(c) ...

(2) Notwithstanding article 25 (4), if a party takes up and pays the cheque in accordance with article 67 and the cheque is transferred to him such transfer does not vest in that party the rights to and upon the cheque which any previous protected holder had.²⁶

Article 70

(1) A party is discharged of liability on the cheque when he pays the holder or a party subsequent to himself who has taken up and paid the cheque and is in possession thereof the amount due pursuant to articles 67 and 68.²⁷

(3) A party is not discharged of his liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the cheque or that the holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.²⁸

(4) (a) A person receiving payment of a cheque must, unless agreed otherwise, deliver:

(i) To the drawee making such payment, the cheque [and a receipted account];

(ii) To any other person making such payment, the cheque, a receipted account and any protest.²⁹

(b) ...

(c) If payment is made but the person paying, other than the drawee, fails to obtain the cheque, such person

²⁴ *Ibid.*, para. 97.

²⁵ *Ibid.*, para. 99.

²⁶ *Ibid.*, para. 105.

²⁷ *Ibid.*, para. 107, with the addition of the words "and is in possession thereof" to the text contained therein.

²⁸ *Ibid.*, para. 107.

²² *Ibid.*, paras. 80 and 159. Subparagraph 2 (f) has been deleted (A/CN.9/WG.IV/WP.22, article 61) (reproduced in this volume, part two, II, A, 2, (b)).

²³ (A/CN.9/196, paras. 87-90 (Yearbook ... 1981, part two, II, A).

²⁹ *Ibid.*, para. 109 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.22, article 70 (4) (a) (reproduced in this volume, part two, II, A, 2, (b)).

is discharged but the discharge cannot be set up as a defence against a protected holder.³⁰

Article 71

(1) ...

(2) If the holder who is offered partial payment does not take it, the cheque is dishonoured by non-payment.³¹

(3) ...

(4) If the holder takes partial payment from a party to the cheque:³²

(a) ...

(b) ...

(5) ...

(6) The person receiving the unpaid amount who is in possession of the cheque must deliver to the payor the receipted cheque and any authenticated protest.³³

Article 74 bis

(1) ...³⁴

(2) (a) If, by virtue of the application of paragraph (1) of this article, a cheque drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts on the date of presentment ruling at the place where the cheque must be presented for payment in accordance with article 53 (g).³⁵

(b) If such a cheque is dishonoured by non-payment:

(i) The amount is to be calculated, at the option of the holder, according to the rate of exchange ruling at the date of presentment or at the date of actual payment;³⁶

(ii) Paragraphs (3) and (4) of article 74 are applicable where appropriate.³⁷

³⁰ A/CN.9/196, para. 111 (Yearbook ... 1981, part two, II, A). The Secretariat was of the view that a provision on these lines was not superfluous because the results in question did not clearly emerge from the wording of articles 24 and 25.

³¹ *Ibid.*, para. 122; A/CN.9/WG.IV/WP.22, article 71 (2) (reproduced in this volume, part two, II, A, 2 (b)).

³² A/CN.9/196, para. 126 (Yearbook ... 1981, part two, II, A).

³³ *Ibid.*, para. 131; A/CN.9/WG.IV/WP.22, article 71 (6) (reproduced in this volume, part two, II, A, 2 (b)).

³⁴ Paragraph 1 consists of the text of article 74 bis as appearing, *ibid.*, at para. 138.

³⁵ A/CN.9/196, paras. 135-139 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.22, article 74 bis (2) (a) (reproduced in this volume, part two, II, A, 2, (b)).

³⁶ A/CN.9/196, paras. 135-139 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.22, article 74 bis (2) (b) (ii) (reproduced in this volume, part two, II, A, 2, (b)).

³⁷ A/CN.9/196, paras. 135-139 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.22, article 74 bis (2) (b) (iii) (reproduced in this volume, part two, II, A, 2, (b)).

Article 74 ter

If the drawer countermands the order to the drawee to pay a cheque drawn on him, the drawee is under a duty not to pay.³⁸

Article 79

(1) A right of action arising on a cheque can no longer be exercised after four years have elapsed:

(a) Against the drawer or his guarantor, after the date of the cheque;³⁹

(b) Against an endorser or his guarantor, after the date of protest for dishonour or, where protest is dispensed with, the date of dishonour.⁴⁰

(2) If a party has taken up and paid the cheque in accordance with article 67 or 68 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year after the date on which he took up and paid the cheque.⁴¹

Article 80⁴²

(Paragraph (3) deleted)

Article 82

(1) A party who has paid a lost cheque in accordance with the provisions of article 80 and who is subsequently required to, and does, pay the cheque, or who then loses his right to recover from any party liable to him and such loss of right was due to the fact that the cheque was lost, has the right:⁴³

(a) ...

(b) ...

(2) ...

Article A

(a) A cheque is crossed when it bears across its face two parallel transverse lines.⁴⁴

(b) A crossing is general if it consists of the two lines only or if between the two lines the word "banker" or an equivalent term or the words "and Company" or any abbreviation thereof is inserted; it is special if the name of a banker is so inserted.⁴⁵

³⁸ A/CN.9/196, para. 142 (Yearbook ... 1981, part two, II, A). Article 74 *quater* previously contained in the Uniform Rules has been deleted. *Ibid.*, para. 144.

³⁹ *Ibid.*, para. 149.

⁴⁰ *Ibid.*, para. 150.

⁴¹ *Ibid.*, para. 151; A/CN.9/WG.IV/WP.22, article 79 (2) (reproduced in this volume, part two, II, A, 2, (b)).

⁴² A/CN.9/196, para. 153 (Yearbook ... 1981, part two, II, A).

⁴³ *Ibid.*, para. 157; A/CN.9/WG.IV/WP.22, article 82 (1) (reproduced in this volume, part two, II, A, 2, (b)).

⁴⁴ A/CN.9/196, para. 166 (Yearbook ... 1981, part two, II, A).

⁴⁵ *Ibid.*, para. 168.

- (c) ...
- (d) ...
- (e) ...
- (f) ...

Article B

If a cheque shows on its face the obliteration either of a crossing or of the name of the banker to whom it is crossed, the obliteration is regarded as not having taken place.⁴⁶

Article C

- (1) (a) ...
- (b) ...
- (c) ...

(2) The drawee who pays or the banker who takes a crossed cheque in violation of the provisions of paragraph (1) of this article incurs liability for any damages which a person may have suffered as a result of such violation, provided that such damages do not exceed the amount of the cheque.⁴⁷

Article E

If the crossing on a cheque contains the words "not negotiable" the transferee becomes a holder but cannot become a protected holder in his own right.⁴⁸

Article F

(1) (a) The drawer or the holder of a cheque may prohibit its payment in cash by writing transversally across the face of the cheque the words "payable in account" or words of similar import.

⁴⁶ *Ibid.*, para. 176.

⁴⁷ *Ibid.*, para. 180.

⁴⁸ *Ibid.*, para. 183.

(b) In such a case the cheque can only be paid by the drawee by means of a book-entry.⁴⁹

(2) The drawee who pays such a cheque other than by means of a book-entry incurs liability for any damages which a person may have suffered as a result thereof, provided that such damages do not exceed the amount of the cheque.⁵⁰

(3) If a cheque shows on its face the obliteration of the words "payable in account", the obliteration is regarded as not having taken place.⁵¹

Article a

If a cheque is drawn against insufficient funds, it is nevertheless valid as a cheque.⁵²

Article β⁵³

(1) A cheque which bears a date other than the date on which it was drawn is nevertheless valid as a cheque.

(2) If a cheque is presented before its stated date:

Variant A

- (a) Payment discharges parties liable on the cheque;
- (b) Refusal by the drawee to pay constitutes dishonour.

Variant B

- (a) Payment does not discharge parties liable on the cheque;
- (b) Refusal by the drawee to pay does not constitute dishonour.

⁴⁹ *Ibid.*, para. 187.

⁵⁰ *Ibid.*, para. 189.

⁵¹ *Ibid.*, para. 190.

⁵² *Ibid.*, para. 196.

⁵³ *Ibid.*, paras. 200-203.

(b) *Note by the Secretariat: draft Convention on International Bills of Exchange and International Promissory Notes: text of articles as redrafted by consultants to the Secretariat and by the Working Group at its tenth session (A/CN.9/WG.IV/WP.22)**

Article 22

Variant A

(1) If an endorsement is forged, any person has against the forger, against the person who took the instrument directly from the forger and against the drawee

who paid the instrument to the forger the right to recover compensation for any damage that he may have suffered because of the forgery.¹

* 12 June 1981. The text of the articles set forth herein is of the following kinds: (a) text as re-drafted by Professors A. Barak and W. Vis, consultants to the Secretariat, in accordance with requests of the Working Group made at its tenth session (b) text as amended by the Working Group at its tenth session and (c) text aligned with amended text of the draft Uniform Rules applicable to International Cheques. References are given to relevant paragraphs in the report

of the tenth session (A/CN.9/196) (Yearbook . . . 1981, part two, II, A) and to the articles of the draft Uniform Rules applicable to International Cheques as re-drafted or amended (A/CN.9/WG.IV/WP.21) (reproduced in this volume, part two, II, A, 2, (a)). Points of ellipsis against a paragraph or subparagraph indicate that no change has been made to the text of that paragraph or subparagraph. (Footnote in original).

¹ A/CN.9/196, paras. 113-118 (Yearbook . . . 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 22, Variant A (reproduced in this volume, part two, II, A, 2, (a)).

(2) ...

Note. The effect of the above rule would be that, for purposes of the drawee's liability to pay compensation to the person who suffered loss because of a forged endorsement, it is immaterial whether the drawee paid with or without knowledge of the forgery.

Variant B

(1) If an endorsement is forged, any party has against the forger, against the person who took the instrument directly from the forger and against the drawee who paid the instrument to the forger with knowledge of the forgery the right to recover compensation for any damage that he may have suffered because of the forgery.²

(2) ...

Note. The effect of the above rule would be that an action for damages would not lie against a drawee who paid without knowledge of the forgery.³

Article 53

...

(a) ...

(b) ...

(c) ...

(d) ...

(e) ...

(f) ...

(g) ...

(i) ...

(ii) ...

(iii) ...

(h) An instrument may be presented for payment at a clearing-house of which the drawee is a member.⁴

Article 58

(1) ...

(a) ...

(b) ...

(c) ...

(2) ...

(a) ...

(b) ...

(3) ...

(3 *bis*) Where an instrument is presented to a clearing-house, protest may be replaced by a dated declaration by the clearing-house to the effect that the instrument had been presented to it and has not been paid.⁵

(4) A declaration made in accordance with paragraph (3) or (3 *bis*) is deemed to be a protest for the purposes of this Convention.⁶

Article 61

(Paragraph (2), subparagraph (f), deleted)⁷

Article 67

(1) ...

(a) ...

(b) ...

(i) The amount of the instrument with interest, if interest has been stipulated for, from the date of presentment;⁸

(ii) ...

(iii) ...

(c) ...

(i) ...

(ii) ...

(2) ...

(3) ...

Article 70

(1) ...

(a) ...

(b) ...

(2) ...

(3) ...

(4) (a) A person receiving payment of an instrument must, unless agreed otherwise, deliver:

² A/CN.9/196, paras. 113-118 (Yearbook ... 1981, part two, II, A), A/CN.9/WG.IV/WP.21, article 22, Variant B (reproduced in this volume, part two, II, A, 2, (a)).

³ One of these Variants could be adopted in both the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Uniform Rules applicable to International Cheques. A further possibility would be that Variant A is adopted in the draft Convention and Variant B in the draft Uniform Rules.

⁴ A/CN.9/196, para. 48 (Yearbook ... 1981, part two, II, A), A/CN.9/WG.IV/WP.21, article 53 (h) (reproduced in this volume, part two, II, A, 2, (a)).

⁵ A/CN.9/196, para. 70 (Yearbook ... 1981, part two, II, A), A/CN.9/WG.IV/WP.21, article 58 (3 *bis*) (reproduced in this volume, part two, II, A, 2, (a)).

⁶ A/CN.9/196, para. 72 (Yearbook ... 1981, part two, II, A), A/CN.9/WG.IV/WP.21, article 58 (4) (reproduced in this volume, part two, II, A, 2, (a)).

⁷ A/CN.9/196, para. 159 (Yearbook ... 1981, part two, II, A), A/CN.9/WG.IV/WP.21, article 61 (paragraph 2 (f) deleted) (reproduced in this volume, part two, II, A, 2, (a)).

⁸ A/CN.9/196, paras. 100-101 (Yearbook ... 1981, part two, II, A).

- (i) to the drawee making such payment the instrument [and a receipted account];
- (ii) to any other person making such payment, the instrument, a receipted account and any protest.⁹
- (b) ...
- (c) If payment is made but the person paying, other than the drawee, fails to obtain the instrument, such person is discharged but the discharge cannot be set up as a defence against a protected holder.¹⁰

Article 71

- (1) ...
- (2) If the holder who is offered partial payment does not take it, the instrument is dishonoured by non-payment.¹¹
- (3) ...
- (a) ...
- (b) ...
- (4) ...
- (a) ...
- (b) ...
- (5) ...
- (6) The person receiving the unpaid amount who is in possession of the instrument must deliver to the payor the receipted instrument and any authenticated protest.¹²

Article 74 bis

- (1) ...¹³
- (2) (a) If, by virtue of the application of paragraph (1) of this article, an instrument drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts on the date of presentment ruling at the place where the instrument must be presented for payment in accordance with article 53 (g);¹⁴

⁹ A/CN.9/196, para. 109 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 70 (4) (a) (reproduced in this volume, part two, II, A, 2 (a)).

¹⁰ A/CN.9/196, para. 111 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 70 (4) (c), and note thereto (reproduced in this volume, part two, II, A, 2 (a)).

¹¹ A/CN.9/196, para. 122 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 71 (2) (reproduced in this volume, part two, II, A, 2, (a)).

¹² A/CN.9/196, para. 131 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 71 (6) (reproduced in this volume, part two, II, A, 2, (a)).

¹³ Paragraph 1 consists of the text of article 74 bis as appearing in A/CN.9/181, Annex (Yearbook ... 1980, part two, III, B).

¹⁴ A/CN.9/196, paras. 135-139 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 74 bis (2) (a) (reproduced in this volume, part two, II, A, 2, (a)).

- (b) (i) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated, at the option of the holder, at the rate of exchange ruling at the date of dishonour, or at the date of actual payment;
- (ii) If such an instrument is dishonoured by non-payment, the amount is to be calculated, at the option of the holder, according to the rate of exchange ruling at the date of presentment or at the date of actual payment.¹⁵
- (iii) Paragraphs (3) and (4) of article 74 are applicable where appropriate.¹⁶

Article 79¹⁷

- (1) ...
- (a) Against the maker, or his guarantor, of a note payable on demand, after the date of the note;
- (b) Against the acceptor or the maker or their guarantor of an instrument payable at a definite time, after the date of maturity;
- (c) Against the acceptor of a bill payable on demand, after the date on which it was accepted;
- (d) Against the drawer or an endorser or their guarantor, after the date of protest for dishonour, or where protest is dispensed with, the date of dishonour.
- (2) If a party has taken up and paid the instrument in accordance with article 67 or 68 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year after the date on which he took up and paid the instrument.

Article 82

- (1) A party who has paid a lost instrument in accordance with the provisions of article 80 and who is subsequently required to, and does, pay the instrument, or who then loses his right to recover from any party liable to him and such loss of right was due to the fact that the instrument was lost, has the right:¹⁸

- (a) ...
- (b) ...
- (2) ...

¹⁵ A/CN.9/196, paras. 135-137 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 74 bis (2) (b) (i) (reproduced in this volume, part two, II, A, 2, (a)).

¹⁶ A/CN.9/196, paras. 135-137 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 74 bis (2) (b) (ii) (reproduced in this volume, part two, II, A, 2, (a)).

¹⁷ A/CN.9/196, paras. 148 and 151 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 79 (2) (reproduced in this volume, part two, II, A, 2, (a)).

¹⁸ A/CN.9/196, para. 157 (Yearbook ... 1981, part two, II, A); A/CN.9/WG.IV/WP.21, article 82 (1) (reproduced in this volume, part two, II, A, 2, (a)).

- (c) *Note by the Secretariat: uniform rules applicable to international cheques (A/CN.9/WG.IV/WP.23); annex: note by the observer of the Hague Conference on Private International Law**

ANNEX

Note by the observer of the Hague Conference on Private International Law intended for the Working Group on International Negotiable Instruments

Gaps in the treaties and conflicts of internal laws

At the tenth session of the Working Group on International Negotiable Instruments held at Vienna from 5 to 16 January 1981, a number of issues relating to cheques were deliberately left to national law and are therefore not dealt with in the new Convention under preparation (such as, it will be recalled: the effect of the death or incapacity of the drawer, the obligation of the bank to honour a cheque, the legal consequences of accepting a cheque etc.). Leaving certain issues outside a treaty for the unification of law naturally poses the question of which law is to govern these issues, and this is the main point which will be studied in this note.

A more delicate problem arises in the context of the Convention on International Cheques currently under preparation. The Convention is not intended to replace, in the State ratifying it, the internal rules on cheques already existing in that State, but rather to coexist with them, leaving the parties free to choose whether their relations are to be governed by the new treaty rules or by the old system. It is, therefore, possible for different internal laws applicable to the gaps in the new Convention to exist within the same State. This is the main issue, for which a solution is proposed in this note.

It should be pointed out that the problem arises not only in the context of the new article 74 *quater*, as would seem to be suggested in the Report of the Working Group on its tenth session (A/CN.9/196, pp. 26-27),** but in relation to *all* issues not dealt with in the Convention on International Cheques. Moreover, the same problem arises in the context of the draft Convention on International Bills of Exchange and International Promissory Notes, so that the solution proposed herein will consequently be valid for both draft Conventions.

A. *Gaps in the treaties*

It is common practice for an international convention to leave certain issues to "national law", either expressly or by leaving gaps in the text of the convention. Leaving issues to national law in this way merely indicates the limits of the process of unification of the laws of different member States; whatever is not unified is left to the jurisdiction of "national" law, i.e. to internal, non-treaty law. Most frequently such "national" law will be the internal law of the State, party to the unifying convention, whose law is found to be applicable under the rules of conflict of the forum. However, when the international convention itself limits its own scope of application in a specific way, without regard to the rules of conflict of laws (see, for example, the United Nations Convention on Contracts for the International Sale of Goods, article 1, paragraph (1) (a)),*** the court must then determine which law should govern issues which have not been dealt with under the unifying treaty.

* 16 June 1981. In the course of its deliberations on the draft uniform rules applicable to international cheques, the Working Group decided that certain issues not be dealt with in the draft text but left to national law. Such a decision was, for example, taken at its tenth session with regard to the question whether the drawee was or was not obliged to pay a cheque upon notice of the death of the drawer (A/CN.9/196, para. 144) (Yearbook . . . 1981, part two, II, A). On this occasion, the observer of the Hague Conference on Private International Law indicated his willingness to prepare a short study on the conflicts aspects of this issue. This study by Mr. Michel Pelichet, Deputy Secretary-General of the Hague Conference on Private International Law, is reproduced in the annex.

** Yearbook . . . 1981, part two, II, A.

*** Yearbook . . . 1980, part three, I, B.

During preparation of the United Nations Convention on Contracts for the International Sale of Goods, adopted at Vienna on 11 April 1980, this question was discussed at length and delegates finally adopted the rule by which gaps in the Convention were to be governed by the law determined under the rules of private international law (article 7, paragraph (2)).*

This solution seems to be entirely satisfactory in that it covers both cases where the unifying Convention will apply, i.e.:

(a) The unifying Convention applies by operation of the conflicts rule of the forum, so that the express or implicit reference to national law is to be understood as being to the internal, non-treaty law of the State party to the Convention;

(b) The Convention applies by virtue of a provision limiting its own scope of application and the law applicable to gaps, which will not therefore necessarily be the internal law of the State party to the Convention, must be subsequently determined by applying the rules of private international law of the forum.

For this reason the observer of the Hague Conference proposes to the Working Group on International Negotiable Instruments that a new article should be adopted on the lines of article 7, paragraph (2), of the United Nations Convention on Contracts for the International Sale of Goods,** which might read as follows:

"Article X

"Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the law applicable by virtue of the rules of private international law."

It should be pointed out that article 7 of the United Nations Convention provides that gaps in the Convention should be governed above all "in conformity with the general principles on which it is based". This reference to general principles may be justifiable in a general convention on the international sale of goods, a field in which unification has proved difficult because of the multiplicity of laws and the existence of commercial customs and practices, but in the opinion of the observer of the Hague Conference, such a reference cannot be justified in conventions on negotiable instruments. The question of negotiable instruments is extremely technical and structured and it is difficult to see to which principles such a reference would refer. To have gaps in the Convention governed solely by the law applicable in conformity with the rules of private international law seems sufficient to cover all cases.

B. *Conflicts of internal laws*

Once it has been determined which State's law is to govern the questions not dealt with in the unifying Convention, there is the problem of which internal provisions of that State the court should apply. As has been mentioned above, since the new conventions on negotiable instruments are not intended to replace the internal laws of the States which ratify them, there will exist within these States alongside the new treaty law, another parallel law dealing with the same issue. Moreover, the general rules of law of these States may also be referred to in issues not dealt with by the conventions under preparation. Therefore, in order to deal with issues not covered by the conventions, a court may have to choose between the parallel law specific to the question and the general rules of law of a State.

A particularly topical example, referred to at the last session of the Working Group, will serve to illustrate the problem faced by the court: following long discussions on article 74 *quater* of the draft Convention on International Cheques,*** as a result of irreconcilable differences of views on this point among the members of the Working Group, it was decided that it should be left to

* Yearbook . . . 1980, part three, I, B.

** Yearbook . . . 1980, part three, I, B.

*** Yearbook . . . 1981, part two, II, A.

national laws to determine the effect of the death or incapacity of the drawer of a cheque. There are many States which in their general law of contracts have a rule under which the death, incapacity or bankruptcy of the principal (in this case the drawer) automatically puts an end to the agent's mandate (For example, the French Civil Code, article 2003; the Swiss Code of Obligations, article 405; etc.). Some of these States have acceded to the Geneva Convention Providing a Uniform Law for Cheques of 19 March 1931, whose article 33 states:

"Neither the death of the drawer or his incapacity taking place after the issue of the cheque should have any effect as regards the cheque."

Let us suppose that one of these States accedes to the new Convention on International Cheques being prepared by UNCITRAL. Since the question of the death or incapacity of the drawer is not dealt with in the Convention, the court, after application of its conflicts rule, will not know whether it should apply the general rules of the State whose law has been declared applicable, in which case the death of the drawer would oblige the drawee not to honour the cheque, or whether the question should be governed by article 33 of the Geneva Convention, in which case the drawee must honour the cheque notwithstanding the death or incapacity of the drawer. It can be seen from this example that the problem is a delicate one. There are three solutions for dealing with it:

(a) To omit any mention in the new Convention and leave the solution of the problem to the discretion of the court. In the opinion of the observer of the Hague Conference, this is not a good solution since it will leave not only the court, but the parties themselves in a state of considerable uncertainty. In countries which have such dual sets of rules, the drawee will not know, in the event of the death or incapacity of the drawer, whether or not to honour the cheque. Moreover, it may destroy the uniformity among those States which have the same general rule concerning agency and which have acceded to the Geneva Convention: in one State the court will be of the opinion that it must apply the general rule, whereas in another it will apply the Geneva Convention provision, all of which, it must be admitted, hardly contributes to unification in this field;

(b) To have the questions not dealt with in the new Convention expressly governed by the general laws of the State whose law is declared applicable. This does not seem to be a very satisfactory solution either, since it would destroy the harmony already existing between States having acceded to a given system (Geneva Convention, Bills of Exchange Act, etc.), while, in States which have acceded to the Geneva Convention, but which have as a general rule the termination of the mandate in case of the death or incapacity of the principal, there would be two different rules for cheques depending on whether the cheques were governed by the Geneva Convention or by the new instrument under preparation;

(d) *Note by the Secretariat: draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles 1-45 as revised by the Drafting Group (A/CN.9/WG.IV/WP.24)**

Article 1

(1) This Convention applies to international bills of exchange and to international promissory notes.

* 30 July 1981. It should be noted that this Working Paper is supplemented and in part superseded by its addenda 1 and 2. The same applies to Working Paper 25 and its addendum 1. As indicated in the report of the Working Group, A/CN.9/210, at paras. 237 and 240 (reproduced in this volume, part two, II, A, 1), the Drafting Group, which began its consideration of the draft Convention on International Bills of Exchange and International Promissory Notes and of the draft Convention on International Cheques during the week prior to the session of the Working Group, continued its work until the last but one day of the session of the Working Group. As a result, some of the articles as originally presented by the Draft-

(c) To adopt in the Convention under preparation a provision whereby gaps in the Convention would be governed by the specific provisions on the subject of the State whose law is declared applicable. This solution appears to be by far the best as it would not create two different systems for cheques in States which have special rules in this field, nor would it destroy the unification already achieved by different groups of States through the Geneva Convention, the Bills of Exchange Act or the Uniform Commercial Code.

For this reason the observer of the Hague Conference proposes to the Working Group on International Negotiable Instruments that article X suggested above should be complemented by a second paragraph as follows:

"If the State, the law of which is found to be applicable under the rules of private international law has, independently of its general rules of law, provisions which are specific [to cheques] [to bills of exchange or promissory notes] for the settlement of the questions referred to in the preceding paragraph, these provisions will be applied with priority over those general rules."

It will be noted that this article is drafted in a very general manner. It is intended to apply not only in the example just considered concerning the death or incapacity of the drawer, but also to any gaps left in either of the conventions currently under preparation within UNCITRAL. The aim of this article is in all cases to have the gaps in either Convention governed in priority by the specific provisions in the field rather than by general rules of law.

C. Conclusion

In conclusion, the observer of the Hague Conference proposes to the Working Group on International Negotiable Instruments that it might adopt, in both the Convention on Bills of Exchange and Promissory Notes and the Convention on International Cheques, an article X which might be placed in the chapter on General Provisions and which would read as follows:

"Article X

"Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the law applicable by virtue of the rules of private international law.

"If the State, the law of which is found to be applicable under the rules of private international law, has, independently of its general rules of law, provisions which are specific [to cheques] [to bills of exchange and promissory notes] for the settlement of the questions referred to in the preceding paragraph, these provisions will be applied with priority over those general rules."

(2) An international bill of exchange is a written instrument which:

(a) Contains, in the text thereof, the words "international bill of exchange [Convention of . . .]";*

ing Group were subsequently modified by it in the light of deliberations in the Working Group. Also, lack of time prevented the Drafting Group from establishing the texts in complete and final form. The complete texts, compiled by the Secretariat upon request by the Working Group, are to be found in A/CN.9/211 (draft Convention on International Bills of Exchange and International Promissory Notes) and A/CN.9/212 (draft Convention on International Cheques), reproduced in this volume, part two, II, A, 3 and 5.

* Brackets indicate matters which have been reserved for further consideration at a later date. (Footnote in original).

(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the bill is drawn;

(ii) The place indicated next to the signature of the drawer;

(iii) The place indicated next to the name of the drawee;

(iv) The place indicated next to the name of the payee;

(v) The place of payment;

(f) Is signed by the drawer.

(3) An international promissory note is a written instrument which:

(a) Contains, in the text thereof, the words "international promissory note [Convention of . . .]";

(b) Contains an unconditional promise whereby the maker undertakes to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the note is made;

(ii) The place indicated next to the signature of the maker;

(iii) The place indicated next to the name of the payee;

(iv) The place of payment;

(f) Is signed by the maker.

(4) Proof that the statements referred to in paragraph (2) (e) or (3) (e) of this article are incorrect does not affect the application of this Convention.

Article 3

This Convention applies without regard to whether the places indicated on an international bill of exchange or on an international promissory note pursuant to paragraph (2) (e) or (3) (e) of article 1 are situated in Contracting States.

Article 4

In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application.

Article 5

In this Convention:

(1) "Bill" means an international bill of exchange governed by this Convention;

(2) "Note" means an international promissory note governed by this Convention;

(3) "Instrument" means a bill or a note;

(4) "Drawee" means the person on whom a bill is drawn but who has not accepted it;

(5) "Payee" means the person in whose favour the drawer directs payment to be made or to whom the maker promises to pay;

(6) "Holder" means a person in possession of an instrument in accordance with article 13 *bis*;

(7) "Protected holder" means the holder of an instrument which, when he became a holder, was complete and regular on its face, provided that:

(a) He was, at that time, without knowledge of circumstances giving rise to a claim to or defence upon the instrument referred to in article 24 or of the fact that it was dishonoured by non-acceptance or non-payment;

(b) The time limit provided by article 53 for presentment of that instrument for payment had not then expired.

(8) "Party" means any person who has signed an instrument [as drawer, maker, acceptor, endorser or guarantor];

(9) "Maturity" means the date of payment referred to in article 9;

(10) "Signature" includes a signature by stamp, symbol, facsimile, perforation or other mechanical means* and "forged signature" includes a signature by the wrongful or unauthorized use of such means.

Article 6

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

Article 7

The sum payable by an instrument is deemed to be a definite sum although the instrument states that it is to be paid:

(a) With interest;

*

Article (X)

A Contracting State whose legislation requires that a signature on an instrument be handwritten may, at the time of signature, ratification or accession, make a declaration to the effect that a signature placed on an instrument in its territory must be handwritten. (Footnote in original).

- (b) By instalments at successive dates;
- (c) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due;
- (d) According to a rate exchange indicated on the instrument or to be determined as directed by the instrument; or
- (e) In a currency other than the currency in which the amount of the instrument is expressed.

Article 8

- (1) If there is a discrepancy between the amount of the instrument expressed in words and the amount expressed in figures, the amount of the instrument is the amount expressed in words.
- (2) If the amount of the instrument is expressed in a currency having the same description as that of at least one other State than the State where payment is to be made as indicated on the instrument and the specified currency is not identified as the currency of any State, the currency is to be considered as the currency of the State where payment is to be made.
- (3) If any instrument states that it is to be paid with interest, without specifying the date from which interest is to run, interest runs from the date of the instrument.
- (4) A stipulation stating that the sum is to be paid with interest is deemed not to have been written on the instrument unless it indicates the rate at which interest is to be paid.

Article 9

- (1) An instrument is deemed to be payable on demand:
 - (a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or
 - (b) If no time for payment is expressed.
- (2) An instrument payable at a definite time which is accepted or endorsed or guaranteed after maturity is an instrument payable on demand as regards the acceptor, the endorser or the guarantor.

- (3) An instrument is deemed to be payable at a definite time if it states that it is payable:
 - (a) On a stated date or at a fixed period after a stated date or at a fixed period after the date of the instrument; or
 - (b) At a fixed period after sight; or
 - (c) By instalments at successive dates; or
 - (d) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due.

(4) The time of payment of an instrument payable at a fixed period after date is determined by reference to the date of the instrument.

(5) The maturity of a bill payable at a fixed period after sight is determined by the date of the acceptance.

(6) [The maturity of a note payable at a fixed period after sight is determined by the date of the visa signed by the maker on the note or, if signature is refused, from the date of presentment.]

(6 bis) The maturity of an instrument payable on demand is the date on which the instrument is presented for payment.

(7) Where an instrument is drawn, or made, payable at one or more months after a stated date or after the date of the instrument or after sight, the instrument matures on the corresponding date of the month when payment must be made. If there is no corresponding date, the instrument matures on the last day of that month.

Article 10

- (1) A bill may:
 - (a) Be drawn upon two or more drawees;
 - (b) Be drawn by two or more drawers;
 - (c) Be payable to two or more payees.
- (2) A note may:
 - (a) Be made by two or more makers;
 - (b) Be payable to two or more payees.

(3) If an instrument is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the instrument may exercise the rights of a holder. In any other case the instrument is payable to all of them and the rights of a holder can only be exercised by all of them.

Article 10 bis

A bill may:

- (a) Be drawn by the drawer on himself;
- (b) Be drawn payable to his order.

Article 11

(1) An incomplete instrument which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) or (a) and (f) of paragraph (3) but which lacks other elements pertaining to one or more of the requirements set out in paragraphs (2) or (3) of article 1 may be completed and the instrument so completed is effective as a bill or a note.

(2) When such an instrument is completed otherwise than in accordance with agreements entered into:

(a) A party who signed the instrument before the completion may invoke the non-observance of the agreement as a defence against a holder, provided the holder had knowledge of the non-observance of the agreement when he became a holder;

(b) A party who signed the instrument after the completion is liable according to the terms of the instrument so completed.

Article 13

An instrument is transferred:

(a) By endorsement and delivery of the instrument by the endorser to the endorsee; or

(b) By mere delivery of the instrument if the last endorsement is in blank.

New Article

(to be inserted between article 13 and article 13 bis)

(1) An endorsement must be written on the instrument or on a slip affixed thereto (*allonge*). It must be signed.

(2) An endorsement may be made:

(a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the instrument is payable to any person in possession thereof;

(b) Special, by a signature accompanied by an indication of the person to whom the instrument is payable.

Article 13 bis

(1) A person is a holder if he is:

(a) The payee in possession of the instrument; or

(b) In possession of an instrument which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

(2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.

(3) A person is not prevented from being a holder by the fact that the instrument was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon, the instrument.

Article 15

The holder of an instrument on which the last endorsement is in blank may:

(a) Further endorse the instrument either in blank or to a specified person; or

(b) Convert the blank endorsement into a special endorsement by indicating therein that the instrument is payable to himself or to some other specified person; or

(c) Transfer the instrument in accordance with paragraph (b) of article 13.

Article 16

When the drawer, or the maker has inserted in the instrument, or an endorser in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the transferee does not become a holder except for purposes of collection.

Article 17

(1) (deleted)

(2) A conditional endorsement transfers the instrument whether or not the condition is fulfilled.

(3) A claim to or a defence upon the instrument based on the fact that the condition was not fulfilled may not be raised except by the party who endorsed conditionally against his immediate transferee.

Article 18

An endorsement in respect of a part of the sum due under the instrument is ineffective as an endorsement.

Article 19

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the instrument.

Article 20

(1) When an endorsement contains the words "for collection", "for deposit", "value in collection", "by procuration", "pay any bank", or words of similar import, authorizing the endorsee to collect the instrument (endorsement for collection), the endorsee:

(a) May only endorse the instrument for purposes of collection;

(b) May exercise all the rights arising out of the instrument;

(c) Is subject to all claims and defences which may be set up against the endorser.

(2) The endorser for collection is not liable upon the instrument to any subsequent holder.

Article 21

The holder of an instrument may transfer it to a prior party or the drawee in accordance with article 13; nevertheless,

less, in the case where the transferee was a prior holder of the instrument, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

Article 21 bis

An instrument may be transferred in accordance with article 13 after maturity, except by the drawee, the acceptor or the maker.

Article 22

(1) (Not considered by the Drafting Group)

(2) For the purposes of this article, an endorsement placed on an instrument by a person in a representative capacity without authority has the same effects as a forged endorsement.

Article 23

(1) The holder of an instrument has all the rights conferred on him by this Convention against the parties to the instrument.

(2) The holder is entitled to transfer the instrument in accordance with article 13.

Article 24

(1) A party may set up against a holder who is not a protected holder:

(a) Any defence available under this Convention;

(b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

(c) Any defence to contractual liability based on a transaction between himself and the holder;

(d) Any defence based on incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence;

(2) The rights to an instrument of a holder who is not a protected holder are subject to any valid claim to the instrument on the part of any person.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

(a) Such third person asserted a valid claim to the instrument; or

(b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft.

Article 25

(1) A party may not set up against a protected holder any defence except:

(a) Defences under articles 27 (1), 28, 29 (1), 30 (2, 3), 50, 55, 57, 60 and 79 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;

(c) Defences based on the incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a protected holder are not subject to any claim to the instrument on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that person.

Article 25 bis

The transfer of an instrument by a protected holder vests in any subsequent holder the rights to and upon the instrument which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to or a defence upon the instrument.

Article 26

Every holder is presumed to be protected holder, unless the contrary is proved.

Article 27

(1) Subject to the provisions of articles 28 and 30, a person is not liable on an instrument unless he signs it.

(2) A person who signs in a name which is not his own is liable as if he had signed it in his own name.

Article 28

A forged signature on an instrument does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed the instrument himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own.

Article 29

(1) If an instrument has been materially altered:

(a) Parties who have signed the instrument subsequent

to the material alteration are liable thereon according to the terms of the altered text;

(b) Parties who have signed the instrument before the material alteration are liable thereon according to the terms of the original text. Nevertheless a party who has himself made, authorized, or assented to, the material alteration is liable on the instrument according to the terms of the altered text.

(2) Failing proof to the contrary, a signature is deemed to have been placed on the instrument after the material alteration.

(3) Any alteration is material which modifies the written undertaking on the instrument of any party in any respect.

Article 30

(1) An instrument may be signed by an agent.

(2) The signature of an agent placed by him on an instrument in a representative capacity for a named principal and with the authority of that principal, or the signature of a principal placed on the instrument by an agent with his authority, imposes liability on the principal and not the agent.

(3) A signature placed on an instrument by a person as agent but without authority to sign or exceeding his authority or by an agent with authority to sign but not showing on the instrument that he is signing in a representative capacity for a named person, or showing on the instrument that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.

(4) The question whether a signature was placed on the instrument in a representative capacity may be determined only by reference to what appears on the instrument.

(5) A person who is liable pursuant to paragraph 3 and who pays the instrument has the same rights as the person for whom he purported to act would have had if that person had paid the instrument.

Article 30 bis

The order to pay contained in a bill does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee outside the bill.

Article 34

(1) The drawer engages that upon dishonour of the bill by non-acceptance or non-payment, and upon necessary protest, he will pay to the holder or to any party who takes up and pays the bill in accordance with article 67 the

amount of the bill, and any interest and expense which may be recovered under article 67 or 68.

(2) The drawer may exclude or limit his own liability by an express stipulation on the bill. Such stipulation has effect only with respect to the drawer.

Article 34 bis

(1) The maker engages that he will pay to the holder or to any party who takes up and pays the note in accordance with article 67 the amount of the note, and any interest and expenses which may be recovered under article 67 or 68.

(2) The maker may not exclude or limit his own liability by a stipulation on the note. Any such stipulation is without effect.

Article 36

(1) The drawee is not liable on a bill until he accepts it.

(2) The acceptor engages that he will pay to the holder or to any party who takes up and pays the bill in accordance with article 67 the amount of the bill, and any interest and expenses which may be recovered under article 67 or 68.

Article 37

An acceptance must be written on the bill and may be effected:

(a) By the signature of the drawee accompanied by the word "accepted" or by words of similar import; or

(b) By the signature alone of the drawee.

Article 38

(1) An incomplete instrument which satisfies the requirements set out in article 1 (2) (a) may be accepted by the drawee before it has been signed by the drawer, or while otherwise incomplete.

(2) A bill may be accepted before, at or after maturity, or after it has been dishonoured by non-acceptance or non-payment.

(3) When a bill drawn payable at a fixed period after sight, or a bill which must be presented for acceptance before a specified date, is accepted, the acceptor must indicate the date of his acceptance; failing such indication by the acceptor, the drawer or the holder may insert the date of acceptance.

(4) If a bill drawn payable at a fixed period after sight is dishonoured by non-acceptance and the drawee subsequently accepts it, the holder is entitled to have the acceptance dated as of the date on which the bill was dishonoured.

Article 39

(1) An acceptance must be unqualified. An acceptance is qualified if it is conditional or varies the terms of the bill.

(2) If the drawee stipulates on the bill that his acceptance is subject to qualification:

(a) He is nevertheless bound according to the terms of his qualified acceptance;

(b) The bill is dishonoured by non-acceptance.

(2 bis) An acceptance relating to only a part of the amount of the bill is a qualified acceptance. If the holder takes such an acceptance, the bill is dishonoured by non-acceptance only as to the remaining parts.

(3) An acceptance indicating that payment will be made at a particular address or by a particular agent is not a qualified acceptance, provided that:

(a) The place in which payment is to be made is not changed;

(b) The bill is not drawn payable by another agent.

Article 41

(1) The endorser engages that upon dishonour of the instrument by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder or to any party who takes up and pays the bill in accordance with article 67 the amount of the instrument, and any interest and expenses which may be recovered under article 67 or 68.

(2) The endorser may exclude or limit his own liability by an express stipulation on the instrument. Such stipulation has effect only with respect to that endorser.

Article 42

(1) Any person who transfers an instrument by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer:

(a) A signature on the instrument was forged or unauthorized; or

(b) The instrument was materially altered; or

(c) A party has a valid claim or defence against him; or

(d) The bill was dishonoured by non-acceptance or non-payment or the note was dishonoured by non-payment.

(2) The damages recoverable under paragraph (1) may not exceed the amount referred to in article 67 or 68.

(3) Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the instrument without knowledge of such defect.

Article 43

(1) Payment of an instrument, whether or not it has been accepted, may be guaranteed, as to the whole or part of its amount, for the account of a party or the drawee. A guarantee may be given by any person who may or may not already be a party.

(2) A guarantee must be written on the instrument or on a slip affixed thereto (*allonge*).

(3) A guarantee is expressed by the words: "guaranteed", "*aval*", "good as *aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires:

(a) A signature alone on the front of the instrument, other than that of the drawer or the drawee, is a guarantee;

(b) The signature alone of the drawee on the front of the instrument is an acceptance; and

(c) A signature alone on the back of the instrument other than that of the drawee is an endorsement.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the acceptor or the drawee in the case of a bill, and the maker in the case of a note.

Article 44

(1) A guarantor is liable on the instrument to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the instrument.

(2) If the person for whom he has become guarantor is the drawee, the guarantor undertakes to pay the bill when due.

Article 45

The guarantor who pays the instrument has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

- (e) *Note by the Secretariat: draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles 46-85 as revised by the Drafting Group: corrections made by the Drafting Group to articles 1-45 (A/CN.9/WG.IV/WP.24/Add.1)**

**CORRECTIONS MADE BY THE DRAFTING GROUP TO
ARTICLES 1-45 (ISSUED AS A/CN.9/WG.IV/WP.24)**

Article 8

In the penultimate line of paragraph (2), insert the word "particular" before the word "State".

Article 11

In the second line of paragraph (2), replace the word "agreements" by "an agreement".

Article 25 bis

Insert "(1)" before the existing paragraph.

Add a new paragraph reading as follows:

"(2) If a party pays the instrument in accordance with article 67 and the instrument is transferred to him, such transfer does not vest in that party the rights to and upon the instrument which any previous protected holder had."

Article 34

In the third line of paragraph (1), delete the words "takes up and".

Article 34 bis

In the second line of paragraph (1), delete the words "takes up and".

Article 36

In the second line of paragraph (2), delete the words "takes up and".

Article 41

In the third line of paragraph (1), delete the words "takes up and".

**TEXT OF DRAFT ARTICLES 46-85 AS REVISED
BY THE DRAFTING GROUP**

Article 46

- (1) A bill may be presented for acceptance.
- (2) A bill must be presented for acceptance:

(a) When the drawer has stipulated on the bill that it must be presented for acceptance;

(b) When the bill is drawn payable at a fixed period after sight; or

(c) When the bill is drawn payable elsewhere than at the residence or place of business of the drawee, except where such a bill is payable on demand.

Article 47

(1) Notwithstanding the provisions of article 46 the drawer may stipulate on the bill that it must not be presented for acceptance or that it must not be so presented before a specified date or before the occurrence of a specified event.

(2) If a bill is presented for acceptance notwithstanding a stipulation permitted under paragraph (1) and acceptance is refused, the bill is not thereby dishonoured.

(3) If the drawee accepts a bill notwithstanding a stipulation that it must not be presented for acceptance, the acceptance is effective.

Article 48

A bill is duly presented for acceptance if it is presented in accordance with the following rules:

(a) The holder must present the bill to the drawee on a business day at a reasonable hour;

(b) A bill drawn upon two or more drawees may be presented to any one of them, unless the bill clearly indicates otherwise;

(c) Presentment for acceptance may be made to a person or authority other than the drawee if that person or authority is entitled under the applicable law to accept the bill;

(d) If a bill is drawn payable on a fixed date, presentment for acceptance must be made before or on the date of maturity;

(e) A bill drawn payable on demand or at a fixed period after sight must be presented for acceptance within one year of its date;

(f) A bill in which the drawer has stated a date or time-limit for presentment for acceptance must be presented on the stated date or within the stated time-limit.

Article 49

Presentment for acceptance is dispensed with:

- (a) If the drawee is dead or has no longer the power

* 31 July 1981.

freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to incur liability on the instrument as an acceptor, or if the drawee is a corporation, partnership, association or other legal entity which has ceased to exist;

(b) When, with reasonable diligence, presentment cannot be effected within the time-limits prescribed for presentment for acceptance.

Article 50

If a bill which must be presented for acceptance is not so presented, the drawer, the endorsers and their guarantors are not liable on the bill.

Article 51

(1) A bill is considered to be dishonoured by non-acceptance:

(a) When the drawee, upon due presentment, expressly refuses to accept the bill or acceptance cannot be obtained with reasonable diligence or when the holder cannot obtain the acceptance to which he is entitled under this Convention;

(b) If presentment for acceptance is dispensed with pursuant to article 49, unless the bill is in fact accepted.

(2) If a bill is dishonoured by non-acceptance the holder may:

(a) Subject to the provisions of article 57, exercise an immediate right of recourse against the drawer, the endorsers and their guarantors;

(b) Exercise an immediate right of recourse against the guarantor of the drawee.

Article 53

An instrument is duly presented for payment if it is presented in accordance with the following rules:

(a) The holder must present the instrument to the drawee or to the acceptor or to the maker on a business day at a reasonable hour;

(b) A bill drawn upon or accepted by two or more drawees, or a note signed by two or more makers, may be presented to any one of them, unless the instrument clearly indicates otherwise;

(c) If the drawee or the acceptor or the maker is dead, presentment must be made to the persons who under the applicable law are his heirs or the persons entitled to administer his estate;

(d) Presentment for payment may be made to a person or authority other than the drawee, the acceptor or the maker if that person or authority is entitled under the applicable law to pay the instrument;

(e) An instrument which is not payable on demand must be presented for payment on the date of maturity or on one of the two business days which follow:

(f) An instrument which is payable on demand must be presented for payment within one year of its date;

(g) An instrument must be presented for payment:

(i) At the place of payment specified on the instrument; or

(ii) If no place of payment is specified, at the address of the drawee or the acceptor or the maker indicated on the instrument; or

(iii) If no place of payment is specified and the address of the drawee or the acceptor or the maker is not indicated, at the principal place of business or habitual residence of the drawee or the acceptor or the maker;

(h) An instrument may be presented for payment at a clearing-house of which the drawee or acceptor or the maker is a member.

Article 54

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If an instrument is not payable on demand, and the cause of delay in making presentment continues to operate beyond 30 days after maturity;

(c) If an instrument is payable on demand, and the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment;

(d) If the drawee, the maker or the acceptor has no longer the power freely to deal with his assets, by reason of his insolvency, or is a fictitious person or a person not having capacity to make payment, or if the drawee, the maker or the acceptor is a corporation, partnership, association or other legal entity which has ceased to exist;

(e) [See new paragraph 3 below]

(g) If there is no place at which the instrument must be presented in accordance with article 53 (g).

(3) Presentment for payment is also dispensed with as regards a bill, if the bill has been protested for dishonour by non-acceptance.

Article 55

(1) If a bill is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note is not duly presented for payment, the endorsers and their guarantors are not liable thereon.

(3) Failure to present an instrument for payment does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

Article 56

(1) An instrument is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment or when the holder cannot obtain the payment to which he is entitled under this Convention;

(c) If presentment for payment is dispensed with pursuant to article 54 (2) and the instrument unpaid at maturity.

(2) If a bill is dishonoured by non-payment, the holder may, subject to the provisions of article 57, exercise a right of recourse against the drawer, the endorsers and their guarantors.

(3) If a note is dishonoured by non-payment, the holder may, subject to the provisions of article 57, exercise a right of recourse against the endorsers and their guarantors.

Article 57

If an instrument has been dishonoured by non-acceptance or by non-payment, the holder may exercise a right of recourse only after the instrument has been duly protested for dishonour in accordance with the provisions of articles 58 to 61.

Article 58

(1) A protest is a statement of dishonour drawn up at the place where the instrument has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

(a) The person at whose request the instrument is protested;

(b) The place of protest; and

(c) The demand made and the answer given, if any, or the fact that the drawee or the acceptor or the maker could not be found.

(2) A protest may be made:

(a) On the instrument itself or on a slip affixed thereto (*allonge*); or

(b) As a separate document, in which case it must clearly identify the instrument that has been dishonoured.

(3) Unless the instrument stipulates that protest must be made, a protest may be replaced by a declaration written on the instrument and signed and dated by the drawee or the acceptor or the maker, or, in the case of an instrument domiciled with a named person for payment, by that named person; the declaration must be to the effect that acceptance or payment is refused.

(3 *bis*) Where an instrument is presented for payment to a clearing-house, protest may be replaced by a dated declaration by the clearing-house to the effect that the instrument has been presented to it and has not been paid.

(4) A declaration made in accordance with paragraph (3) or (3 *bis*) is deemed to be a protest for the purposes of this Convention.

Article 59

(1) Protest for dishonour of a bill by non-acceptance must be made on the day on which the bill is dishonoured or on one of the two business days which follow.

(2) Protest for dishonour of an instrument by non-payment must be made on the day on which the instrument is dishonoured or on one of the two business days which follow.

Article 60

(1) If a bill which must be protested for non-acceptance or for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note which must be protested for non-payment is not duly protested, the endorsers and their guarantors are not liable thereon.

(3) Failure to protest an instrument does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

Article 61

(1) Delay in protesting an instrument for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-acceptance or by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If the cause of delay in making protest continues to operate beyond 30 days after the date of dishonour;

(c) As regards the drawer of a bill, if the drawer and the drawee or the acceptor are the same person;

(e) If presentment for acceptance or for payment is dispensed with in accordance with article 49 or 54 (2).

Article 62

(1) The holder, upon dishonour of a bill by non-acceptance or by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.

(2) The holder, upon dishonour of a note by non-payment, must give notice of such dishonour to the endorsers and their guarantors.

(3) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the instrument.

(4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the instrument against the party notified.

Article 63

(1) Notice of dishonour may be given in any form whatever and in any terms which identify the instrument and state that it has been dishonoured. The return of the dishonoured instrument is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.

(2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.

(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

Article 64

Notice of dishonour must be given within the two business days which follow:

(a) The day of protest or, if protest is dispensed with, the day of dishonour; or

(b) The receipt of notice given by another party.

Article 65

(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(2) Notice of dishonour is dispensed with:

(a) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If after the exercise of reasonable diligence notice cannot be given;

(c) As regards the drawer of a bill, if the drawer and the drawee or the acceptor are the same person.

Article 66

Failure to give notice of dishonour renders a person who is required to give such notice under article 62 to a party who is entitled to receive such notice liable for any damages which that party may suffer directly from such failure, provided that such damages do not exceed the amount referred to in article 67 or 68.

Article 66 bis

The holder may exercise his rights on the instrument against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

Article 67

(1) The holder may recover from any party liable:

(a) At maturity: the amount of the instrument with interest, if interest has been stipulated for;

(b) After maturity:

(i) The amount of the instrument with interest, if interest has been stipulated for, from the date of presentment;

- (ii) If interest has been stipulated to be paid after maturity, interest at the rate stipulated, or in the absence of such stipulation interest at the rate specified in paragraph (2), calculated from the date of maturity on the sum specified in paragraph 1 (b) (i);
- (iii) Any expenses of protest and of the notices given by him;
- (c) Before maturity:
 - (i) The amount of the bill with interest, if interest has been stipulated for, to the date of payment, subject to a discount from the date of payment to the date of maturity, calculated in accordance with paragraph (3);
 - (ii) Any expenses of protest and of the notices given by him.
- (2) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the instrument is payable, or if there is no such rate, then at the rate of [] per cent per annum, to be calculated on the basis of the number of days in accordance with the custom of that centre.
- (3) The discount shall be at the official rate (discount rate) or other similar appropriate rate effective on the date when recourse is exercised at the place where the holder has his principal place of business, or if he does not have a place of business his habitual residence, or if there is no such rate then at the rate of [] per cent per annum, to be calculated on the basis of the number of days and in accordance with the custom of that place.

Article 68

- (1) A party who pays an instrument in accordance with article 67 may recover from the parties liable to him:
 - (a) The entire sum which he was obliged to pay in accordance with article 67 and has paid;
 - (b) Interest on that sum at the rate specified in article 67, paragraph 2, from the date on which he made payment;
 - (c) Any expenses of the notices given by him.

Article 70

- (1) A party is discharged of his liability on the instrument when he pays the holder or a party subsequent to himself who has paid the instrument and is in possession thereof the amount due pursuant to articles 67 and 68:
 - (a) At or after maturity; or
 - (b) Before maturity, upon dishonour by non-acceptance.

(2) Payment before maturity other than under paragraph (1) (b) of this article does not discharge the party making the payment of his liability on the instrument except in respect of the person to whom payment was made.

(3) A party is not discharged of his liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(4) (a) (Not considered by the Drafting Group)

(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the instrument to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 56.

(c) (Not considered by the Drafting Group)

Article 71

- (1) The holder is not obliged to take partial payment.
- (2) If the holder who is offered partial payment does not take it, the instrument is dishonoured by non-payment.
- (3) If the holder takes partial payment from the drawee or the acceptor or the maker:
 - (a) The acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; and
 - (b) The instrument is to be considered as dishonoured by non-payment as to the amount unpaid.
- (4) If the holder takes partial payment from a party to the instrument other than the drawee, the acceptor or the maker:
 - (a) The party making payment is discharged of his liability on the instrument to the extent of the amount paid; and
 - (b) The holder must give such party a certified copy of the bill and of any authenticated protest.
- (5) The drawee or a party making partial payment may require that mention of such payment be made on the instrument and that a receipt therefore be given to him.
- (6) If the balance is paid, the person who receives it and who is in possession of the instrument must deliver to the payor the receipted instrument and any authenticated protest.

Article 72

- (1) The holder may refuse to take payment in a place other than the place where the instrument was duly presented for payment in accordance with article 53.

(2) If in such case payment is not made in the place where the instrument was duly presented for payment in accordance with article 53, the instrument is considered as dishonoured by non-payment.

Article 74

(1) An instrument must be paid in the currency in which the amount of the instrument is expressed.

(2) The drawer or the maker may indicate on the instrument that it must be paid in a specified currency other than the currency in which the amount of the instrument is expressed. In that case:

(a) The instrument must be paid in the currency so specified;

(b) The amount payable is to be calculated according to the rate of exchange indicated on the instrument. Failing such an indication, the amount payable is to be calculated according to the rate of exchange for sight drafts on the date of maturity:

(i) Ruling at the place where the instrument must be presented for payment in accordance with article 53 (g), if the specified currency is that of that place (local currency); or

(ii) If the specified currency is not that of that place, according to the usages of the place where the instrument must be presented for payment in accordance with article 53 (g);

(c) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the instrument, according to that rate;

(ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling at the date of dishonour or on the date of actual payment;

(d) If such an instrument is dishonoured by non-payment, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the instrument, according to that rate;

(ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of maturity or on the date of actual payment.

(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-acceptance or non-payment.

(4) The rate of exchange ruling at a certain date is the rate of exchange ruling, at the option of the holder, at the place where the instrument must be presented for payment

in accordance with article 53 (g) or at the place of actual payment.

Article 74 bis

(1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party.

Article 78

(1) When a party is discharged wholly or partly of his liability on the instrument, any party who has a right of recourse against him is discharged to the same extent.

(2) Payment by the drawee of the whole or a part of the amount of a bill to the holder, or to any party who has paid the bill in accordance with article 67, discharges all parties of their liability to the same extent.

Article 79

(1) (Not considered by the Drafting Group)

(2) If a party has paid the instrument in accordance with articles 67 or 68 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year after the date on which he paid the instrument.

Article 80

(1) When an instrument is lost, whether by destruction, theft or otherwise, the person who lost the instrument has, subject to the provisions of paragraphs (2) and (3) of this article, the same right to payment which he would have had if he had been in possession of the instrument. The party from whom payment is claimed cannot set up as a defence against liability on the instrument the fact that the person claiming payment is not in possession thereof.

(2) (a) The person claiming payment of a lost instrument must state in writing to the party from whom he claims payment:

(i) The elements of the lost instrument pertaining to the requirements set forth in article 1 (2) or 1 (3); for this purpose the person claiming payment of the lost instrument may present to that party a copy of that instrument;

(ii) The facts showing that, if he had been in possession of the instrument, he would have had a right to payment from the party from whom payment is claimed;

(iii) The facts which prevent production of the instrument.

(b) The party from whom payment of a lost instrument is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost instrument.

(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms.

(d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost instrument, and any interest and expenses which may be claimed under article 67 or 68, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

Article 81

(1) A party who has paid a lost instrument and to whom the instrument is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

(2) Such notification must be given on the day the instrument is presented or on one of the two business days which follow and must state the name of the person presenting the instrument and the date and place of presentment.

(3) Failure to notify renders the party who has paid the lost instrument liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 67 or 68.

(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost instrument and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

Article 82

(1) A party who has paid a lost instrument in accordance with the provisions of article 80 and who is subsequently required to, and does, pay the instrument, or who, by reason of the loss of the instrument, then loses his right to recover from any party liable to him, has the right:

(a) If security was given, to realize the security; or

(b) If the amount was deposited with the court or other competent authority, to reclaim the amount so deposited.

(2) The person who has given security in accordance with the provisions of paragraph (2) (b) of article 80 entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the instrument is lost.

Article 83

A person claiming payment of a lost instrument duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 80, paragraph (2) (a).

Article 84

A person receiving payment of a lost instrument in accordance with article 80 must deliver to the party paying the written statement required under article 80, paragraph (2) (a), receipted by him and any protest and a receipted account.

Article 85

(a) A party who paid a lost instrument in accordance with article 80 has the same rights which he would have had if he had been in possession of the instrument.

(b) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 84.

LIST OF HEADINGS AND SUBHEADINGS AS SUGGESTED BY THE DRAFTING GROUP

CHAPTER ONE	Sphere of application and form (articles 1, 3)
CHAPTER TWO	Interpretation <ul style="list-style-type: none"> Section 1: General provisions (articles 4, 5, 6) Section 2: Interpretation of formal requirements (articles 7-10 <i>bis</i>) Section 3: Completion of an incomplete instrument (article 11)
CHAPTER THREE	Transfer (articles 12-22)
CHAPTER FOUR	Rights and liabilities <ul style="list-style-type: none"> Section 1: The rights of a holder and a protected holder (articles 23-26) Section 2: The liability of the parties <ul style="list-style-type: none"> A. General provisions (articles 27-30 <i>bis</i>) B. The drawer (article 34) C. The maker (article 34 <i>bis</i>) D. The drawee and the acceptor (articles 36-39) E. The endorser (articles 41-42) F. The guarantor (articles 43-45)

CHAPTER FIVE	Presentment, dishonour for non-acceptance or non-payment, and recourse
	Section 1: Presentment for acceptance and dishonour by non-acceptance (articles 46-51)
	Section 2: Presentment for payment and dishonour by non-payment (articles 53-56)
	Section 3: Recourse (articles 57-66)
	A. Protest (articles 57-61)
	B. Notice of dishonour (articles 62-66)

	Section 4: Amount payable (articles 66 bis-68)
CHAPTER SIX	Discharge
	Section 1: Discharge by payment (articles 70-74 bis)
	Section 2: Discharge of a prior party (article 78)
CHAPTER SEVEN	Limitation (Prescription) (article 79)
CHAPTER EIGHT	Lost instruments (articles 80-85)

- (f) *Note by the Secretariat: draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles (set out in A/CN.9/WG.IV/WP.24 and Add. 1) as revised by the Drafting Group (A/CN.9/WG.IV/WP.24/Add.2)**

MODIFICATIONS TO THE TEXT OF THE DRAFT CONVENTION ON BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES AS SET OUT IN A/CN.9/WG.IV/WP.24 AND ADD. 1

Article 1, paragraphs 2 (a) and 3 (a)

Replace square brackets by parentheses, and delete footnote appended to paragraph 2 (a).

Article 5, paragraph (7) (a)

Delete the words "circumstances giving rise to".

Article 5, paragraph (8)

Delete the square brackets.

Article 5, new paragraph (11)

Add new paragraph (11), as follows:

[(11) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution even if intended by it to be transferable only in its records and between it and persons designated by it or between such persons.]

Article (X) appended to article 5 (10)

Place article between square brackets.

Article 9, paragraph (6 bis)

Place paragraph (6 bis) after paragraph (5) and renumber paragraph (6 bis) as (5 bis).

"New article" appearing after article 13

Replace the opening words of paragraph (2) "An endorsement may be made", by the words:

"(2) An endorsement may be:"

Article 17, paragraphs (1) and (3)

Add paragraph (1) to read as follows:

"(1) An endorsement must be unconditional".

Delete paragraph (3)

Article 22, paragraph (1)

Add following paragraph as paragraph (1):

"(1) If an endorsement is forged, any party has against the forger, and against the person to whom the instrument was directly transferred by the forger, the right to recover compensation for any damages that he may have suffered because of the forgery."

Article 22, new paragraph (1 bis)

Add following paragraph as paragraph (1 bis):

"The liability of an acceptor, drawee, or maker who pays, or of an endorsee for collection who collects, an instrument on which there is a forged endorsement is not regulated by this Convention."

Article 22, paragraph (2)

After the words "without authority", insert the words "or exceeding his authority".

Article 25, paragraph (1) (a)

Delete the reference to articles "57, 60".

Article 27, paragraph (2)

After the words "A person who signs" insert the words "an instrument".

Article 30, paragraph (2)

The Working Group modified the text as follows:

"(2) The signature of an agent placed by him on an instrument with the authority of his principal and show-

* 13 August 1981.

ing on the instrument that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the instrument by an agent with his authority, impose liability on the principal and not on the agent."

Article 30 bis

Delete at end of article the words "outside the bill".

Article 34, paragraph (1)

After the words "holder or to any", add the word "subsequent".

Article 34 bis

Replace the existing paragraph (1) with the following text:

"(1) The maker engages he will pay to the holder, or to any party who pays the note in accordance with article 67, the amount of the note in accordance with the terms of that note, and any interest and expenses which may be recovered under article 67 or 68."

Article 36, paragraph (2)

Replace the existing paragraph (2) with the following text:

"(2) The acceptor engages that he will pay to the holder, or to any party who pays the bill in accordance with article 67, the amount of the bill in accordance with the terms of his acceptance, and any interest and expenses which may be recovered under article 67 or 68."

Article 41, paragraph (1)

After the words "holder or to any", insert the word "subsequent" and replace the word "bill" by the word "instrument".

Article 44, paragraph (2)

Replace the words "when due" appearing at the end of this paragraph with the words "at maturity".

Article 53 (e)

Replace the words "on one of the two business days which follow" by the words "on the business day which follows".

Article 53 (h)

Delete the words "of which the drawee or acceptor or the maker is a member".

Article 54 (2) (e)

Delete "(e)" and the words following.

Article 56 (1) (c)

Replace the words "the instrument unpaid" by the words "the instrument is unpaid".

Article 58 (3 bis)

Delete this paragraph.

Article 58 (4)

Delete the words "or (3 bis)".

Article 61 (2) (b)

After the words "cause of delay" insert the words "under paragraph (1)".

Article 65 (2)

Invert subparagraphs (a) and (b), and re-letter existing subparagraph (a) as (b), and (b) as (a).

Article 66

Delete the word "directly".

Article 67 (1) (b)

Replace existing subparagraph (b) by the following text:

"(b) After maturity:

"(i) The amount of the instrument with interest, if interest has been stipulated for, to the date of maturity;

"(ii) If interest has been stipulated to be paid after maturity, interest at the rate stipulated, or in the absence of such stipulation, interest at the rate specified in paragraph (2), calculated from the date of presentment on the sum specified in paragraph (1) (b) (i);

"(iii) Any expenses of protest and of the notices given by him;"

Article 67 (2)

Replace the existing paragraph by the following text:

"(2) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the instrument is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the instrument is payable. In the absence of any such rates, the rate of interest shall be [] per cent per annum."

Article 67 (3)

Delete the words "to be calculated on the basis of the number of days and in accordance with the custom of that place".

Article 68

Delete the number "(1)" appearing at beginning of text.

Article 70, paragraph (1)

Replace the words "discharged of his liability" by the words "discharged of liability" and insert commas after the words "the holder" and "to himself".

Article 70, paragraph (3)

Replace the words "discharged of his liability" by the words "discharged of liability".

Article 70 (4) (a)

Add following text:

"(4) (a) A person receiving payment of an instrument must, unless agreed otherwise, deliver:

- "(i) To the drawee making such payment, the instrument;
- "(ii) To any other person making such payment, the instrument, a receipted account, and any protest."

Article 70 (4) (c)

Add following text:

"(c) If payment is made but the person paying, other than the drawee, fails to obtain the instrument, such person is discharged but the discharge cannot be set up as a defence against a protected holder."

Article 72, paragraphs (1) and (2)

Delete in both paragraphs the word "duly".

Article 74 (2) (b)

Replace the opening words of this subparagraph by the following text:

"(b) The amount payable is to be calculated according to the rate of exchange indicated on the instrument. Failing such indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of maturity."

Article 74 bis

Add the following text as new paragraph (2):

"(2) (a) If, by virtue of the application of paragraph (1) of this article, an instrument drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment.

"(b) (i) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated, at the option of the holder, at the rate of exchange ruling at the date of dishonour, or at the date of actual payment;

"(ii) If such an instrument is dishonoured by non-payment, the amount is to be calculated, at the option of the holder, according to the rate of exchange ruling at the date of presentment or at the date of actual payment.

"(iii) Paragraphs (3) and (4) of article 74 are applicable where appropriate."

Article 79, paragraph (1)

Add following text as paragraph (1):

"(1) A right of action arising on an instrument may no longer be exercised after four years have elapsed:

"(a) Against the maker, or his guarantor, of a note payable on demand, from the date of the note;

"(b) Against the acceptor or the maker or their guarantor of an instrument payable at a definite time, from the date of maturity;

"(c) Against the acceptor of a bill payable on demand, from the date on which it was accepted.

"(d) Against the drawer or an endorser or their guarantor, from the date of protest for dishonour by non-acceptance or non-payment or, where protest is dispensed with, from the date of dishonour."

Article 79, paragraph (2)

Replace the words "articles 67 or 68" by the words "article 67 or 68" and replace the word "after" by the word "from".

Article 82, paragraph (1) (b)

After the words "competent authority" insert the words "or institution".

Article 85

Renumber paragraphs (a) and (b) to read (1) and (2) and in paragraph (1) replace the words "A party who paid" by the words "A party who has paid".

List of headings and subheadings

Title of Chapter One to read as follows: "SPHERE OF APPLICATION AND FORM OF THE INSTRUMENT".

Chapter Four, Section Two, add the following list of articles covered: "(articles 27-45)".

In Chapter Five, section 3, A, Protest, the articles covered should be listed as follows: "(articles 57-59, 61, 60)".

Chapters Seven and Eight to read as follows: "Chapter Seven: Lost instruments (articles 80-85). Chapter Eight: Limitation (Prescription) (article 79)."

(g) *Note by the Secretariat: draft Convention on International Cheques: text of draft articles 1-66 bis as revised by the Drafting Group (A/CN.9/WG.IV/WP.25)**

Article 1

- (1) This Convention applies to international cheques.
- (2) An international cheque is a written instrument which:
 - (a) Contains, in the text thereof, the words "international cheque (Convention of ...)";
 - (b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order or to bearer;
 - (c) Is drawn on a banker;
 - (e) Is dated;
 - (f) Shows that at least two of the following places are situated in different States:
 - (i) The place where the cheque is drawn;
 - (ii) The place indicated next to the name or the signature of the drawer;
 - (iii) The place indicated next to the name of the drawee;
 - (iv) The place indicated next to the name of the payee;
 - (v) The place of payment;
 - (g) Is signed by the drawer.
- (3) Proof that the statements referred to in paragraph (2) (f) of this article are incorrect does not affect the application of this Convention.

Article 3

This Convention applies without regard to whether the places indicated on an international cheque pursuant to paragraph (2) (f) of article 1 are situated in Contracting States.

Article 4

In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application.

* 13 August 1981. See the asterisked footnote to "(d) Note by the Secretariat . . . (A/CN.9/WG.IV/WP.24)" on page 81.

Article 5

In this Convention:

- (1) "Cheque" means an international cheque governed by this Convention;
- (2) "Drawee" means the banker on whom a cheque is drawn;
- (2 bis) "Banker" includes any person or institution assimilated to a banker;
- (3) "Payee" means the person in whose favour the drawer directs payment to be made;
- (5) "Holder" means a person in possession of a cheque in accordance with article 13 bis.
- (6) "Protected holder" means the holder of a cheque which, when he became a holder, was complete and regular on its face, provided that:
 - (a) He was, at that time, without knowledge of a claim to or defence upon the cheque referred to in article 24 or of the fact that it was dishonoured by non-payment;
 - (b) The time-limit provided by article 53 for presentment of that cheque for payment had not then expired.
- (7) "Party" means any person who has signed a cheque as drawer, endorser or guarantor.
- (8) "Signature" includes a signature by stamp, symbol, facsimile, perforation or other mechanical means* and "forged signature" includes a signature by the wrongful or unauthorized use of such means.
- [(9) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution, even if intended by it to be transferable only in its records and between it and persons designated by it or between such persons.]

*

[Article (X)]

A Contracting State whose legislation requires that a signature on a cheque be handwritten may, at the time of signature, ratification or accession, make a declaration to the effect that a signature placed on a cheque in its territory must be handwritten. (Footnote in original.)

Article 6

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

Article 7

The sum payable by a cheque is deemed to be a definite sum although the cheque states that it is to be paid:

(b) According to a rate of exchange indicated on the cheque or to be determined as directed by the cheque; or

(c) In a currency other than the currency in which the amount of the cheque is expressed.

Article 7 bis

Any stipulation on a cheque that it is to be paid with interest is deemed not to have been written.

Article 8

(1) If there is a discrepancy between the amount of the cheque expressed in words and the amount expressed in figures, the amount of the cheque is the amount expressed in words.

(2) If the amount of the cheque is expressed in a currency having the same description as that of at least one other State than the State where payment is to be made as indicated on the cheque and the specified currency is not identified as the currency of any particular State, the currency is to be considered as the currency of the State where payment is to be made.

Article 9

(1) A cheque is always payable on demand. It is so payable:

(a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or

(b) If no time of payment is expressed.

(2) A stipulation on a cheque that it is payable at a definite time is deemed not to have been written.

Article 10

(1) A cheque may:

(a) Be drawn by the drawer on himself or be drawn payable to his order;

(b) Be drawn by two or more drawers;

(c) Be payable to two or more payees.

(2) If a cheque is payable to two or more payees in the alternative, it is payable to any one of them and any

one of them in possession of the cheque may exercise the rights of a holder. In any other case the cheque is payable to all of them and the rights of a holder can only be exercised by all of them.

Article 11

(1) An incomplete cheque which satisfies the requirements set out in subparagraphs (a) and (g) of paragraph (2) but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) of article 1 may be completed and the cheque so completed is effective as a cheque.

(2) When such a cheque is completed otherwise than in accordance with an agreement entered into:

(a) A party who signed the cheque before the completion may invoke the non-observance of the agreement as a defence against a holder, provided the holder had knowledge of the non-observance of the agreement when he became a holder.

(b) A party who signed the cheque after the completion is liable according to the terms of the cheque so completed.

Article 13

A cheque is transferred:

(a) By endorsement and delivery of the cheque by the endorser to the endorsee; or

(b) By mere delivery of the cheque if it is drawn payable to bearer or if the last endorsement is in blank.

New article

(1) An endorsement must be written on the cheque or on a slip affixed thereto (*allonge*). It must be signed.

(2) An endorsement may be:

(a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the cheque is payable to any person in possession thereof;

(b) Special, by a signature accompanied by an indication of the person to whom the cheque is payable.

Article 13 bis

(1) A person is a holder if he is:

(a) In possession of a cheque drawn payable to bearer; or

(b) The payee in possession of the cheque; or

(c) In possession of a cheque which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

(2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.

(3) A person is not prevented from being a holder by the fact that the cheque was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon the cheque.

Article 15

The holder of a cheque on which the last endorsement is in blank may:

- (a) Further endorse the cheque either in blank or to a specified person; or
- (b) Convert the blank endorsement into a special endorsement by indicating therein that the cheque is payable to himself or to some other specified person; or
- (c) Transfer the cheque in accordance with paragraph (b) of article 13.

Article 16

When the drawer of a cheque payable to a payee or to his order has inserted in the cheque, or an endorser in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the transferee does not become a holder except for purposes of collection.

Article 17

- (1) An endorsement must be unconditional.
- (2) A conditional endorsement transfers the cheque whether or not the condition is fulfilled.

Article 18

An endorsement in respect of a part of the sum due under the cheque is ineffective as an endorsement.

Article 19

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the cheque.

Article 20

(1) When an endorsement contains the words "for collection", "for deposit", "value in collection", "by procuration", "pay any bank", or words of similar import, authorizing the endorsee to collect the cheque (endorsement for collection) the endorsee:

(a) May only endorse the cheque for purposes of collection;

(b) May exercise all the rights arising out of the cheque;

(c) Is subject to all claims and defences which may be set up against the endorser.

(2) The endorser for collection is not liable upon the cheque to any subsequent holder.

Article 21

(1) The holder of a cheque may transfer it to a prior party in accordance with article 13; nevertheless, in the case where the transferee was a prior holder of the cheque, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

(2) The endorsement to the drawee operates only as an acknowledgement that the endorser has received from the drawee the amount of the cheque except in the case where the drawee has several establishments and the endorsement is made in favour of an establishment other than that on which the cheque has been drawn.

Article 21 bis

A cheque may be transferred in accordance with article 13 after the expiration of the period of time for presentment.

Article 22

(1) If an endorsement is forged, any party has against the forger, and against the person to whom the cheque was directly transferred by the forger, the right to recover compensation for any damage that he may have suffered because of the forgery.

(1 bis) Except to the extent provided in article C, the liability of a drawee who pays, or of an endorsee for collection who collects, a cheque on which there is a forged endorsement is not regulated by this Convention.

(3) For the purpose of this article, an endorsement placed on a cheque by a person in a representative capacity without authority or exceeding his authority has the same effects as a forged endorsement.

Article 23

(1) The holder of a cheque has all the rights conferred on him by this Convention against the parties to the cheque.

(2) The holder is entitled to transfer the cheque in accordance with article 13.

Article 24

(1) A party may set up against a holder who is not a protected holder:

- (a) Any defence available under this Convention;
- (b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

(c) Any defence to contractual liability based on a transaction between himself and the holder;

(d) Any defence based on incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque, provided that such absence of knowledge was not due to his negligence.

(2) The rights to a cheque of a holder who is not a protected holder are subject to any valid claim to the cheque on the part of any person.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the cheque unless:

(a) Such third person asserted a valid claim to the cheque; or

(b) Such holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft.

Article 25

(1) A party may not set up against a protected holder any defence except:

(a) Defences under articles 27 (1), 28, 29 (1), 30 (2, 3), 50, 55 and 79 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that party;

(c) Defences based on the incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque provided that such absence of knowledge was not due to his negligence.

(2) The rights to a cheque of a protected holder are not subject to any claim to the cheque on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that person.

Article 25 bis

(1) The transfer of a cheque by a protected holder vests in any subsequent holder the rights to and upon the cheque which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to or a defence upon the cheque.

(2) If a party pays the cheque in accordance with article 67 and the cheque is transferred to him, such transfer does not vest in that party the rights to and upon the cheque which any previous protected holder had.

Article 26

Every holder is presumed to be a protected holder, unless the contrary is proved.

Article 27

(1) Subject to the provisions of articles 28 and 30, a person is not liable on a cheque unless he signs it.

(2) A person who signs a cheque in a name which is not his own is liable as if he had signed it in his own name.

Article 28

A forged signature on a cheque does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed the cheque himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own.

Article 29

(1) If a cheque has been materially altered:

(a) Parties who have signed the cheque subsequent to the material alteration are liable thereon according to the terms of the altered text;

(b) Parties who have signed the cheque before the material alteration are liable thereon according to the terms of the original text. Nevertheless, a party who has himself made, authorized, or assented to, the material alteration is liable on the cheque according to the terms of the altered text.

(2) Failing proof to the contrary, a signature is deemed to have been placed on the cheque after the material alteration.

(3) Any alteration is material which modifies the written undertaking on the cheque of any party in any respect.

Article 30

(1) A cheque may be signed by an agent.

(2) The signature of an agent placed by him on a cheque with the authority of his principal and showing on the cheque that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the cheque by an agent with his authority, imposes liability on the principal and not on the agent.

(3) A signature placed on a cheque by a person as agent but without authority to sign or exceeding his authority

or by an agent with authority to sign but not showing on the cheque that he is signing in a representative capacity for a named person, or showing on the cheque that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.

(4) The question whether a signature was placed on the cheque in a representative capacity may be determined only by reference to what appears on the cheque.

(5) A person who is liable pursuant to paragraph 3 and who pays the cheque has the same rights as the person for whom he purported to act would have had if that person had paid the cheque.

Article 30 bis

The order to pay contained in a cheque does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee.

Article 34

(1) The drawer engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the cheque in accordance with article 67, the amount of the cheque, and any interest and expenses which may be recovered under article 67 or 68.

(2) The drawer may not exclude or limit his own liability by a stipulation on the cheque. Any such stipulation is without effect.

Article X

(1) Any statement written on a cheque indicating certification, confirmation, acceptance, *visa* or any other equivalent expression has only the effect to ascertain the existence of funds and prevents the withdrawal of such funds by the drawer, or the use of such funds by the drawee for purposes other than payment of the cheque bearing such a statement, before the expiration of the time-limit for presentment.

(2) However, a Contracting State may provide that a drawee may accept a cheque and determine the legal effects thereof. Such acceptance must be effected by the signature of the drawee accompanied by the word "accepted".

Article 41

(1) The endorser engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the cheque in accordance with article 67, the amount of the cheque, and any interest and expenses which may be recovered under article 67 or 68.

(2) The endorser may exclude or limit his own liability by an express stipulation on the cheque. Such stipulation has effect only with respect to that endorser.

Article 42

(1) Any person who transfers a cheque by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer:

- (a) A signature on the cheque was forged or unauthorized; or
- (b) The cheque was materially altered; or
- (c) A party has a valid claim or defence against him; or
- (d) The cheque was dishonoured by non-payment.

(2) The damages recoverable under paragraph (1) may not exceed the amount referred to in article 67 or 68.

(3) Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the cheque without knowledge of such defect.

Article 43

(1) Payment of a cheque may be guaranteed, as to the whole or part of its amount, for the account of a party by any person who may or may not have become a party.

(2) A guarantee must be written on the cheque or on a slip affixed thereto (*allonge*).

(3) A guarantee is expressed by the words: "guaranteed", "*aval*", "good as *aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires:

(a) A signature alone on the front of the cheque, other than that of the drawer, is a guarantee;

(b) A signature alone on the back of the cheque is an endorsement. A special endorsement of a cheque made payable to bearer does not convert the cheque into an order instrument.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the drawer.

Article 44

A guarantor is liable on the cheque to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the cheque.

Article 45

The guarantor who pays the cheque has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

Article 53

A cheque is duly presented for payment if it is presented in accordance with the following rules:

- (a) The holder must present the cheque to the drawee on a business day at a reasonable hour;
- (f) A cheque must be presented for payment within 120 days of its stated date;
- (g) A cheque must be presented for payment:
 - (i) At the place of payment specified on the cheque; or
 - (ii) If no place of payment is specified, at the address of the drawee indicated on the cheque; or
 - (iii) If no place of payment is specified and the address of the drawee is not indicated, at the principal place of business of the drawee.
- (h) A cheque may be presented for payment at a clearing-house.

Article 54

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

- (a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:
 - (i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;
 - (ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;
 - (iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.
- (c) If the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment.

Article 55

If a cheque is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon. However, if a cheque is not duly presented because of delay in making presentment, the drawer is not discharged of liability except to the extent of the loss suffered because of the delay.

Article 56

(1) A cheque is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment, or when the holder cannot obtain the payment to which he is entitled under this Convention, or as regards the drawer only, if presentment of the cheque, otherwise duly made, is delayed and payment is refused;

(c) If presentment for payment is dispensed with pursuant to article 54 (2) and the cheque is unpaid.

(2) If a cheque is dishonoured by non-payment, the holder may, subject to the provisions of article 57, exercise a right of recourse against the drawer, the endorsers and their guarantors.

Article 57

If a cheque has been dishonoured by non-payment, the holder may exercise a right of recourse only after the cheque has been duly protested for dishonour in accordance with the provisions of articles 58 to 61.

Article 58

(1) A protest is a statement of dishonour drawn up at the place where the cheque has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

- (a) The person at whose request the cheque is protested;
- (b) The place of protest; and
- (c) The demand made and the answer given, if any, or the fact that the drawee could not be found.

(2) A protest may be made:

- (a) On the cheque itself or on a slip affixed thereto (*allonge*); or
- (b) As a separate document, in which case it must clearly identify the cheque that has been dishonoured.

(3) Unless the cheque stipulates that protest must be made, a protest may be replaced by a declaration written on the cheque and signed and dated by the drawee; the declaration must be to the effect that payment is refused.

(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purposes of this Convention.

Article 59

Protest for dishonour of a cheque by non-payment must be made on the day on which the cheque is dishonoured or on one of the two business days which follow.

Article 60

(1) If a cheque which must be protested for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.

(2) Delay in protesting a cheque for non-payment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered by the delay.

Article 61

(1) Delay in protesting a cheque for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

- (i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;
- (iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;

(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person;

(e) If presentment for payment is dispensed with in accordance with article 54 (2).

Article 62

(1) The holder, upon dishonour of a cheque by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.

(3) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the cheque.

(4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the cheque against the party notified.

Article 63

(1) Notice of dishonour may be given in any form whatever and in any terms which identify the cheque and state that it has been dishonoured. The return of the dishonoured cheque is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.

(2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.

(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

Article 64

Notice of dishonour must be given within the two business days which follow:

(a) The day of protest, or, if protest is dispensed with, the day of dishonour; or

(b) The receipt of notice given by another party.

Article 65

(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(2) Notice of dishonour is dispensed with:

(a) If after the exercise of reasonable diligence notice cannot be given;

(b) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:

- (i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;
- (iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.

(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person.

Article 66

Failure to give notice of dishonour renders a person who is required to give such notice under article 62 to a party who is entitled to receive such notice liable for any damages which that party may suffer from such failure, provided that such damages do not exceed the amount referred to in article 67 or 68.

Article 66 bis

The holder may exercise his rights on the cheque against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

- (h) *Note by the Secretariat: draft Convention on International Cheques: text of draft articles 67-85, A-F and α and β as revised by the Drafting Group: corrections made by the Drafting Group to draft articles 1-66 (A/CN.9/WG.IV/WP.25/Add.1)*.*

**CORRECTIONS MADE BY THE DRAFTING GROUP TO
DRAFT ARTICLES 1-66 (ISSUED AS A/CN.9/WG.IV/WP.25)**

Article 22

In paragraph (1 *bis*) replace the words "provided in article C" by "provided in articles C and F".

**TEXT OF DRAFT ARTICLES 67-85, A-F AND α AND β AS
REVISED BY THE DRAFTING GROUP**

Article 67

(1) The holder may recover from any party liable the amount of the cheque.

(2) When payment is made after the cheque has been dishonoured, the holder may recover from any party liable the amount of the cheque with interest at the rate specified in paragraph (4) calculated from the date of presentment to the date of payment and any expenses of protest and of the notices given by him.

(4) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the cheque is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the cheque is payable. In the absence of any such rates, the rate of interest shall be [] per cent per annum.

Article 68

(1) A party who takes up and pays a cheque in accordance with article 67 may recover from the parties liable to him:

- (a) The entire sum which he was obliged to pay in accordance with article 67 and has paid;
- (b) Interest on that sum at the rate specified in article 67, paragraph (4) from the date on which he made payment;
- (c) Any expenses of the notices given by him.

Article 70

(1) A party is discharged of liability on the cheque when he pays the holder, or a party subsequent to himself who has paid the cheque and is in possession thereof, the amount due pursuant to articles 67 and 68.

(3) A party is not discharged of liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid

claim to the cheque or that the holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(4) (a) A person receiving payment of a cheque must, unless agreed otherwise, deliver:

- (i) To the drawee making such payment, the cheque;
- (ii) To any other person making such payment, the cheque, a receipted account and any protest.

(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the cheque to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 56.

(c) If payment is made but the person paying, other than the drawee, fails to obtain the cheque, such person is discharged but the discharge cannot be set up as a defence against a protected holder.

Article 71

- (1) The holder is not obliged to take partial payment.
- (2) If the holder who is offered partial payment does not take it, the cheque is dishonoured by non-payment.
- (3) If the holder takes partial payment from the drawee the cheque is to be considered as dishonoured by non-payment as to the amount unpaid.
- (4) If the holder takes partial payment from a party to the cheque

(a) The party making payment is discharged of his liability on the cheque to the extent of the amount paid; and

(b) The holder must give such party a certified copy of the cheque, and of any authenticated protest.

(5) The drawee or a party making partial payment may require that mention of such payment be made on the cheque and that a receipt therefore be given to him.

(6) If the balance is paid, the person who receives it and who is in possession of the cheque must deliver to the payor the receipted cheque and any authenticated protest.

Article 72

(1) The holder may refuse to take payment in a place other than the place where the cheque was presented for payment in accordance with article 53.

(2) If in such case payment is not made in the place where the cheque was presented for payment in accordance with article 53, the cheque is considered as dishonoured by non-payment.

Article 74

(1) A cheque must be paid in the currency in which the amount of the cheque is expressed.

(2) The drawer may indicate on the cheque that it must be paid in a specified currency other than the currency in which the amount of the cheque is expressed. In that case:

(a) The cheque must be paid in the currency so specified;

(b) The amount payable is to be calculated according to the rate of exchange indicated on the cheque. Failing such an indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment;

(c) If such a cheque is dishonoured by non-payment, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the cheque, according to that rate;

(ii) If no rate of exchange is indicated on the cheque, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment at the place where the cheque must be presented for payment in accordance with article 53 (g) or at the place of actual payment.

(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-payment.

Article 74 bis

(1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party.

(2) (a) If, by virtue of the application of paragraph (1) of this article, a cheque drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment ruling at the place where the cheque must be presented for payment in accordance with article 53 (g).

(b) If such a cheque is dishonoured by non-payment:

(i) The amount is to be calculated, at the option of the holder, according to the rate of exchange ruling at the date of presentment or at the date of actual payment;

(ii) Paragraph (3) of article 74 is applicable where appropriate.

Article 74 ter

If the drawer countermands the order to the drawee to pay a cheque drawn on him, the drawee is under a duty not to pay.

Article 79

(1) A right of action arising on a cheque can no longer be exercised after four years have elapsed:

(a) Against the drawer or his guarantor, from the date of the cheque;

(b) Against an endorser or his guarantor, from the date of protest for dishonour or, where protest is dispensed with, the date of dishonour.

(2) If a party has paid the cheque in accordance with article 67 or 68 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year from the date on which he paid the cheque.

Article 80

(1) When a cheque is lost, whether by destruction, theft or otherwise, the person who lost the cheque has, subject to the provisions of paragraphs (2) and (3) of this article, the same right to payment which he would have had if he had been in possession of the cheque. The party from whom payment is claimed cannot set up as a defence against liability on the cheque the fact that the person claiming payment is not in possession thereof.

(2) (a) The person claiming payment of a lost cheque must state in writing to the party from whom he claims payment:

(i) The elements of the lost cheque pertaining to the requirements set forth in article 1 (2); for this purpose the person claiming payment of the lost cheque may present to that party a copy of that cheque;

(ii) The facts showing that, if he had been in possession of the cheque, he would have had a right to payment from the party from whom payment is claimed;

(iii) The facts which prevent production of the cheque.

(b) The party from whom payment of a lost cheque is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost cheque;

(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms;

(d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost cheque, and any interest and expenses which may be claimed under article 67 or 68, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

New (3) The person claiming payment of a lost cheque in accordance with the provisions of this article need not give security to the drawer who has inserted in the cheque, or to an endorser who has inserted in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import.

Article 81

(1) A party who has paid a lost cheque and to whom the cheque is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

(2) Such notification must be given on the day the cheque is presented for payment or on one of the two business days which follow and must state the name of the person presenting the cheque and the date and place of presentment.

(3) Failure to notify renders the party who has paid the lost cheque liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 67 or 68.

(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost cheque and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

Article 82

(1) A party who has paid a lost cheque in accordance with the provisions of article 80 and who is subsequently required to, and does, pay the cheque, or who, by reason of the loss of the cheque, then loses his right to recover from any party liable to him, has the right:

(a) If security was given, to realize the security; or

(b) If the amount was deposited with the court or other competent authority or institution, to reclaim the amount so deposited.

(2) The person who has given security in accordance with the provisions of paragraph (2) (b) of article 80 is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the cheque is lost.

Article 83

A person claiming payment of a lost cheque duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 80, paragraph (2) (a).

Article 84

A person receiving payment of a lost cheque in accordance with article 80 must deliver to the party paying the written statement required under article 80, paragraph (2) (a), receipted by him and any protest and a receipted account.

Article 85

(1) A party who has paid a lost cheque in accordance with article 80 has the same rights which he would have had if he had been in possession of the cheque.

(2) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 84.

Article A

(1) A cheque is crossed if it bears across its face two parallel transverse lines.

(2) A crossing is general if it consists of the two lines only or if between the two lines the word "banker" or an equivalent term or the words "and Company" or any abbreviation thereof is inserted; it is special if the name of a banker is so inserted.

(3) A cheque may be crossed generally or specially by the drawer or the holder.

(4) The holder may convert a general crossing into a special crossing.

(5) A special crossing may not be converted into a general crossing.

(6) The banker to whom a cheque is crossed specially may again cross it specially to another banker for collection.

Article B

If a cheque shows on its face the obliteration either of a crossing or of the name of the banker to whom it is crossed, the obliteration is considered as not having taken place.

Article C

(1) (a) A cheque which is crossed generally is payable only to a banker or to a customer of the drawee;

(b) A cheque which is crossed specially is payable only to the banker to whom it is crossed or, if such banker is the drawee, to his customer;

(c) A banker may not take a crossed cheque except from his customer or from another banker and may not collect such a cheque except for such a person.

(2) The drawee who pays, or the banker who takes or collects, a crossed cheque in violation of the provisions of paragraph (1) of this article incurs liability for any damages which a person may have suffered as a result of such violation, provided that such damages do not exceed the amount of the cheque.

Article E

If the crossing on a cheque contains the words "not negotiable" the transferee becomes a holder but cannot become a protected holder. However, such transferee may acquire the rights of a protected holder under article 25 *bis*.

Article F

(1) (a) The drawer or the holder of a cheque may prohibit its payment in cash by writing transversally across the face of the cheque the words "payable in account" or words of similar import;

(b) In such case the cheque may only be paid by the drawee by means of a book-entry.

(2) The drawee who pays such a cheque otherwise than by means of a book-entry incurs liability for any damages which a person may have suffered as a result thereof, provided that such damages do not exceed the amount of the cheque.

(3) If a cheque shows on its face the obliteration of the words "payable in account", the obliteration is considered as not having taken place.

Article a

If a cheque is drawn against insufficient funds, it is nevertheless valid as a cheque.

Article β

(1) A cheque which bears a date other than the date on which it was drawn is nevertheless valid as a cheque.

(2) If a cheque is presented before its stated date, refusal by the drawee to pay does not constitute dishonour by non-payment under article 56.

LIST OF HEADINGS AND SUBHEADINGS (CHEQUES)

CHAPTER ONE	Sphere of application and form of the cheque (articles 1, 3)
CHAPTER TWO	Interpretation Section 1: General provisions (α, β (1); 4, 5, 6) Section 2: Interpretation of formal requirements (articles 7-10)
CHAPTER THREE	Transfer (articles 13-22)
CHAPTER FOUR	Rights and Liabilities Section 1: The rights of a holder and a protected holder (articles 23-26) Section 2: A. General provisions (articles 26-30 <i>bis</i> ; X) B. The drawer (article 34) C. The endorser (articles 41, 42) D. The guarantor (articles 43-45)
CHAPTER FIVE	Presentment, Dishonour for non-payment and Recourse Section 1: Presentment for payment and dishonour by non-payment (articles 53-56; β (2)) Section 2: Recourse A. Protest (articles 57-59, 61, 60) B. Notice of dishonour (articles 62-66) Section 3: Amount payable (articles 66 <i>bis</i> -68)
CHAPTER SIX	Discharge Section 1: Discharge by payment (articles 70-74 <i>ter</i>) Section 2: Discharge of a prior party (article 78)
CHAPTER SEVEN	Crossed Cheques and Cheques Payable in Account Section 1: Crossed cheques (articles A-E) Section 2: Cheques payable in account (article F)
CHAPTER EIGHT	Lost cheques (articles 80-85)
CHAPTER NINE	Limitation (Prescription) (article 79)

3. NOTE BY THE SECRETARIAT: DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES: TEXT OF DRAFT ARTICLES AS ADOPTED BY THE WORKING GROUP ON INTERNATIONAL NEGOTIABLE INSTRUMENTS (A/CN.9/211)*

**Draft Convention on International Bills of Exchange
and International Promissory Notes**

**CHAPTER ONE. SPHERE OF APPLICATION AND FORM
OF THE INSTRUMENT**

Article 1

(1) This Convention applies to international bills of exchange and to international promissory notes.

(2) An international bill of exchange is a written instrument which:

(a) Contains, in the text thereof, the words "international bill of exchange (Convention of . . .)";

(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the bill is drawn;

(ii) The place indicated next to the signature of the drawer;

(iii) The place indicated next to the name of the drawee;

(iv) The place indicated next to the name of the payee;

(v) The place of payment;

(f) Is signed by the drawer.

(3) An international promissory note is a written instrument which:

(a) Contains, in the text thereof, the words "international promissory note (Convention of . . .)";

(b) Contains an unconditional promise whereby the maker undertakes to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the note is made;

(ii) The place indicated next to the signature of the maker;

(iii) The place indicated next to the name of the payee;

(iv) The place of payment;

(f) Is signed by the maker.

(4) Proof that the statements referred to in paragraph (2) (e) or (3) (e) of this article are incorrect does not affect the application of this Convention.

Article 2

This Convention applies without regard to whether the places indicated on an international bill of exchange or on an international promissory note pursuant to paragraph (2) (e) or (3) (e) of article 1 are situated in Contracting States.

CHAPTER TWO. INTERPRETATION

Section 1. General provisions

Article 3

In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application.

Article 4

In this Convention:

(1) "Bill" means an international bill of exchange governed by this Convention;

(2) "Note" means an international promissory note governed by this Convention;

(3) "Instrument" means a bill or a note;

(4) "Drawee" means the person on whom a bill is drawn but who has not accepted it;

(5) "Payee" means the person in whose favour the drawer directs payment to be made or to whom the maker promises to pay;

(6) "Holder" means a person in possession of an instrument in accordance with article 14;

(7) "Protected holder" means the holder of an instrument which, when he became a holder, was complete and regular on its face, provided that:

(a) He was, at that time, without knowledge of a claim to or defence upon the instrument referred to in article 25 or of the fact that it was dishonoured by non-acceptance or non-payment;

* 18 February 1982.

(b) The time-limit provided by article 51 for presentment of that instrument for payment had not then expired;

(8) "Party" means any person who has signed an instrument as drawer, maker, acceptor, endorser or guarantor;

(9) "Maturity" means the date of payment referred to in article 8;

(10) "Signature" includes a signature by stamp, symbol, facsimile, perforation or other mechanical means* and "forged signature" includes a signature by the wrongful or unauthorized use of such means;

[(11) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution even if intended by it to be transferable only in its records and between it and persons designated by it or between such persons.]

Article 5

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

Section 2. Interpretation of formal requirements

Article 6

The sum payable by an instrument is deemed to be a definite sum although the instrument states that it is to be paid:

- (a) With interest;
- (b) By instalments at successive dates;
- (c) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due;
- (d) According to a rate of exchange indicated on the instrument or to be determined as directed by the instrument; or
- (e) In a currency other than the currency in which the amount of the instrument is expressed.

Article 7

(1) If there is a discrepancy between the amount of the instrument expressed in words and the amount expressed in figures, the amount of the instrument is the amount expressed in words.

(2) If the amount of the instrument is expressed in a currency having the same description as that of at least one

other State than the State where payment is to be made as indicated on the instrument and the specified currency is not identified as the currency of any particular State, the currency is to be considered as the currency of the State where payment is to be made.

(3) If any instrument states that it is to be paid with interest, without specifying the date from which interest is to run, interest runs from the date of the instrument.

(4) A stipulation stating that the sum is to be paid with interest is deemed not to have been written on the instrument unless it indicates the rate at which interest is to be paid.

Article 8

(1) An instrument is deemed to be payable on demand:

- (a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or
- (b) If no time for payment is expressed.

(2) An instrument payable at a definite time which is accepted or endorsed or guaranteed after maturity is an instrument payable on demand as regards the acceptor, the endorser or the guarantor.

(3) An instrument is deemed to be payable at a definite time if it states that it is payable:

- (a) On a stated date or at a fixed period after a stated date or at a fixed period after the date of the instrument; or
- (b) At a fixed period after sight; or
- (c) By instalments at successive dates; or
- (d) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due.

(4) The time of payment of an instrument payable at a fixed period after date is determined by reference to the date of the instrument.

(5) The maturity of a bill payable at a fixed period after sight is determined by the date of the acceptance.

(6) The maturity of an instrument payable on demand is the date on which the instrument is presented for payment.

(7) The maturity of a note payable at a fixed period after sight is determined by the date of the visa signed by the maker on the note or, if signature is refused, from the date of presentment.

(8) Where an instrument is drawn, or made, payable at one or more months after a stated date or after the date of the instrument or after sight, the instrument matures on the corresponding date of the month when payment must be made. If there is no corresponding date, the instrument matures on the last day of that month.

[Article (X)]

* A Contracting State whose legislation requires that a signature on an instrument be handwritten may, at the time of signature, ratification or accession, make a declaration to the effect that a signature placed on an instrument in its territory must be handwritten. (Footnote in original).

Article 9

(1) A bill may:

- (a) Be drawn upon two or more drawees;
- (b) Be drawn by two or more drawers;
- (c) Be payable to two or more payees.

(2) A note may:

- (a) Be made by two or more makers;
- (b) Be payable to two or more payees.

(3) If an instrument is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the instrument may exercise the rights of a holder. In any other case the instrument is payable to all of them and the rights of a holder can only be exercised by all of them.

Article 10

A bill may:

- (a) Be drawn by the drawer on himself;
- (b) Be drawn payable to his order.

*Section 3. Completion of an incomplete instrument**Article 11*

(1) An incomplete instrument which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) or (a) and (f) of paragraph (3) of article 1 but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) or (3) of article 1 may be completed and the instrument so completed is effective as a bill or a note.

(2) When such an instrument is completed otherwise than in accordance with an agreement entered into:

(a) A party who signed the instrument before the completion may invoke the non-observance of the agreement as a defence against a holder, provided the holder had knowledge of the non-observance of the agreement when he became a holder;

(b) A party who signed the instrument after the completion is liable according to the terms of the instrument so completed.

CHAPTER THREE. TRANSFER*Article 12*

An instrument is transferred:

- (a) By endorsement and delivery of the instrument by the endorser to the endorsee; or
- (b) By mere delivery of the instrument if the last endorsement is in blank.

Article 13

(1) An endorsement must be written on the instrument or on a slip affixed thereto (*allonge*). It must be signed.

(2) An endorsement may be:

(a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the instrument is payable to a person in possession thereof;

(b) Special, by a signature accompanied by an indication of the person to whom the instrument is payable.

Article 14

(1) A person is a holder if he is:

(a) The payee in possession of the instrument; or

(b) In possession of an instrument which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

(2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.

(3) A person is not prevented from being a holder by the fact that the instrument was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon, the instrument.

Article 15

The holder of an instrument on which the last endorsement is in blank may:

(a) Further endorse the instrument either in blank or to a specified person; or

(b) Convert the blank endorsement into a special endorsement by indicating therein that the instrument is payable to himself or to some other specified person; or

(c) Transfer the instrument in accordance with paragraph (b) of article 12.

Article 16

When the drawer or the maker has inserted in the instrument, or an endorser in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the transferee does not become a holder except for purposes of collection.

Article 17

(1) An endorsement must be unconditional.

(2) A conditional endorsement transfers the instrument whether or not the condition is fulfilled.

Article 18

An endorsement in respect of a part of the sum due under the instrument is ineffective as an endorsement.

Article 19

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the instrument.

Article 20

(1) When an endorsement contains the words "for collection", "for deposit", "value in collection", "by procuration", "pay any bank", or words of similar import, authorizing the endorsee to collect the instrument (endorsement for collection), the endorsee:

- (a) May only endorse the instrument for purposes of collection;
- (b) May exercise all the rights arising out of the instrument;
- (c) Is subject to all claims and defences which may be set up against the endorser.

(2) The endorser for collection is not liable upon the instrument to any subsequent holder.

Article 21

The holder of an instrument may transfer it to a prior party or the drawee in accordance with article 12; nevertheless, in the case where the transferee was a prior holder of the instrument, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

Article 22

An instrument may be transferred in accordance with article 12 after maturity, except by the drawee, the acceptor or the maker.

Article 23

(1) If an endorsement is forged, any party has against the forger, and against the person to whom the instrument was directly transferred by the forger, the right to recover compensation for any damages that he may have suffered because of the forgery.

(2) The liability of a party or of the drawee who pays, or of an endorsee for collection who collects, an instrument on which there is a forged endorsement is not regulated by this Convention.

(3) For the purposes of this article, an endorsement placed on an instrument by a person in a representative capacity without authority or exceeding his authority has the same effects as a forged endorsement.

CHAPTER FOUR. RIGHTS AND LIABILITIES

Section 1. *The rights of a holder and of a protected holder*

Article 24

(1) The holder of an instrument has all the rights conferred on him by this Convention against the parties to the instrument.

(2) The holder is entitled to transfer the instrument in accordance with article 12.

Article 25

(1) A party may set up against a holder who is not a protected holder:

- (a) Any defence available under this Convention;
- (b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;
- (c) Any defence to contractual liability based on a transaction between himself and the holder;
- (d) Any defence based on incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a holder who is not a protected holder are subject to any valid claim to the instrument on the part of any person.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

- (a) Such third person asserted a valid claim to the instrument; or
- (b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft.

Article 26

(1) A party may not set up against a protected holder any defence except:

- (a) Defences under articles 29 (1), 30, 31 (1), 32 (3), 49, 53 and 80 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;

(c) Defences based on the incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a protected holder are not subject to any claim to the instrument on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that person.

Article 27

(1) The transfer of an instrument by a protected holder vests in any subsequent holder the rights to and upon the instrument which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to, or a defence upon, the instrument.

(2) If a party pays the instrument in accordance with article 66 and the instrument is transferred to him, such transfer does not vest in that party the rights to and upon the instrument which any previous protected holder had.

Article 28

Every holder is presumed to be a protected holder unless the contrary is proved.

Section 2. The liability of the parties

A. General provisions

Article 29

(1) Subject to the provisions of articles 30 and 32, a person is not liable on an instrument unless he signs it.

(2) A person who signs an instrument in a name which is not his own is liable as if he had signed it in his own name.

Article 30

A forged signature on an instrument does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed the instrument himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own.

Article 31

(1) If an instrument has been materially altered:

(a) Parties who have signed the instrument subsequent to the material alteration are liable thereon according to the terms of the altered text;

(b) Parties who have signed the instrument before the material alteration are liable thereon according to the terms of the original text. Nevertheless a party who has himself made, authorized, or assented to, the material alteration is liable on the instrument according to the terms of the altered text.

(2) Failing proof to the contrary, a signature is deemed to have been placed on the instrument after the material alteration.

(3) Any alteration is material which modifies the written undertaking on the instrument of any party in any respect.

Article 32

(1) An instrument may be signed by an agent.

(2) The signature of an agent placed by him on an instrument with the authority of his principal and showing on the instrument that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the instrument by an agent with his authority, imposes liability on the principal and not on the agent.

(3) A signature placed on an instrument by a person as agent but without authority to sign or exceeding his authority, or by an agent with authority to sign but not showing on the instrument that he is signing in a representative capacity for a named person, or showing on the instrument that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.

(4) The question whether a signature was placed on the instrument in a representative capacity may be determined only by reference to what appears on the instrument.

(5) A person who is liable pursuant to paragraph (3) and who pays the instrument has the same rights as the person for whom he purported to act would have had if that person had paid the instrument.

Article 33

The order to pay contained in a bill does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee.

B. The drawer

Article 34

(1) The drawer engages that upon dishonour of the bill by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any sub-

sequent party who pays the bill in accordance with article 66, the amount of the bill, and any interest and expenses which may be recovered under article 66 or 67.

(2) The drawer may exclude or limit his own liability by an express stipulation on the bill. Such stipulation has effect only with respect to the drawer.

C. *The maker*

Article 35

(1) The maker engages that he will pay to the holder, or to any party who pays the note in accordance with article 66, the amount of the note in accordance with the terms of that note, and any interest and expenses which may be recovered under article 66 or 67.

(2) The maker may not exclude or limit his own liability by a stipulation on the note. Any such stipulation is without effect.

D. *The drawee and the acceptor*

Article 36

(1) The drawee is not liable on a bill until he accepts it.

(2) The acceptor engages that he will pay to the holder, or to any party who pays the bill in accordance with article 66, the amount of the bill in accordance with the terms of his acceptance, and any interest and expenses which may be recovered under article 66 or 67.

Article 37

An acceptance must be written on the bill and may be effected:

- (a) By the signature of the drawee accompanied by the word "accepted" or by words of similar import; or
- (b) By the signature alone of the drawee.

Article 38

(1) An incomplete instrument which satisfies the requirements set out in article 1 (2) (a) may be accepted by the drawee before it has been signed by the drawer, or while otherwise incomplete.

(2) A bill may be accepted before, at or after maturity, or after it has been dishonoured by non-acceptance or non-payment.

(3) When a bill drawn payable at a fixed period after sight, or a bill which must be presented for acceptance before a specified date, is accepted, the acceptor must indicate the date of his acceptance; failing such indication by the acceptor, the drawer or the holder may insert the date of acceptance.

(4) If a bill drawn payable at a fixed period after sight is dishonoured by non-acceptance and the drawee subsequently accepts it, the holder is entitled to have the acceptance dated as of the date on which the bill was dishonoured.

Article 39

(1) An acceptance must be unqualified. An acceptance is qualified if it is conditional or varies the terms of the bill.

(2) If the drawee stipulates on the bill that his acceptance is subject to qualification:

(a) He is nevertheless bound according to the terms of his qualified acceptance;

(b) The bill is dishonoured by non-acceptance.

(3) An acceptance relating to only a part of the amount of the bill is a qualified acceptance. If the holder takes such an acceptance, the bill is dishonoured by non-acceptance only as to the remaining part.

(4) An acceptance indicating that payment will be made at a particular address or by a particular agent is not a qualified acceptance, provided that:

(a) The place in which payment is to be made is not changed;

(b) The bill is not drawn payable by another agent.

E. *The endorser*

Article 40

(1) The endorser engages that upon dishonour of the instrument by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the instrument in accordance with article 66, the amount of the instrument, and any interest and expenses which may be recovered under article 66 or 67.

(2) The endorser may exclude or limit his own liability by an express stipulation on the instrument. Such stipulation has effect only with respect to that endorser.

Article 41

(1) Any person who transfer an instrument by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer:

(a) A signature on the instrument was forged or unauthorized; or

(b) The instrument was materially altered; or

(c) A party has a valid claim or defence against him; or

(d) The bill was dishonoured by non-acceptance or non-payment or the note was dishonoured by non-payment.

(2) The damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.

(3) Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the instrument without knowledge of such defect.

F. The guarantor

Article 42

(1) Payment of an instrument, whether or not it has been accepted, may be guaranteed, as to the whole or part of its amount, for the account of a party or the drawee. A guarantee may be given by any person who may or may not already be a party.

(2) A guarantee must be written on the instrument or on a slip affixed thereto (*allonge*).

(3) A guarantee is expressed by the words "guaranteed", "*aval*", "good as *aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires:

(a) A signature alone on the front of the instrument, other than that of the drawer or the drawee, is a guarantee;

(b) The signature alone of the drawee on the front of the instrument is an acceptance; and

(c) A signature alone on the back of the instrument other than that of the drawee is an endorsement.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the acceptor or the drawee in the case of a bill, and the maker in the case of a note.

Article 43

(1) A guarantor is liable on the instrument to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the instrument.

(2) If the person for whom he has become guarantor is the drawee, the guarantor undertakes to pay the bill at maturity.

Article 44

The guarantor who pays the instrument has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

CHAPTER FIVE. PRESENTMENT, DISHONOUR BY NON-ACCEPTANCE OR NON-PAYMENT, AND RECOURSE

Section 1. Presentment for acceptance and dishonour by non-acceptance

Article 45

(1) A bill may be presented for acceptance.

(2) A bill must be presented for acceptance:

(a) When the drawer has stipulated on the bill that it must be presented for acceptance;

(b) When the bill is drawn payable at a fixed period after sight; or

(c) When the bill is drawn payable elsewhere than at the residence or place of business of the drawee, except where such a bill is payable on demand.

Article 46

(1) Notwithstanding the provisions of article 45 the drawer may stipulate on the bill that it must not be presented for acceptance or that it must not be so presented before a specified date or before the occurrence of a specified event.

(2) If a bill is presented for acceptance notwithstanding a stipulation permitted under paragraph (1) and acceptance is refused, the bill is not thereby dishonoured.

(3) If the drawee accepts a bill notwithstanding a stipulation that it must not be presented for acceptance, the acceptance is effective.

Article 47

A bill is duly presented for acceptance if it is presented in accordance with the following rules:

(a) The holder must present the bill to the drawee on a business day at a reasonable hour;

(b) A bill drawn upon two or more drawees may be presented to any one of them, unless the bill clearly indicates otherwise;

(c) Presentment for acceptance may be made to a person or authority other than the drawee if that person or authority is entitled under the applicable law to accept the bill;

(d) If a bill is drawn payable on a fixed date, presentment for acceptance must be made before or on the date of maturity;

(e) A bill drawn payable on demand or at a fixed period after sight must be presented for acceptance within one year of its date;

(f) A bill in which the drawer has stated a date or time-limit for presentment for acceptance must be presented on the stated date or within the stated time-limit.

Article 48

A necessary or optional presentment for acceptance is dispensed with:

(a) If the drawee is dead or has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to incur liability on the instrument as an acceptor, or if the drawee is a corporation, partnership, association or other legal entity which has ceased to exist;

(b) When, with reasonable diligence, presentment cannot be effected within the time-limits prescribed for presentment for acceptance.

Article 49

If a bill which must be presented for acceptance is not so presented, the drawer, the endorsers and their guarantors are not liable on the bill.

Article 50

(1) A bill is considered to be dishonoured by non-acceptance;

(a) When the drawee, upon due presentment, expressly refuses to accept the bill or acceptance cannot be obtained with reasonable diligence or when the holder cannot obtain the acceptance to which he is entitled under this Convention;

(b) If presentment for acceptance is dispensed with pursuant to article 48, unless the bill is in fact accepted.

(2) If a bill is dishonoured by non-acceptance the holder may:

(a) Subject to the provisions of article 55, exercise an immediate right of recourse against the drawer, the endorsers and their guarantors;

(b) Exercise an immediate right of recourse against the guarantor of the drawee.

Section 2. *Presentment for payment and dishonour by non-payment*

Article 51

An instrument is duly presented for payment if it is presented in accordance with the following rules:

(a) The holder must present the instrument to the drawee or to the acceptor or to the maker on a business day at a reasonable hour;

(b) A bill drawn upon or accepted by two or more drawees, or a note signed by two or more makers, may be

presented to any one of them, unless the instrument clearly indicates otherwise;

(c) If the drawee or the acceptor or the maker is dead, presentment must be made to the persons who under the applicable law are his heirs or the persons entitled to administer his estate;

(d) Presentment for payment may be made to a person or authority other than the drawee, the acceptor or the maker if that person or authority is entitled under the applicable law to pay the instrument;

(e) An instrument which is not payable on demand must be presented for payment on the date of maturity or on the business day which follows;

(f) An instrument which is payable on demand must be presented for payment within one year of its date;

(g) An instrument must be presented for payment:

(i) At the place of payment specified on the instrument; or

(ii) If no place of payment is specified, at the address of the drawee or the acceptor or the maker indicated on the instrument; or

(iii) If no place of payment is specified and the address of the drawee or the acceptor or the maker is not indicated, at the principal place of business or habitual residence of the drawee or the acceptor or the maker;

(h) An instrument may be presented for payment at a clearing-house.

Article 52

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If an instrument is not payable on demand, and the cause of delay in making presentment continues to operate beyond 30 days after maturity;

(c) If an instrument is payable on demand, and the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment;

(d) If the drawee, the maker or the acceptor has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to make payment, or if the drawee, the maker or the acceptor is a corporation, partnership, association or other legal entity which has ceased to exist;

(e) If there is no place at which the instrument must be presented in accordance with article 51 (g).

(3) Presentment for payment is also dispensed with as regards a bill, if the bill has been protested for dishonour by non-acceptance.

Article 53

(1) If a bill is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note is not duly presented for payment, the endorsers and their guarantors are not liable thereon.

(3) Failure to present an instrument for payment does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

Article 54

(1) An instrument is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment or when the holder cannot obtain the payment to which he is entitled under this Convention;

(b) If presentment for payment is dispensed with pursuant to article 52 (2) and the instrument is unpaid at maturity.

(2) If a bill is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the drawer, the endorsers and their guarantors.

(3) If a note is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the endorsers and their guarantors.

Section 3. Recourse

A. Protest

Article 55

If an instrument has been dishonoured by non-acceptance or by non-payment, the holder may exercise a right of re-

course only after the instrument has been duly protested for dishonour in accordance with the provisions of articles 56 to 58.

Article 56

(1) A protest is a statement of dishonour drawn up at the place where the instrument has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

(a) The person at whose request the instrument is protested;

(b) The place of protest; and

(c) The demand made and the answer given, if any, or the fact that the drawee or the acceptor or the maker could not be found.

(2) A protest may be made:

(a) On the instrument itself or on a slip affixed thereto (*allonge*); or

(b) As a separate document, in which case it must clearly identify the instrument that has been dishonoured.

(3) Unless the instrument stipulates that protest must be made, a protest may be replaced by a declaration written on the instrument and signed and dated by the drawee or the acceptor or the maker, or, in the case of an instrument domiciled with a named person for payment, by that named person; the declaration must be to the effect that acceptance or payment is refused.

(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purpose of this Convention.

Article 57

(1) Protest for dishonour of a bill by non-acceptance must be made on the day on which the bill is dishonoured or on one of the two business days which follow.

(2) Protest for dishonour of an instrument by non-payment must be made on the day on which the instrument is dishonoured or on one of the two business days which follow.

Article 58

(1) Delay in protesting an instrument for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-acceptance or by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

- (i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;
 - (ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;
 - (iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;
- (b) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;
- (c) As regards the drawer of a bill, if the drawer and the drawee or the acceptor are the same person;
- (d) If presentment for acceptance or for payment is dispensed with in accordance with article 48 or 52 (2).

Article 59

- (1) If a bill which must be protested for non-acceptance or for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.
- (2) If a note which must be protested for non-payment is not duly protested, the endorsers and their guarantors are not liable thereon.
- (3) Failure to protest an instrument does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

B. Notice of dishonour

Article 60

- (1) The holder, upon dishonour of a bill by non-acceptance or by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.
- (2) The holder, upon dishonour of a note by non-payment, must give notice of such dishonour to the endorsers and their guarantors.
- (3) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the instrument.
- (4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the instrument against the party notified.

Article 61

- (1) Notice of dishonour may be given in any form whatever and in any terms which identify the instrument and state that it has been dishonoured. The return of the dishonoured instrument is sufficient notice, provided it is

accompanied by a statement indicating that it has been dishonoured.

- (2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.

- (3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

Article 62

Notice of dishonour must be given within the two business days which follow:

- (a) The day of protest or, if protest is dispensed with, the day of dishonour; or
- (b) The receipt of notice given by another party.

Article 63

- (1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

- (2) Notice of dishonour is dispensed with:

- (a) If after the exercise of reasonable diligence notice cannot be given;
- (b) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:
 - (i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;
 - (ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;
 - (iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;
- (c) As regards the drawer of the bill, if the drawer and the drawee or the acceptor are the same person.

Article 64

Failure to give notice of dishonour renders a person who is required to give such notice under article 60 to a party who is entitled to receive such notice liable for any damages which that party may suffer from such failure, provided that such damages do not exceed the amount referred to in article 66 or 67.

Section 4. Amount payable

Article 65

The holder may exercise his rights on the instrument against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

Article 66

(1) The holder may recover from any party liable:

(a) At maturity: the amount of the instrument with interest, if interest has been stipulated for;

(b) After maturity:

(i) The amount of the instrument with interest, if interest has been stipulated for, to the date of maturity;

(ii) If interest has been stipulated to be paid after maturity, interest at the rate stipulated, or in the absence of such stipulation, interest at the rate specified in paragraph (2), calculated from the date of presentment on the sum specified in paragraph (1) (b) (i);

(iii) Any expenses of protest and of the notices given by him;

(c) Before maturity:

(i) The amount of the bill with interest, if interest has been stipulated for, to the date of payment, subject to a discount from the date of payment to the date of maturity, calculated in accordance with paragraph (3);

(ii) Any expenses of protest and of the notices given by him.

(2) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the instrument is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the instrument is payable. In the absence of any such rates, the rate of interest shall be [] per cent per annum.

(3) The discount shall be at the official rate (discount rate) or other similar appropriate rate effective on the date when recourse is exercised at the place where the holder has his principal place of business, or if he does not have a place of business his habitual residence, or if there is no such rate then at the rate of [] per cent per annum.

Article 67

A party who pays an instrument in accordance with article 66 may recover from the parties liable to him:

(a) The entire sum which he was obliged to pay in accordance with article 66 and has paid;

(b) Interest on that sum at the rate specified in article 66, paragraph (2) from the date on which he made payment;

(c) Any expenses of the notices given by him.

CHAPTER SIX. DISCHARGE

Section 1. Discharge by payment

Article 68

(1) A party is discharged of liability on the instrument when he pays the holder, or a party subsequent to himself who has paid the instrument and is in possession thereof, the amount due pursuant to article 66 or 67:

(a) At or after maturity; or

(b) Before maturity, upon dishonour by non-acceptance.

(2) Payment before maturity other than under paragraph (1) (b) of this article does not discharge the party making the payment of his liability on the instrument except in respect of the person to whom payment was made.

(3) A party is not discharged of liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(4) (a) A person receiving payment of an instrument must, unless agreed otherwise, deliver:

(i) To the drawee making such payment, the instrument;

(ii) To any other person making such payment, the instrument, a receipted account, and any protest.

(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the instrument to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 54.

(c) If payment is made but the person paying, other than the drawee, fails to obtain the instrument, such person is discharged but the discharge cannot be set up as a defence against a protected holder.

Article 69

(1) The holder is not obliged to take partial payment.

(2) If the holder who is offered partial payment does not take it, the instrument is dishonoured by non-payment.

(3) If the holder takes partial payment from the drawee or the acceptor or the maker:

(a) The acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; and

(b) The instrument is to be considered as dishonoured by non-payment as to the amount unpaid.

(4) If the holder takes partial payment from a party to the instrument other than the drawee, the acceptor or the maker:

(a) The party making payment is discharged of his liability on the instrument to the extent of the amount paid; and

(b) The holder must give such party a certified copy of the instrument and of any authenticated protest.

(5) The drawee or a party making partial payment may require that mention of such payment be made on the instrument and that a receipt therefor be given to him.

(6) If the balance is paid, the person who receives it and who is in possession of the instrument must deliver to the payor the receipted instrument and any authenticated protest.

Article 70

(1) The holder may refuse to take payment in a place other than the place where the instrument was presented for payment in accordance with article 51.

(2) If in such case payment is not made in the place where the instrument was presented for payment in accordance with article 51, the instrument is considered as dishonoured by non-payment.

Article 71

(1) An instrument must be paid in the currency in which the amount of the instrument is expressed.

(2) The drawer or the maker may indicate on the instrument that it must be paid in a specified currency other than the currency in which the amount of the instrument is expressed. In that case:

(a) The instrument must be paid in the currency so specified;

(b) The amount payable is to be calculated according to the rate of exchange indicated on the instrument. Failing such indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of maturity;

(i) Ruling at the place where the instrument must be presented for payment in accordance with article 51 (g), if the specified currency is that of that place (local currency); or

(ii) If the specified currency is not that of that place, according to the usages of the place where the instrument must be presented for payment in accordance with article 51 (g);

(c) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the instrument, according to that rate.

(ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of dishonour or on the date of actual payment;

(d) If such an instrument is dishonoured by non-payment, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the instrument, according to that rate;

(ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of maturity or on the date of actual payment.

(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchanges if such loss is caused by dishonour for non-acceptance or non-payment.

(4) The rate of exchange ruling at a certain date is the rate of exchange ruling, at the option of the holder, at the place where the instrument must be presented for payment in accordance with article 51 (g) or at the place of actual payment.

Article 72

(1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party.

(2)(a) If, by virtue of the application of paragraph (1) of this article, an instrument drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment ruling at the place where the instrument must be presented for payment in accordance with article 51 (g).

(b)(i) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated,

at the option of the holder, at the rate of exchange ruling on the date of dishonour, or on the date of actual payment.

- (ii) If such an instrument is dishonoured by non-payment, the amount is to be calculated, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment.
- (iii) Paragraphs (3) and (4) of article 71 are applicable where appropriate.

Section 2. Discharge of a prior party

Article 73

(1) When a party is discharged wholly or partly of his liability on the instrument, any party who has a right of recourse against him is discharged to the same extent.

(2) Payment by the drawee of the whole or a part of the amount of a bill to the holder, or to any party who has paid the bill in accordance with article 66, discharges all parties of their liability to the same extent.

CHAPTER SEVEN. LOST INSTRUMENT

Article 74

(1) When an instrument is lost, whether by destruction, theft or otherwise, the person who lost the instrument has, subject to the provisions of paragraph (2) of this article, the same right to payment which he would have had if he had been in possession of the instrument. The party from whom payment is claimed cannot set up as a defence against liability on the instrument the fact that the person claiming payment is not in possession thereof.

(2)(a) The person claiming payment of a lost instrument must state in writing to the party from whom he claims payment:

- (i) The elements of the lost instrument pertaining to the requirements set forth in article 1 (2) or 1 (3); for this purpose the person claiming payment of the lost instrument may present to that party a copy of that instrument;
 - (ii) The facts showing that, if he had been in possession of the instrument, he would have had a right to payment from the party from whom payment is claimed;
 - (iii) The facts which prevent production of the instrument.
- (b) The party from whom payment of a lost instrument is claimed may require the person claiming payment to

give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost instrument;

(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms;

(d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost instrument, and any interest and expenses which may be claimed under article 66 or 67, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

Article 75

(1) A party who has paid a lost instrument and to whom the instrument is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

(2) Such notification must be given on the day the instrument is presented or on one of the two business days which follow and must state the name of the person presenting the instrument and the date and place of presentment.

(3) Failure to notify renders the party who has paid the lost instrument liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 66 or 67.

(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost instrument and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

Article 76

(1) A party who has paid a lost instrument in accordance with the provision of article 74 and who is subsequently required to, and does, pay the instrument, or who by reason of the loss of the instrument, then loses his right to recover from any party liable to him, has the right:

- (a) If security was given, to realize the security; or

(b) If the amount was deposited with the court or other competent authority or institution, to reclaim the amount so deposited.

(2) The person who has given security in accordance with the provisions of paragraph (2) (b) of article 74 is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the instrument is lost.

Article 77

A person claiming payment of a lost instrument duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 74, paragraph (2) (a).

Article 78

A person receiving payment of a lost instrument in accordance with article 74 must deliver to the party paying the written statement required under article 74, paragraph (2) (a), receipted by him and any protest and a receipted account.

Article 79

(1) A party who has paid a lost instrument in accordance with article 74 has the same rights which he would have had if he had been in possession of the instrument.

(2) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 78.

CHAPTER EIGHT. LIMITATION (PRESCRIPTION)

Article 80

(1) A right of action arising on an instrument may no longer be exercised after four years have elapsed:

(a) Against the maker, or his guarantor, of a note payable on demand, from the date of the note;

(b) Against the acceptor or the maker or their guarantor of an instrument payable at a definite time, from the date of maturity;

(c) Against the acceptor of a bill payable on demand, from the date on which it was accepted;

(d) Against the drawer or an endorser or their guarantor, from the date of protest for dishonour by non-acceptance or non-payment or, where protest is dispensed with, from the date of dishonour.

(2) If a party has paid the instrument in accordance with article 66 or 67 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year from the date on which he paid the instrument.

4. REPORT OF THE SECRETARY-GENERAL: COMMENTARY ON DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES (A/CN.9/213)*

Introduction

1. The United Nations Commission on International Trade Law (UNCITRAL), at its first session, decided to include in its work programme, as a priority topic, the law of international payments. The Commission selected, as one of the items falling within the scope of international payments, the harmonization and unification of law relating to negotiable instruments.¹ At the request of the Commission the International Institute for the Unification of Private Law (UNIDROIT) prepared a "Preliminary report on the possibilities of extending the unification of the law of bills of exchange and cheques".²

* 15 March 1982.

¹ Report of the United Nations Commission on International Trade Law on the work of its first session (1968), *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16* (A/7216), para. 48 (III.) (Yearbook . . . 1968-1970, part two, I, A).

² The preliminary report is reproduced in an annex to A/CN.9/19 (Unification of the law of bills of exchange and cheques: note by the Secretary-General and preliminary report by the International Institute for the Unification of Private Law (UNIDROIT) (Yearbook . . . 1968-1970, part three, III, A, 1).

2. At its second session the Commission considered the preliminary report prepared by UNIDROIT and concluded that a solution to problems arising out of the existence of different systems of negotiable instruments law might lie in the creation of a new negotiable instrument to be used in international transactions only. The Commission decided to make a further study of the possibility of creating such an instrument, based upon an enquiry aimed at securing the views and suggestions of Governments and banking and trade institutions.³ In compliance with this request the Secretariat, in consultation with representatives of international organizations and banking institutions drew up a detailed questionnaire enquiring about (a) current methods and practice for making and receiving international payments; (b) problems encountered in settling international transactions by means of negotiable instruments; and (c) the substance of possible new uniform

³ Report of the Commission on the work of its second session (1969), *Official Records of the General Assembly, Twenty-fourth Session, Supplement No. 18* (A/7618), paras. 79, 86 and 87 (Yearbook . . . 1968-1970, part two, II, A).

rules. The text of the questionnaire and the analysis of the replies received from Governments and banking and trade institutions to the questionnaire are set forth in documents A/CN.9/38* and Add. 1** and A/CN.9/48.***

3. At its third⁴ and fourth⁵ sessions the Commission continued its consideration of the harmonization and unification of the law of negotiable instruments in the light of the above-mentioned documents. At its fourth session the Commission requested the Secretary-General to prepare a draft of uniform rules applicable to a special negotiable instrument for optional use in international transactions.⁶

4. In the course of the preparatory work on such draft uniform rules, carried out in close consultation with banking and trade circles through the vehicle of a Study Group on International Payments,⁷ further questionnaires on specific aspects of negotiable instruments were prepared and addressed to banking and trade institutions throughout the world. The evidence on law and practice thus obtained greatly contributed to the formulation of the "draft uniform law on international bills of exchange and commentary" on that draft,⁸ which the Secretariat in 1972 submitted to the Commission's fifth session.

5. The Commission, at its fifth session, established a Working Group on International Negotiable Instruments consisting of eight Member States of the Commission⁹ and entrusted the Working Group with the preparation of a final draft uniform law on international bills of exchange and promissory notes.¹⁰

6. The Working Group on International Negotiable Instruments held eleven sessions between 1973 and 1981.

The documents setting forth the reports of the Group on the work of its sessions are the following:

Report of the Working Group on the work of its first session (Geneva, 8-19 January 1973), A/CN.9/77; (Yearbook ... 1973; part two, II, 1);

Report of the Working Group on the work of its second session (New York, 7-18 January 1974), A/CN.9/86; (Yearbook ... 1974, part two, II, 1);

Report of the Working Group on the work of its third session (Geneva, 6-17 January 1975), A/CN.9/99; (Yearbook ... 1975, part two, II, 1);

Report of the Working Group on the work of its fourth session (New York, 2-12 February 1976), A/CN.9/117; (Yearbook ... 1976, part two, II, 1);

Report of the Working Group on the work of its fifth session (New York, 18-29 July 1977), A/CN.9/141; (Yearbook ... 1978, part two, II, A);

Report of the Working Group on the work of its sixth session (Geneva, 3-13 January 1978), A/CN.9/147; (Yearbook ... 1978, part two, II, B);

Report of the Working Group on the work of its seventh session (New York, 3-12 January 1979, A/CN.9/157; Yearbook ... 1979, part two, II, A);

Report of the Working Group on the work of its eighth session (Geneva, 3-14 September 1979), A/CN.9/178; (Yearbook ... 1980, part two, III, A);

Report of the Working Group on the work of its ninth session (New York, 2-11 January 1980, A/CN.9/181; (Yearbook ... 1980, part two, III, B);

Report of the Working Group on the work of its tenth session (Vienna, 5-16 January 1981), A/CN.9/196; (Yearbook ... 1981, part two, II, A);

Report of the Working Group on the work of its eleventh session (New York, 3-14 August 1981), A/CN.9/210; (reproduced in this volume, part two, II, A, 1).

7. At an early stage thought was given to the feasibility of restricting the uniform rules to a much narrower scope than that of any of the existing formulations of negotiable instruments law. This approach had been advocated by a UNIDROIT Sub-Commission in a 1955 report referred to in UNIDROIT's "Preliminary report on the possibilities of extending the unification of the law of bills of exchange and cheques".¹¹ This report concluded that the essential differences between the major systems were few,¹² and suggested that the rules applicable to international negotiable instruments should be less numerous than those of the laws now in force. Consequently,

* Yearbook ... 1968-1970, part three, III, A, 2.

** Yearbook ... 1971, part two, 1.

*** Yearbook ... 1971, part two, 2.

⁴ Report of the Commission on the work of its third session (1970), *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17* (A/8017), paras. 103-118 (Yearbook ... 1968-1970, part two, III, A).

⁵ Report of the Commission on the work of its fourth session (1971), *Official Records of the General Assembly, Twenty-sixth Session, Supplement No. 17* (A/8417), paras. 24-35 (Yearbook ... 1971, part one, II, A).

⁶ *Ibid.*, para. 35.

⁷ The meetings of the Study Group, held between 1969 and 1979, have been attended by experts provided by interested international organizations and banking and trade institutions: Commission of the European Communities, European Banking Federation, International Monetary Fund, Organization of American States, UNIDROIT, Hague Conference on Private International Law, International Bank for Economic Co-operation (Moscow), Bank for International Settlements (Basle), International Chamber of Commerce, Accepting Houses Committee (London), Bank of England, Deutsche Bank, National Westminster Bank (London), Federal Reserve Bank of New York, Italian Bankers' Association.

⁸ A/CN.9/67 (Yearbook ... 1972, part two, II, 1).

⁹ The members of the Working Group were Egypt, France, India, Mexico (replaced by Chile at the tenth session), Nigeria, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, United States of America.

¹⁰ Report of the Commission on the work of its fifth session (1972), *Official Records of the General Assembly, Twenty-seventh Session, Supplement No. 17* (A/8717), para. 61 (Yearbook ... 1972, part one, II, A).

¹¹ See para. 1 above.

¹² The examination by the Sub-Commission showed that these differences came down to two specific points: the regulation of protest and forged endorsement. Cf. Report of UNIDROIT, A/CN.9/19, annex (Yearbook ... 1968-1970, part three, III, A, 1).

the uniform existing legal systems have proved to be the most troublesome in the international circulation of bills or notes. After careful consideration and consultations with UNCITRAL Study Group this approach was not accepted. A comparison of the Anglo-American and Geneva system does indeed reveal a similarity in basic principles that govern the contractual rights and obligations embodied in negotiable instruments and the concept of negotiability that is attributed to them. And it is undoubtedly true that a lawyer or merchant dealing with a bill or note under another system will recognize an instrument that is familiar to him. Yet, closer analysis of the existing formulations shows that they vary considerably in terms of the issues covered and that when identical issues are compared they differ with only few exceptions in substance. Furthermore, parts of negotiable instruments law involve a network of interrelationships on the instrument. This network needs to be dealt with as a unit; selecting only some of these issues for inclusion in the uniform rules and remitting all other issues to the applicable law would lead to uncertainty and, since the uniform rules and those of national law may not mesh precisely with each other, to difficulties.

8. The draft prepared by the Working Group therefore purports to be a self-contained system of negotiable instruments law. It reflects a deliberate policy to minimize departures from the content of the existing principal legal systems. Where these systems concur in a given rule, that rule generally has been followed in the draft unless, as in rare instances, contemporary commercial practice indicates a justified departure from such a rule. In the instances where the systems differ, a choice or a compromise between divergent rules was based on available evidence of current commercial practice and needs.

9. Though in common law jurisdictions cheques are traditionally considered to be bills of exchange and are governed by the provisions relating to bills of exchange and certain provisions specific to cheques, the civil law jurisdictions have traditionally considered bills of exchange and cheques as separate instruments fulfilling separate functions governed each by a separate body of legal rules. The Commission, after considering the various options open to it, decided at its fourteenth session that the uniform rules on international bills of exchange and international promissory notes and the uniform rules on international cheques should be drawn up as separate texts and not as a consolidated text.¹³

10. The Working Group on International Negotiable Instruments adopted the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211)* and the draft Convention on International

Cheques (A/CN.9/212)* at the close of its eleventh session (August 1981), after a Drafting Group had reviewed both drafts and established corresponding language versions (in Chinese, English, French, Russian and Spanish).

11. The Commission at its fourteenth session requested the Secretary-General, after the completion of the texts by the Working Group, to circulate them, together with a commentary, to all Governments and interested international organizations for comments. At the request of the Secretariat the commentary on the two draft Conventions was prepared by Professor Aharon Barak and Professor Willem Vis who as former members of the Commission's Secretariat and subsequently as consultants assisted the Working Group on International Negotiable Instruments in the drawing up of the draft Conventions. The commentary on the draft Convention on International Bills of Exchange and International Promissory Notes is set forth in the present report, the commentary on the draft Convention on International Cheques is set forth in document A/CN.9/214.**

Comparative table of the numbering of the articles of the draft Convention adopted by the Working Group and of the draft articles as considered by it

The articles of the Convention have been numbered consecutively only upon its adoption by the Working Group. Until then, the original numbering of the draft articles has generally been maintained throughout the various stages of the deliberations by the Working Group in order to facilitate reference to the relevant reports of the Working Group; where, exceptionally, draft provisions have been transferred or combined with other provisions, their previous location is also indicated in the following table.

The original numbering may also assist in a comparison between provisions on bills or notes and on cheques since each draft article on cheques had been numbered to correspond to the draft article on bills or notes which relates to the same or a similar issue.

Number of article in Convention	Number of previous draft article	Number of article in Convention	Number of previous draft article
1	1	18	18
2	3	19	19
3	4	20	20
4	5	21	21
	(5 (10) incorporating earlier 27 (3))	22	22 bis
5	6	23	22
6	7	24	23
7	8	25	24
8	9	26	25
9	10	27	25 bis
10	10 bis		(earlier 25 (4) and 68 (2))
11	11	28	26
12	13	29	27
13	New article (between 13 and 13 bis)	30	28
	13 bis	31	29
14	15	32	30
15	16	33	30 bis
16	17	34	34
17		35	34 bis
		36	36
		37	37

* Reproduced in this volume, part two, II, A, 3.

¹³ Report of the Commission on the work of its fourteenth session (1981), *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 22 (Yearbook . . . 1981, part one, A).

* Reproduced in this volume, part two, II, A, 5.

** Reproduced in this volume, part two, II, A, 6.

Number of article in Convention	Number of previous draft article	Number of article in Convention	Number of previous draft article
38	38	60	62
39	39	61	63
40	41	62	64
41	42	63	65
42	43	64	66
43	44	65	66 bis
44	45	66	67
45	46	67	68
46	47	68	70
47	47 bis, 48	69	71
48	49	70	72
49	50	71	74
50	51	72	74 bis
51	53	73	78
52	54	74	80
53	55	75	81
54	56	76	82
55	57	77	83
56	58	78	84
57	59	79	85
58	61	80	79
59	60		

Abbreviations used in the commentary

BEA:	Bills of Exchange Act, 1882 (United Kingdom)
Convention:	Draft Convention on International Bills of Exchange and International Promissory Notes, as adopted by the UNCITRAL Working Group on International Negotiable Instruments (A/CN.9/211)*
Geneva Convention of 1930:	Convention Providing a Uniform Law for Bills of Exchange and Promissory Notes (Geneva, 1930)
UCC:	Uniform Commercial Code (United States)
ULB:	Uniform Law on Bills of Exchange and Promissory Notes, set forth in annex I to the Geneva Convention of 1930

* Reproduced in this volume, part two, II, A, 3.

Commentary on draft Convention on International Bills of Exchange and International Promissory Notes

CHAPTER ONE. SPHERE OF APPLICATION AND FORM OF THE INSTRUMENT

Article 1

(1) This Convention applies to international bills of exchange and to international promissory notes.

(2) An international bill of exchange is a written instrument which:

(a) Contains, in the text thereof, the words "international bill of exchange (Convention of ...)";

(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the bill is drawn;

(ii) The place indicated next to the signature of the drawer;

(iii) The place indicated next to the name of the drawee;

(iv) The place indicated next to the name of the payee;

(v) The place of payment;

(f) Is signed by the drawer.

(3) An international promissory note is a written instrument which:

(a) Contains, in the text thereof, the words "international promissory note (Convention of ...)";

(b) Contains an unconditional promise whereby the maker undertakes to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the note is made;

(ii) The place indicated next to the signature of the maker;

(iii) The place indicated next to the name of the payee;

(iv) The place of payment;

(f) Is signed by the maker.

(4) Proof that the statements referred to in paragraph (2) (e) or (3) (e) of this article are incorrect does not affect the application of this Convention.

Relevant legislation

BEA – section 3.

UCC – section 3-103.

ULB – articles 1 and 2.

Cross references

Definite sum of money: article 6.

Payable on demand: article 8 (1) and (2).

Payable at a definite time: article 8 (3).

Money: article 4 (11).

Commentary

1. This article provides the rules for determining when a written instrument qualifies as an "international bill of exchange" or an "international promissory note" under the Convention. If an instrument so qualifies the Convention is applicable. Definitions of an international bill of

exchange and of an international promissory note are set forth in paragraphs (2) and (3), respectively, which make clear that the use of an instrument governed by the provisions of this Convention is entirely optional. The initial choice to use an instrument subject to the Convention is exercised by the drawer of a bill or the maker of a note. He may do so if certain international elements are present, but he is under no obligation to draw a bill or make a note under the Convention. Persons other than the drawer or the maker are bound by the provisions of the Convention by virtue of their signature on the international instrument or by taking it up. As regards the applicability of this Convention, see also article 2.

Paragraph (1)

2. This paragraph is of a declaratory character.

Paragraph (2)

3. This paragraph defines an international bill of exchange, i.e. it lays down the basic formal requisites with which an instrument must comply in order to be an international bill of exchange governed by this Convention. Non-compliance of an instrument with these requisites makes the Convention inapplicable. However it is to be noted that an incomplete instrument may be completed in accordance with article 11. The inapplicability of this Convention is the sole consequence of non-compliance with paragraph (2); such non-compliance does not interfere with the validity of the instrument under applicable national law (e.g., the law of the place of drawing or of the place of issuance).

"A written instrument"

4. The term "written" is not defined in the Convention. This term, in the context in which it is here used, would include any mode of representing or reproducing words in visible form, such as handwritten, typed or printed.

5. Subject to the requirements laid down in paragraph (2), the validity of an instrument as an international bill of exchange is not dependent on the use of any specific wording or any specific language.

Formal requisites of an international bill of exchange

6. Subparagraphs (a) to (f) set forth the formal requisites of a bill of exchange.

Subparagraph (a)

7. An instrument is valid as an international bill of exchange under the Convention only when the drawer, in the text thereof, has inserted the words "international bill of exchange (Convention of . . .)". This designation, which expresses the intent of the parties that their liability on the instrument is governed by the Convention, must be incorporated "in the text" of the instrument. Such designation would not meet the requirement of subparagraph (a) if it appeared outside the text, as where it

would be printed or stamped in the margin of the instrument. The requirement is intended to guard against altering the character of an instrument after its issuance.

Subparagraph (b)

8. An international bill of exchange must be an "unconditional order" (it must not be payable upon a contingency) to pay a "definite sum of money" (as defined in article 6). The sum is payable to the "payee". Therefore, the Convention does not permit that a bill of exchange is drawn payable to bearer. However, the payee or a special endorsee may make the bill payable to bearer by endorsing it in blank (see article 13 (2) (a)).

9. The wording of subparagraph (b) permits a drawer to draw an international bill of exchange on himself or to draw it payable to himself (see also article 10).

10. The words "or to his order" have been added after the words "to the payee" because of a well-established practice in certain common law countries to draw bills of exchange "to the order of" a payee. However, the omission of the words "or to his order" does not prevent the bill of exchange from being a negotiable instrument under this Convention. Therefore, an international bill of exchange may be drawn "pay to X", "pay to the order of X", or "pay to X or to his order".

Subparagraph (c)

11. An international bill of exchange must be payable either "on demand" (as defined in article 8 (1)) or "at a definite time" (as defined in article 8 (3)). If an instrument does not state a time of payment, it may nevertheless be a valid instrument under this Convention since it is then deemed to be payable on demand (cf. article 8 (1) (b)).

Subparagraph (d)

12. The date of the instrument is relevant in the context of other provisions of this Convention, such as article 51 (f).

Subparagraph (e)

13. International bills of exchange are intended to be used in international payment transactions. Therefore, the Convention should be applicable only when elements are present evidencing the international character of the payment transaction. Consideration was given, during the preparatory stage of the work, to the feasibility of linking the test of internationality to the requirement that an international bill of exchange be used solely to settle international transactions, such as an international sale of goods, or a test geared to potential conflict of law situations. These tests were not retained because they were considered impracticable and uncertain. Instead, preference was given to the approach reflected in subparagraph (e) which requires that the elements of internationality be apparent from the face of the instrument.

14. Subparagraph (e) requires that at least two of the following places indicated on the bill of exchange be situated in different States: the place of drawing, the place indicated next to the signature of the drawer, the place indicated next to the name of the drawee, the place indicated next to the name of the payee, and the place of payment. The analysis of this test shows that it embraces the majority of cases in which there is an international movement of credit and also the principal situations in which conflicts of law may arise. Subparagraph (e) does not require that a street address and the name of a town appear on the bill of exchange. For the purpose of internationality it suffices for the bill to mention two different States. Thus a bill drawn by J. Brown, Australia, made payable to A. Petrov, Bulgaria, would meet the requirement of subparagraph (e).

Subparagraph (f)

15. The order to pay, contained in the bill of exchange, is an order that can only be given by the drawer. His signature is an indispensable element of the validity of an instrument as a bill of exchange. If the signature of the drawer is lacking, the instrument cannot be made into a bill of exchange by completion (cf. article 11).

16. A bill of exchange may be drawn by two or more drawers (cf. article 9 (1) (b)).

Paragraph (3)

17. The comments in respect of the international bill of exchange apply, *mutatis mutandis*, to the international promissory note.

Paragraph (4)

18. The security of transactions in connection with international bills of exchange and international promissory notes depends on a clear and indisputable identification of the legal regime. To this end, paragraphs (2) (a) and (3) (a) require that the bill or note contain in its text the words "international bill of exchange", or "international promissory note", followed by the words "(Convention of . . .)". In addition, under paragraphs (2) (e) and (3) (e), an instrument, in order to be subject to this Convention, must show that at least two places, as specified, are situated in different States. The requisite of "internationality" consequently must appear from the statements made on the instrument. These rules are strengthened by the rule of paragraph (4) whereby the applicability of this Convention cannot be placed in doubt by controverting the statements made on the face of the bill or the note in conformity with paragraph (2) (e) or (3) (e).

19. Paragraph (4) has the same effect as a provision that, for the purpose of application of the Convention, the appearance of international elements, required under paragraph (2) (e) or (3) (e), constitutes an irrebuttable

presumption. Therefore, an incorrect statement as to the place of drawing or making etc., so as to bring the instrument under the Convention, does not thereby make the instrument invalid as an international bill of exchange or an international promissory note, and cannot be a defence to be raised against a holder, even if the holder, when taking the instrument, had knowledge of the fact that a statement was incorrect. To provide otherwise would lend grounds for casting doubts on the applicability of the Convention, and would impair the circulation of the international bill of exchange or promissory note.

20. Incorrect or false statements made on a bill or a note as to the international elements may of course be considered by a State as violating its law.

Article 2

This Convention applies without regard to whether the places indicated on an international bill of exchange or on an international promissory note pursuant to paragraph (2) (e) or (3) (e) of article 1 are situated in Contracting States.

Cross references

Definition of "international bill of exchange": article 1 (2).

Definition of "international promissory note": article 1 (3).

Commentary

1. The sole requirement for the Convention's applicability is that the instrument is an international bill of exchange or an international promissory note, i.e. an instrument which complies with the formal requirements laid down in article 1 (2) or (3). Under this test, the forum of a Contracting State would apply the Convention, and not its domestic law or the negotiable instruments law of a foreign State which, through the application of conflict rules, might otherwise be applicable.

2. The provision of article 2 may be illustrated by the following example. An instrument containing, in the text thereof, the words "international bill of exchange (Convention of . . .)" (see article 1 (2) (a)) on its face shows that it is drawn in State X on drawee in State Y. Neither X nor Y is a Contracting State. The instrument is accepted by the drawer, and the payee endorses the bill to E. The acceptor dishonours the bill by non-payment and E requests the drawer to pay the bill. The drawer asserts a defence (for instance, failure by the holder to observe applicable formalities as to protest), and the holder brings his claim before the court of a Contracting State. By virtue of article 2, the Convention is applicable, and the rights and liabilities of all parties to the bill are governed by the Convention, irrespective of the place where each separate contract on the bill was made, where the bill

was dishonoured, or where protest was made or should have been made. This rule on the applicability of the Convention thus supplants the various rules on conflict of laws that might otherwise be applicable.

3. In substance, article 2 gives effect to the intention of the parties that their legal relationships on the bill or note are to be governed by the Convention, in accordance with the statement on the instrument. Thus parties signing an international bill or note as drawer, maker, endorser, guarantor or acceptor thereby manifest their intention that their liabilities on the instrument be governed by the Convention. The same may be said of a person who takes the bill or note as transferee, holder or protected holder. The application of the Convention to legal relationships between parties to an international bill or note on the sole ground that the instrument is an international instrument responds therefore to the reasonable expectations of the parties.

4. Of course, the obligation to apply the Convention in the circumstances defined in articles 1 and 2 is incumbent on Contracting States only. Consequently, whether the forum of a non-contracting State would apply the Convention to an instrument that complies with the requirements set forth in article 1 (2) or (3) would depend on the conflict of law rules of that forum. Presumably, the forum of a non-contracting State would consider such an instrument to be an international bill of exchange or promissory note subject to the Convention if its conflict rules referred to the law of the country where the instrument was drawn and if the country is a Contracting State. But in other factual settings a non-contracting State may apply the rules of the national law rather than this Convention. In such cases, an instrument, drawn as an international bill or note under the Convention, might not qualify as a bill or note under the applicable law. The Convention seeks to meet that potential problem by laying down, in article 1 (2) and (3), requisites that are in substance similar to those which in the principal legal systems are considered to be the minimum requirements for an instrument to qualify as a bill of exchange or promissory note. Hence, the presence on an instrument of the requisites under article 1 (2) or (3) will, in most cases, also qualify the instrument as a bill of exchange or promissory note under whatever national law may be applicable. Therefore, article 1 (2) or (3) helps to ensure that an instrument drawn pursuant to its provisions will qualify as a negotiable instrument even if the forum of a non-contracting State applies its own law or, by reason of its conflict rules, applies the law of another non-contracting State. However, there may be cases where an instrument that satisfies the requisites of article 1 (2) or (3) will not meet one of the requirements imposed by a national law.

5. Consideration has been given to adding a provision that the Convention would be applicable only if the

instrument was drawn, made or issued in a Contracting State. The principal effect of such a rule would be to discourage banking and trade circles from drawing international bills of exchange or making international promissory notes in non-contracting States and thereby reduce the complications that might result from the application of conflict rules by the fora of non-contracting States. Such a rule limiting the applicability of the Convention has not been incorporated in the Convention. Under this Convention a person is given the opportunity to draw, make, accept, endorse or guarantee an international instrument without regard to whether it is drawn in a Contracting State or a non-contracting State, and a court in a Contracting State would give effect to his intent that the rules of the Convention should apply which was expressed on the face of the instrument and by the voluntary use thereof. Of course, the court of a non-contracting State may not give effect to this intent. This possibility, however, can be taken into account by the parties in deciding whether to employ the international instrument in the light of their expectations as to whether litigation would be brought in a Contracting or in a non-contracting State. Furthermore, the rule mentioned above would necessarily make the Convention inapplicable to an instrument drawn as an international bill of exchange in a non-contracting State, even where the drawee is in a Contracting State, or the bill is payable in a Contracting State, and litigation arises in a Contracting State. Such a rule would unduly restrict the scope of application of the Convention.

6. The above problem, and others related to the application of uniform rules to rights and liabilities on an international instrument, are inherent in the process of adoption of uniform rules for as long as a Convention setting forth such rules is not universally adopted and applied.

CHAPTER TWO. INTERPRETATION

Section I. General provisions

Article 3

In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application.

Commentary

1. One of the important objectives of the article is to promote uniformity in the interpretation and application of this Convention. To this end, the text of the Convention directs attention to its "international character"; due regard for the international character of the Convention would avoid interpreting its provisions by recourse to local (and varying) national concepts, rather than to

the Convention's provisions read as an independent piece of international legislation. This article may also be helpful to encourage tribunals in one State to promote uniformity by interpreting the Convention with due regard to the interpretation given to it in other States.

2. The general principle with regard to the interpretation and application of the Convention, laid down in this article, is found in other Conventions that originated in the work of the United Nations Commission on International Trade Law (UNCITRAL), see article 7 of the Convention on the Limitation Period in the International Sale of Goods (1974)*, article 3 of the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules)**, and article 7 (1) of the United Nations Convention on Contracts for the International Sale of Goods (1980)***.

Article 4

In this Convention:

- (1) "Bill" means an international bill of exchange governed by this Convention;
- (2) "Note" means an international promissory note governed by this Convention;
- (3) "Instrument" means a bill or a note;
- (4) "Drawee" means the person on whom a bill is drawn but who has not accepted it;
- (5) "Payee" means the person in whose favour the drawer directs payment to be made or to whom the maker promises to pay;
- (6) "Holder" means a person in possession of an instrument in accordance with article 14;
- (7) "Protected holder" means the holder of an instrument which, when he became a holder, was complete and regular on its face, provided that:
 - (a) He was, at that time, without knowledge of a claim to or defence upon the instrument referred to in article 25 or of the fact that it was dishonoured by non-acceptance or non-payment;
 - (b) The time-limit provided by article 51 for presentment of that instrument for payment had not then expired;
- (8) "Party" means any person who has signed an instrument as drawer, maker, acceptor, endorser or guarantor;
- (9) "Maturity" means the date of payment referred to in article 8;

(10) "Signature" includes a signature by stamp, symbol, facsimile, perforation or other mechanical means* and "forged signature" includes a signature by the wrongful or unauthorized use of such means;

[(11) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution even if intended by it to be transferable only in its records and between it and persons designated by it or between such persons.]**

Commentary

Paragraphs (1) and (2): "bill" and "note"

1. Article 1 (1) of this Convention provides that the Convention applies to an international bill of exchange and an international promissory note. Article 1 (2) or (3) specifies the formal requisites with which an instrument must comply in order to be an international bill or note. This Convention uses the expression "bill" or "note" to replace the longer expression "international bill of exchange" or "international promissory note".

Paragraph (3): "instrument"

2. The expression "instrument" denotes an international bill of exchange or an international promissory note and is employed in this Convention whenever a provision is applicable to either a bill or a note.

Paragraph (4): "drawee"

3. In this Convention, the drawee who has accepted a bill is called the "acceptor". Therefore, in all instances in which the term "drawee" is used, he is not an acceptor and thus not a party to a bill.

Paragraph (5): "payee"

4. In a bill or a note, the payee is the specified person to whom payment must initially be made. An instrument may be made payable to two or more payees (cf. article 9 (2)). In a bill, the payee may be the drawer (cf. article 10 (b)) or the drawee.

Paragraph (6): "holder"

Relevant legislation

BEA — section 2.
 UCC — section 1-201 (20).
 ULB — article 16.

*

[Article (X)]

A Contracting State whose legislation requires that a signature on an instrument be handwritten may, at the time of signature, ratification or accession, make a declaration to the effect that a signature placed on an instrument in its territory must be handwritten. (Footnote in original).

** Square brackets, used in the text of the Convention, indicate matters which have been reserved for further consideration and decision at a later stage. (Footnote in original).

* Yearbook . . . 1974, part three, I, B.

** Yearbook . . . 1978, part three, I, B.

*** Yearbook . . . 1980, part three, I, B.

Cross references

Holder: article 14.

Rights of a holder: articles 24 and 25.

5. The rights to and upon an instrument are vested in the holder. He has the right to receive payment at maturity, and payment to him discharges the party paying (article 68). Being a "holder" is a necessary element for qualifying as a protected holder. Under Chapter Five of this Convention, the holder is to present the bill for acceptance and for payment, and, in the event of dishonour, to protest the bill and to give notice of dishonour.

6. Pursuant to article 14, in order to be a holder, a person must be the payee or the endorsee of an instrument and in possession of it, or a person in possession of an instrument on which the last endorsement is in blank. If an instrument shows more than one endorsement, there is the further requirement that the series of endorsements be uninterrupted.

Example A. The payee endorsed the bill "to A" (a "special" endorsement) and delivered the bill to A. A is the holder.

Example B. The payee endorsed the bill to "A", and delivered the bill to B. Neither A nor B is a holder.

Example C. The payee endorsed the bill in blank and delivered it to A. A is the holder.

Example D. The payee endorsed the bill in blank. The bill was stolen by T. T is the holder. Since the payee is not "in possession" of the bill, he is not the holder.

7. Under the definition of "holder", a drawer, a maker or guarantor are not holders since they are neither a "payee" nor "endorsee". If the instrument is endorsed to them or if an instrument on which the last endorsement is in blank is delivered to them, they are a holder.

Example E. The acceptor dishonoured the bill. The holder exercised his rights of recourse, and was paid by the drawer. The bill was delivered to the drawer without an endorsement. The drawer (being neither "payee" nor "endorsee") is not the holder of the bill. However, he has rights on the bill against the acceptor in accordance with article 36 (2).

8. A payee or endorsee may reacquire an instrument. Even though the instrument is not endorsed to them, in connection with the reacquisition, the "payee" or "endorsee" comply with the definition of "holder" (article 21).

9. If a holder parts with possession of the instrument he ceases to be the holder. If the lack of possession is caused by the loss of the instrument his rights are determined by the rules on "lost instruments" (articles 74-79).

10. For the purposes of the definition of holder it is irrelevant whether the possession of the instrument is lawful or not. As seen from example D, even a thief may be a holder. Of course, if the possession is unlawful, there

may be a defence on or a claim to the instrument pursuant to article 25.

11. To be a "holder" the possessor need not be the owner of the instrument. When an instrument is endorsed "for collection", the endorsee in possession is the holder of the instrument, although he may be only an agent of the endorser rather than the owner of it.

Paragraph (7): "protected holder"

Relevant legislation

BEA — section 29.

UCC — sections 3-302 and 3-304.

ULB — articles 16 and 17.

Cross reference

Protected holder: article 26.

12. The main advantages of an instrument result from the strong legal position of a protected holder: as a general rule, he takes the instrument free from claims of ownership third parties may have to the instrument and from defences to an action by him on the instrument (article 26).

"Was complete and regular on its face"

13. A person does not acquire the status of a protected holder if the instrument, on the face of it, is not complete and regular. For example, a "bill" on which the sum payable is lacking is not complete even though a person may complete it in accordance with article 11. It may be noted that a person, upon so completing an incomplete instrument, may become a holder but cannot become a protected holder. A bill is not regular if, for instance, the name of the first endorser does not correspond to the name of the payee. The expression "on its face" means that the holder need not look beyond the instrument, and refers to both the face and the back of the instrument.

"Without knowledge"

14. A holder does not qualify as a protected holder if, when taking the instrument, he knows about the existence of a claim or a defence affecting the instrument or about the fact that it was dishonoured. Such holder takes the instrument at his own risk, and it is not the policy of this Convention to protect him. However, it should be noted that under article 27 (the so-called "shelter-rule") the transfer of an instrument by a protected holder may vest in any subsequent holder the rights of the protected holder, even though the subsequent holder is not a protected holder in his own right as where, for instance, he knew of a claim or a defence.

15. For the definition of the expression "without knowledge", see article 5 and commentary.

"At that time"

16. A holder may be a protected holder even though he acquired knowledge of claims, defences or the fact that the instrument had been dishonoured after he became a holder.

17. A person may be a protected holder even though he has not given value or consideration for the instrument. This rule is consistent with some legal systems, notably those of civil law inspiration, and departs from others (e.g. BEA, section 29 (1), and UCC, sections 3-302 (1) (a) and 3-303). The present approach was selected because of the problems of unifying the different approaches to the relevance of "value" or "consideration" by legal systems.

Paragraph (8): "party"

18. The Convention uses the term "party" to refer to a party to an instrument, i.e. a person who has signed a bill or a note. The drawer, maker, endorser, acceptor and guarantor are parties to an instrument. On the other hand, the payee is not a party to the bill or the note (unless he has endorsed it) and the drawee is not a party to the bill.

Paragraph (9): "maturity"*Relevant legislation*

BEA — sections 10, 11 and 14.

UCC — sections 3-108 and 3-109.

ULB — articles 34, 35, 36 and 37.

Cross reference

Time of payment and maturity: article 8.

19. The expression "maturity" appears in several provisions of this Convention (e.g. articles 8 (2), (5), (6) and (7), 47 (d), 51 (e), 66 (1) and 71 (2)).

20. In the case of a fixed-term instrument the maturity date is indicated on the instrument. In the case of a demand instrument the maturity date is the date on which the instrument is presented for payment. In the case of a bill payable at a fixed period after sight the maturity date is to be determined according to the period indicated on the instrument to be calculated as from the date on which the bill is presented for acceptance.

Paragraph (10): "signature" and "forged signature"

21. This provision accommodates modern practice in respect of signatures on negotiable instruments. Therefore a signature need not be handwritten. A complete signature is not necessary.

22. Article (X) permits a Contracting State whose legislation requires that signatures on negotiable instruments be executed in handwriting to make, at the time of signing, ratifying or acceding to the Convention, a declara-

tion derogating from the provision of paragraph (10) to the effect that a signature placed on an international bill of exchange or an international promissory note in its territory must be handwritten.

23. The term "forged signature" is relevant in the context of article 23, concerning the rights and liabilities of parties to an instrument on which an endorsement is forged, and article 30, concerning the liability of the person whose signature is forged. This paragraph makes articles 23 and 30 applicable where an instrument was signed by an agent without authority or was signed by the wrongful use of any means by which a signature may be made in accordance with the present provision.

Paragraph (11): "money" or "currency"

24. Amongst the formal requisites with which a written instrument must comply in order to qualify as an international bill of exchange or an international promissory note is the requisite that the instrument must contain "an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order" (article 1 (2) (b)) or "an unconditional promise whereby the maker undertakes to pay a definite sum of money to the payee or to his order" (article 1 (3) (b)). The definition of "money" or "currency" set forth in paragraph (11) suggests that the Convention, in addition to providing the usual rule that an instrument is payable in a medium of exchange authorized or adopted by a Government as its official currency, should further provide that an instrument:

(a) May be made payable in other monetary units or units of account such as the special drawing rights (SDRs) of the International Monetary Fund, the European currency units (ECUs) of the European Economic Community and the transferable rouble of the International Bank for Economic Co-operation; and

(b) May call for payment in a specified currency but be denominated in such monetary units or units of account.

25. Whilst it is true that only a limited class (member States of the intergovernmental institution concerned and, exceptionally, certain other authorized holders who are not members) may hold or use the units referred to, their use in a variety of transactions is on the increase. There would appear to be no special reason not to permit the application of the Convention to an instrument payable in such units if the drawer or the maker (who must perform belong to the limited class) should wish to make the instrument subject to the provisions of the Convention. Furthermore, private parties, as a safeguard against currency fluctuations, might wish to denominate the amount of the instrument in, say, SDRs and specify in the instrument the currency in which it is to be paid. Such a denomination would be a "definite sum of money" in that the valua-

tion of an SDR against the specified currency would be available on the date when the instrument is payable.

26. Whether the application of the Convention should be extended in this manner will, in the last resort, depend on the desire of Governments to use the Convention for the above stated purposes. Consequently, the proposed definition of "money" or "currency" is placed between square brackets so as to indicate the tentative nature of the definition. If the views of Governments should be of a positive nature certain provisions of the Convention will have to be amended accordingly.

Article 5

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

Relevant legislation

BEA — sections 29 (1), 59 (1) and 90.

UCC — sections 1-201 (19) and (25), and 3-304.

ULB — articles 16, 17 and 40.

Cross references

Knowledge of a fact: articles 4 (7), 11 (2) (a), 25 (1) (d), 26 (1) (c), 41 (3), and 68 (3).

Commentary

In several provisions of the Convention the rights and liabilities of a party are dependent on whether he took or paid the instrument without knowledge of a certain fact. Under this article the concept of "knowledge" covers (a) actual knowledge of a fact and (b) constructive knowledge, i.e. the person could not have been unaware of the existence of a fact.

Section 2. Interpretation of formal requirements

Article 6

The sum payable by an instrument is deemed to be a definite sum although the instrument states that it is to be paid:

- (a) With interest;
- (b) By instalments at successive dates;
- (c) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due;
- (d) According to a rate of exchange indicated on the instrument or to be determined as directed by the instrument; or
- (e) In a currency other than the currency in which the amount of the instrument is expressed.

Relevant legislation

BEA — section 9.

UCC — section 3-106.

ULB — articles 5 and 33.

Cross references

Amount of the instrument: article 7 (1) and (2).

Interest: article 7 (3) and (4).

Interest to be paid after maturity: articles 66 and 67.

Rate of exchange: article 71.

Commentary

1. This article provides that if an instrument states that it is to be paid with interest, by instalments at successive dates, according to a certain rate of exchange or in another currency, the sum payable is a definite sum for the purpose of article 1 (2) (b) or (3) (b).

Paragraphs (a), (b) and (c)

2. These paragraphs settle a sharp controversy between the principal legal systems. The English and American statutes permit the stipulation of interest on any bill or note and the drawing or making of an instrument with successive maturity dates. In contrast the Geneva Uniform Law permits a stipulation of interest only in the case of a bill or note payable at sight or at a fixed period after sight and denies any effect to a stipulation for interest on bills or notes payable at other maturities. Moreover, the Geneva Uniform Law does not allow instruments to be drawn or made with successive maturity dates. The rules proposed in paragraphs (a), (b) and (c) respond to the majority view expressed by banking and trade circles that it would be desirable for the Convention to permit the drawing or making of instruments containing a stipulation of interest or with successive maturity dates.

3. The sum payable by an instrument is a definite sum only if its amount can be determined *ex facie* the instrument without reference to evidence or sources extrinsic to it. Therefore, the rate of interest must be specified on the instrument, and a mere stipulation that the instrument carries interest without specifying the rate is without effect (article 7 (4)). Similarly, if an instrument is made payable by instalments it must, by virtue of article 1 (2) (b) and (c) or (3) (b) and (c), specify the amount of each instalment and the date on which it is payable.

Paragraphs (d) and (e)

4. These paragraphs sanction the common practice of instruments drawn or made in a currency which is not the currency of the place of payment. If no rate of exchange is indicated on the instrument or the instrument contains no directions to that effect, article 71 applies.

5. Paragraph (d) is intended to cover instruments drawn as follows: "Pay £5,000 in Swiss francs at the rate of exchange of (x) Swiss francs to one pound sterling" or "Pay £5,000 in Swiss francs at the rate of exchange prevailing at maturity"

Article 7

(1) If there is a discrepancy between the amount of the instrument expressed in words and the amount expressed in figures, the amount of the instrument is the amount expressed in words.

(2) If the amount of the instrument is expressed in a currency having the same description as that of at least one other State than the State where payment is to be made as indicated on the instrument and the specified currency is not identified as the currency of any particular State, the currency is to be considered as the currency of the State where payment is to be made.

(3) If any instrument states that it is to be paid with interest, without specifying the date from which interest is to run, interest runs from the date of the instrument.

(4) A stipulation stating that the sum is to be paid with interest is deemed not to have been written on the instrument unless it indicates the rate at which interest is to be paid.

Relevant legislation

BEA – sections 9 (2) and (3), and 72 (4).

UCC – section 3-118 (c).

ULB – articles 5 and 6.

Cross reference

Interest: article 6.

Commentary

Paragraph (1)

1. The sum payable by an instrument may be expressed in words only, in figures only, or in words and figures. If both words and figures are used and there is a discrepancy between them, the words control. The paragraph follows in substance the relevant provisions of the principal legislations.

Paragraph (2)

2. This provision envisages the case where an instrument for X dollars is drawn or made in, say, Toronto, Canada, and made payable in Canberra, Australia. In the absence of any express indication to the contrary, the instrument is then payable in Australian dollars.

Paragraph (3)

3. Unless a stipulation of interest specifies the date from which interest is to run, it runs from the date of the instrument. According to article 1 (2) (d) and (3) (d) an instrument must be dated.

Paragraph (4)

4. It has not proved feasible to indicate a legal rate of interest applicable in the event that a stipulation of interest does not specify a rate. This paragraph follows article 5 of the Geneva Uniform Law according to which "in default of such specification, the stipulation shall be deemed not to be written".

Article 8

(1) An instrument is deemed to be payable on demand:

(a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or

(b) If no time for payment is expressed.

(2) An instrument payable at a definite time which is accepted or endorsed or guaranteed after maturity is an instrument payable on demand as regards the acceptor, the endorser or the guarantor.

(3) An instrument is deemed to be payable at a definite time if it states that it is payable:

(a) On a stated date or at a fixed period after a stated date or at a fixed period after the date of the instrument; or

(b) At a fixed period after sight; or

(c) By instalments at successive dates; or

(d) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due.

(4) The time of payment of an instrument payable at a fixed period after date is determined by reference to the date of the instrument.

(5) The maturity of a bill payable at a fixed period after sight is determined by the date of the acceptance.

(6) The maturity of an instrument payable on demand is the date on which the instrument is presented for payment.

(7) The maturity of a note payable at a fixed period after sight is determined by the date of the visa signed by the maker on the note or, if signature is refused, from the date of presentment.

(8) Where an instrument is drawn, or made, payable at one or more months after a stated date or after the date of the instrument or after sight, the instrument matures on the corresponding date of the month when payment

must be made. If there is no corresponding date, the instrument matures on the last day of that month.

Relevant legislation

BEA — sections 10 and 11.

UCC — sections 3-108 and 3-109.

ULB — articles 2 and 33 to 37.

Cross references

Time of payment: article 1 (2) (c) and (3) (c).

Maturity: article 4 (9).

Commentary

Instruments payable on demand

1. Paragraph (1) (a) permits a wide latitude in the use of expressions which make an instrument payable on demand. The requirement of one standard expression would not appear to be justified in view of well-established practices in different parts of the world.

2. As to the period of time within which an instrument payable on demand must be presented for payment, see article 51 (f).

3. Paragraph (1) (b) restates similar rules found in the principal legal systems.

4. Paragraph (2) provides that where a bill is accepted, or where a bill or note is endorsed or guaranteed, after maturity it is to be deemed payable on demand as regards such acceptor, endorser or guarantor. A similar rule is found in the BEA (section 10).

Instruments payable at a definite time

5. The word "sight" in paragraph (3) (b) refers to presentment for acceptance. "After sight" bills must be presented for acceptance (article 45 (2) (b)) in order to determine the date of maturity.

6. Article 6 provides that a sum payable is a "definite sum" if the instrument states that it is to be paid by instalments (i.e. say \$100 on the first of January 1983, \$100 on the first of January 1984 etc.). Article 8 (3) (c) and (d) provides a parallel rule as to the date of the bill or note, i.e. that a bill or note is payable at a definite time if it states that it is payable by instalments at successive dates. It is also provided that an instrument is payable at a definite time if it states that upon default in payment of an instalment the unpaid balance shall become due immediately.

7. Paragraph (4) provides that when an instrument is payable at a fixed period after date the time of payment is determined by reference to the date of the instrument. This is so even though the instrument is ante-dated or post-dated. According to article 1 (2) (d) and (3) (d) an instrument must be dated.

8. Paragraph (5) deals with the maturity date of a bill of exchange made payable at a fixed period after sight. In respect of such a bill the period begins to run from the date of acceptance. If the acceptor has not dated his acceptance, the holder may insert the date of acceptance (cf. article 38 (3)).

9. Paragraph (6) provides that the maturity of a demand instrument is the date on which the instrument is presented for payment. Instruments payable on demand include those expressly stating that they are payable "on demand", "at sight", "on presentment" or "on presentation", and those in which no time of payment is expressed (cf. article 8 (1)).

10. Paragraph (7) deals with the unfrequent case of a note made payable at a fixed period after sight. Since a note cannot be accepted, the sole purpose of presentment of an after sight note is to determine the date of maturity. The paragraph follows the provisions of article 78 of the ULB.

11. Paragraph (8) is designed to resolve the ambiguity caused by the unevenness in the number of days which make up calendar months. It is based on article 36 of the ULB.

Article 9

(1) A bill may:

(a) Be drawn upon two or more drawees;

(b) Be drawn by two or more drawers;

(c) Be payable to two or more payees.

(2) A note may:

(a) Be made by two or more makers;

(b) Be payable to two or more payees.

(3) If an instrument is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the instrument may exercise the rights of a holder. In any other case the instrument is payable to all of them and the rights of a holder can only be exercised by all of them.

Relevant legislation

BEA — sections 6 (2) and 32 (3).

UCC — sections 3-110 (1) (d) and 3-116.

Cross references

Signature: articles 4 (10) and 29.

Holder: articles 4 (6) and 14.

Commentary

Paragraphs (1) and (2)

1. Article 1 (2) provides that an international bill of exchange is a written instrument which, *inter alia*, contains

an unconditional order whereby one person (the drawer) directs another person (the drawee) to pay a definite sum of money to a specified person (the payee). Article 1 (3) provides that an international promissory note is a written instrument which, *inter alia*, contains an unconditional promise whereby one person (the maker) undertakes to pay a definite sum of money to another person (the payee).

2. The purpose of paragraphs (1) and (2) of this article is to make clear that a written instrument is also a bill or a note if the direction or undertaking to pay is made by more than one person or if the persons directed to pay or directed or promised to receive payment are several.

3. Although enquiries amongst banking and trade institutions revealed that a plurality of drawees is only infrequently found on bills, the majority view amongst those consulted favoured a rule that would permit such practice expressly.

Paragraph (3)

4. This paragraph deals with the case where an instrument is drawn or made payable to two or more payees. It provides a rule of interpretation whereby, if the instrument does not state expressly that such payees are in the alternative, it is payable to all of them and only all of them can exercise the rights of a holder.

Example. A bill is drawn payable to A and B. A endorses the bill to C. What are C's rights? If A has authority to endorse the bill in the name of B, C is the holder, and has all the rights which a holder has under this Convention. On the other hand, if A has no authority to endorse the bill on behalf of B, his signature is not an "endorsement" since it is not signed by the proper persons, i.e., A and B together.

5. Where an instrument provides that it is payable to A or B, every one of them in possession of the instrument is its holder (see definition of holder in article 14); and every one of them in possession of the instrument may exercise the rights of a holder as provided by this Convention.

6. Where an instrument is drawn or made payable to A and/or B, it is considered to be payable to both A and B, and not any one of them.

Article 10

A bill may:

- (a) Be drawn by the drawer on himself;
- (b) Be drawn payable to his order.

Relevant legislation

BEA – section 5.
UCC – section 3-110.
ULB – article 3.

Commentary

The drawer of a bill may address the order to pay to himself, and he may draw the bill payable to himself or to his order. Therefore, one person may be both drawer and drawee, or both drawer and payee.

Section 3. Completion of an incomplete instrument

Article 11

(1) An incomplete instrument which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) or (a) and (f) of paragraph (3) of article 1 but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) or (3) of article 1 may be completed and the instrument so completed is effective as a bill or a note.

(2) When such an instrument is completed otherwise than in accordance with an agreement entered into:

(a) A party who signed the instrument before the completion may invoke the non-observance of the agreement as a defence against a holder, provided the holder had knowledge of the non-observance of the agreement when he became a holder;

(b) A party who signed the instrument after the completion is liable according to the terms of the instrument so completed.

Relevant legislation

BEA – section 20.
UCC – sections 3-115 and 3-407.
ULB – article 10.

Cross references

Holder: articles 4 (6) and 14.
Knowledge: article 5.

Commentary

1. Article 11 deals with the completion of a writing which lacks one or more of the requirements set forth in article 1 (2) or (3) of this Convention: a definite sum of money, the name of the payee, the name of the drawee, or one or more of the places referred to in article 1 (2) (e) or (3) (e) etc. However, the power conferred by article 11 does not include the power to insert: (a) the signature of the drawer or the maker and (b) the words "international bill of exchange (Convention of . . .)" or "international promissory note (Convention of . . .)". Therefore, only an instrument on which such designation already appears and which is signed by the drawer or the maker may be completed as a bill or a note by inserting such other elements as are required by article 1 (2) or (3). The rationale underlying this rule is that only the drawer or the maker decides

whether the instrument he issues is to be governed by the Convention. It may be noted that a writing which lacks the words "international bill of exchange (Convention of . . .)" or "international promissory note (Convention of . . .)" may be completed under the applicable national law but would, if completed, not be governed by the Convention.

2. If a writing lacks elements pertaining to one or more of the requirements set out in article 1 (2) or (3) it is not a bill or a note under this Convention and cannot be enforced as a bill or a note until completed. When the lacking elements have been inserted the writing becomes a bill or a note within the meaning of article 1 and the Convention is applicable.

3. Article 11 deals with the completion of an instrument which lacks elements that are required for purposes of validity under the Convention. The article does not apply to the alteration or correction of elements that appear on an incomplete or complete instrument. In the latter case article 31 concerning material alterations applies.

4. The mere fact that an instrument was issued incomplete cannot be set up by a party as a defence against his liability on the instrument as completed. However, if an incomplete instrument is completed otherwise than in accordance with an agreement entered into, two situations affecting the liability of parties to that instrument are envisaged by paragraph (2):

(a) If a party signed the instrument before its completion he may raise the fact that it was completed otherwise than in accordance with the agreement entered into as a defence to his liability against any holder with knowledge of that fact;

(b) If a party signed the instrument after its completion, inobservance of the agreement entered into cannot be set up as a defence to his liability, not even against a holder with knowledge of such inobservance.

Example. An incomplete instrument, containing in the text thereof the words "international bill of exchange (Convention of . . .)" and signed by the drawer is issued to the payee without the sum being stated. It is agreed between the drawer and the payee that the sum to be inserted should be "X". Contrary to this agreement the payee inserts sum "Y" and endorses the bill to A. What are A's rights? If A took the bill without knowledge of the inobservance of the agreement by the payee he has rights on the bill, as completed, against the drawer and the payee. If A knew about the inobservance, the drawer may raise a defence based upon the fact that the incomplete instrument was completed contrary to the agreement between himself and the payee. This defence cannot be raised by the payee. If A with knowledge of the inobservance of the agreement transfers the instrument to B who is without knowledge of the inobservance neither the drawer nor the

payee nor A may raise such inobservance as a defence against B even if B is not a protected holder.

CHAPTER THREE. TRANSFER

Article 12

An instrument is transferred:

(a) By endorsement and delivery of the instrument by the endorser to the endorsee; or

(b) By mere delivery of the instrument if the last endorsement is in blank.

Relevant legislation

BEA — sections 22 (2) and 31.

UCC — section 3-202 (1).

ULB — article 11.

Cross reference

Endorsement: article 13.

Commentary

1. A negotiable instrument, by its nature, is transferable although parties may exclude or limit its transferability (see article 16). The transfer of an instrument is in some legal systems known as "negotiation".

2. Article 12 sets forth the ways in which an instrument may be transferred. It follows in substance the relevant provisions of the existing legal systems. An instrument is transferred when the holder endorses it, either specially or in blank, and delivers it to the endorsee (paragraph (a)) or, if the last endorsement is in blank, when the holder delivers the instrument (paragraph (b)).

3. When an instrument is transferred under this article, the transferee becomes a holder (cf. articles 4 (6) and 14 (1) (b)) and thus acquires the rights, and is subject to all the duties, of a holder. The result obtains irrespective of whether the transfer takes place before, at or after maturity.

Example A. The payee endorses a bill specially to A and delivers it to A. By these acts the bill is transferred to A and A becomes the holder of it.

Example B. The payee endorses a bill specially to A but does not deliver it to A. Without further endorsement the payee delivers the bill to B. The bill is not transferred either to A or to B. Neither A nor B is a holder.

Example C. The payee endorses a note in blank and delivers it to A. The note is thereby transferred to A who becomes its holder. If A delivers the note to B, even without endorsement, the note is thereby transferred to B and B is the holder.

4. It should be noted that article 12 deals only with the transfer of an instrument by endorsement and delivery

or, if the last endorsement is in blank, by mere delivery. The article does not deal with other ways by which a person may acquire the rights to and upon an instrument, as where a person is the heir of the holder or where the holder assigns his rights on the instrument to another person. These questions are left to the applicable national law.

Article 13

(1) An endorsement must be written on the instrument or on a slip affixed thereto (*allonge*). It must be signed.

2. An endorsement may be:

(a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the instrument is payable to any person in possession thereof;

(b) Special, by a signature accompanied by an indication of the person to whom the instrument is payable.

Relevant legislation

BEA — sections 2 and 32.

UCC — section 202 (2).

ULB — article 13.

Cross reference

Signature: article 4 (10).

Commentary

1. An endorsement serves two functions. It is a necessary element in the transfer of an order instrument (article 12 (a)), and it renders the endorser liable on the instrument as a party (article 40 (1)). In most cases, the endorsement is intended to serve both functions. However, the endorser may exclude or limit the liability function of the endorsement by an express stipulation on the instrument as provided in article 40 (2), e.g. by inserting the words "without recourse". Also the endorser can exclude or limit the transfer function as regards any possible transfer from his endorsee to others. For example, he may exclude the possibility that a person other than his endorsee becomes a holder except for purposes of collection. He would achieve this by inserting in his endorsement the words "not transferable", "pay (X) only" or words of similar import (article 16).

2. Article 13 explains what is meant by endorsement and how it is effected. An endorsement is effected by the signature of the person endorsing the instrument.

3. The endorsement may be a special or a blank endorsement. A special endorsement is effected by the signature of the endorser accompanied by an indication of the person to whom the instrument is payable (paragraph (2) (b)). A blank endorsement may be effected by the endorser's signature alone or by a signature combined with a statement to the effect that the instrument is payable to any person in possession thereof (paragraph (2) (a)).

Example. The payee signs "pay A". This is a special endorsement to A. However, when the payee signs his name or accompanies his signature by such words as "pay any person" or "pay bearer", the endorsement is a blank endorsement.

4. It should be noted that a signature alone on the instrument is not necessarily a blank endorsement; it may be an acceptance (cf. article 37) or a guarantee (cf. article 42).

5. It may be recalled that the Convention does not permit an instrument to be drawn payable to bearer (see commentary to article 1, paragraph 8); but an order instrument may be made payable to bearer by a blank endorsement by the payee or a special endorsee.

Article 14

(1) A person is a holder if he is:

(a) The payee in possession of the instrument; or

(b) In possession of an instrument which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

(2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.

(3) A person is not prevented from being a holder by the fact that the instrument was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon, the instrument.

Relevant legislation

BEA — section 2.

UCC — sections 1-201 (20) and 3-202 (1).

ULB — article 16.

Cross references

Holder: article 4 (6)

Payee: article 4 (5).

Instrument: article 4 (3).

Endorsement: article 13.

Commentary

1. Under the Convention the concept of "holder" is relevant in, *inter alia*, the following context:

(a) Being a holder is a necessary element of the status of a protected holder (cf. article 5 (7));

(b) The holder may exercise all rights on the instrument against the parties to it (cf. article 24);

(c) A party to an instrument is discharged when he pays the holder (cf. article 68).

2. Pursuant to article 14 a person in order to be a holder

(a) Must be in possession of the instrument; and

(b) Must be a payee or a transferee under a special endorsement or an endorsement in blank.

Example A. The drawer issues a bill and delivers it to the payee. The payee is a holder.

Example B. The payee lost the instrument. Not being in possession of the instrument he is not a holder (as to lost instruments see articles 74-79).

Example C. The payee endorses the instrument to A and delivers it to A. A is a holder.

Example D. The payee endorses the instrument to A and delivers it to B. Neither A nor B is a holder.

Example E. The payee endorses the instrument in blank and delivers it to A. A is a holder.

Example F. The payee endorses the instrument in blank. It is stolen by T. T is a holder.

3. Under this Convention a drawer, a maker, a guarantor or an acceptor is not a holder even though he be in possession of the instrument unless he acquired the instrument under an endorsement in blank. However, these parties have rights to and upon the instrument by virtue of special provisions in this Convention.

Example G. The acceptor of a bill dishonours it by non-payment. The holder is paid by the drawer and delivers the bill to him without an endorsement. The drawer, though in possession of the bill, is not a holder. Nevertheless, by virtue of article 36 (2) the drawer has rights on the bill against the acceptor.

4. A payee or an endorsee may reacquire the instrument by payment or otherwise. By virtue of article 21 such a payee or endorsee, even though the instrument is not endorsed to him, is a holder.

5. For the purposes of holder status it is irrelevant whether the possession of the instrument is lawful or not. As seen from example *F* above even a thief may be a holder. However, if the possession is unlawful the owner of the instrument has a valid claim to the instrument and such claim may be set up as a defence against liability (cf. article 25).

6. To be a holder the possessor of an instrument need not be the owner of it. Where an instrument is endorsed "for collection" the endorsee in possession is the holder of it even though he may be only an agent of the endorser rather than the owner of it.

"Uninterrupted series of endorsements"

7. The question whether the possessor of the instrument is a holder is to be determined only from what appears on the instrument. It is necessary, but it suffices, that the

chain of endorsements: (a) is uninterrupted and (b) designates the possessor as the last endorsee unless the last endorsement is in blank.

Example H. The instrument is stolen from the payee. T, the thief, forges the signature of the payee and endorses the instrument to A. A is a holder. However, the drawer may raise the defence of forgery against A (cf. article 25). Such a defence would not prevail if A is a protected holder (cf. article 26). The payee may claim the instrument from A (cf. article 25 (2)) unless A is a protected holder.

Example I. The payee delivers the instrument to A without an endorsement. A endorses the instrument to B. B is not a holder because the endorsement that is necessary for the establishment of an uninterrupted chain of endorsements (the endorsement of the payee to A) is lacking.

Paragraph (2)

8. The provisions of paragraph (2) may be illustrated by the following example:

Example J. The payee endorses the instrument to A and delivers it to him. A endorses the instrument in blank and delivers it to B. B endorses the instrument specially to C or in blank and delivers it to C. Under article 14 (2), B is deemed to be the endorsee of A by his endorsement in blank. It follows that C is a holder since he received the instrument under an uninterrupted series of endorsements.

Paragraph (3)

9. The purpose of this paragraph is to provide that the transferee is a holder even though the transferor is a person without legal capacity, or the endorsement or delivery was obtained by fraud or other illegal means. The main importance of this provision lies in the fact that such transferee, being a holder, may qualify himself in proper circumstances as a protected holder. Even if such holder is not a protected holder he may transfer the instrument to a person who may take it in proper circumstances as a protected holder.

10. This paragraph does not deal with the question of liability upon an instrument of the party transferring it, nor does it deal with the rights of a person to the instrument. The party transferring the instrument may assert any defence or any claim available to him under articles 25 and 26 of this Convention.

11. Paragraph (3) does not impose any liability on a party who signed the instrument under the circumstances mentioned in the paragraph. The question whether such party may raise the defence of *ius tertii* is governed by article 25 (3).

Example K. A induces the payee by way of fraud to endorse to him a note owned by the payee. Pursuant to article 14 A is a holder of the note. The consequences are shown by the following examples.

Example L. The same facts as in example K. A brings an action against the payee (P). Nothing in this article makes the payee (P) liable to A in spite of the fraud practised by A on P. Pursuant to article 25 the payee has a valid defence to A's action.

Example M. The same facts as in example K. The payee (P) brings an action against A to recover the note or to prohibit A from transferring the note. The payee (P) will succeed if remedies of this type are permitted under the law of the place where the transfer took place.

Example N. The same facts as in example K. A brings an action against the maker. This question is not solved by article 14. The answer to this question is to be found in article 25.

Example O. By fraud A induces the payee (P) to transfer to him a bill owned by P. A transfers the bill to B, who takes it as a protected holder. P brings an action against B for conversion of the bill. P's action fails. According to article 14 A is a holder, and the bill was transferred to B in circumstances that make B a protected holder. According to article 26 P's claim fails against a protected holder.

Example P. The same facts as in example O. B brings an action against the drawer and the payee (P). According to article 26 the defences of the drawer and the payee are not available against B, a protected holder.

Article 15

The holder of an instrument on which the last endorsement is in blank may:

- (a) Further endorse the instrument either in blank or to a specified person; or
- (b) Convert the blank endorsement into a special endorsement by indicating therein that the instrument is payable to himself or to some other specified person; or
- (c) Transfer the instrument in accordance with paragraph (b) of article 12.

Relevant legislation

BEA — section 34 (4).
 UCC — section 3-204.
 ULB — article 14.

Cross references

Holder: article 14.
 Endorsement: article 13.
 Transfer: article 12.

Commentary

If the last endorsement on an instrument is in blank and the holder transfers the instrument, several situations may arise which in various ways determine whether the transferor is liable on the instrument, as shown by the following examples.

Example A. The holder A delivers the instrument to B. This is a proper transfer (cf. article 12 (b)) and B is a holder under article 14 (1) (b). A is not liable on the instrument because he has not signed it (cf. article 29). However, he may be liable off the instrument under article 41. The instrument remains an instrument payable to bearer.

Example B. A, the holder, delivers the instrument to B after endorsing it in blank. This is a proper transfer under article 12 (b) and B is a holder. A is liable on his signature as an endorser. It may be noted that A's signature is not required for the purpose of transferring the instrument to B (the instrument is a bearer instrument by reason of the blank endorsement). The effect of A's blank endorsement is to render A liable on the instrument and this may be commercially expedient.

Example C. A, the holder, delivers the instrument to B after having converted the blank endorsement into a special endorsement (by indicating in that endorsement that the instrument is payable to B). This is a proper transfer under article 12 (a) and B is a holder. A is not liable on the instrument because he has not signed it (cf. article 29). The conversion of a blank endorsement into a special endorsement is authorized under article 15 (b) and is therefore not a material alteration under article 31.

Article 16

When the drawer or the maker has inserted in the instrument, or an endorser in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the transferee does not become a holder except for purposes of collection.

Relevant legislation

BEA — sections 8 (1) and 35.
 UCC — sections 3-205, 3-206 and 3-805.
 ULB — articles 11 and 15.

Cross references

Holder: article 14.
 Endorsement: article 13.
 Transfer: article 12.
 Collection: article 20.

Commentary

1. Under article 16 the transfer of an instrument in accordance with article 12 may be excluded or limited by the drawer, the maker or an endorser by using such words as "not negotiable", "not transferable" or words of similar import. The drawer or maker must insert these words in the instrument, and the endorser would have to insert them in his endorsement.

2. The purpose of such insertion is to ensure that payment of the instrument may only be claimed by the

payee or the endorsee or the agent for collection, as the case may be. This insertion does not affect the character of the instrument as a bill or note but the endorsee does not become a holder except for purposes of collection. He may not further transfer the instrument, not even for purposes of collection; he would have this latter power only if the endorsement to him would have been made expressly for purposes of collection (cf. article 20).

3. Under article 1 (2) and (3) of this Convention an instrument need not be made payable to "the order" of the payee. Therefore, a mere omission of the words "to order" does not prevent further transfer, and where an instrument lacking that expression is transferred by the payee in accordance with article 12 the transferee is a holder and may in turn further transfer the instrument.

Article 17

(1) An endorsement must be unconditional.

(2) A conditional endorsement transfers the instrument whether or not the condition is fulfilled.

Relevant legislation

BEA — section 33.
UCC — section 3-202.
ULB — article 12.

Cross references

Transfer: article 12.
Endorsement: article 13.

Commentary

1. Article 17 expresses the fundamental policy of the Convention that an endorsement may not be made subject to a condition (paragraph (1)).

2. If an endorsement contains a condition the endorsement is a valid endorsement for purposes of transferring the instrument and the transferee is a holder whether or not the condition has been fulfilled. Furthermore the condition to the extent that it affects the liability of the endorser is to be disregarded. However, the fact that a condition was not fulfilled is not necessarily irrelevant. It may, for example, form the basis of a claim or defence under article 25 if the condition relates to the underlying transaction. For that reason, the same result would obtain if the condition had not been included in the endorsement but was only expressed in the agreement of the underlying transaction.

3. It should be noted that article 17 deals only with conditions in the proper sense of the term, i.e. making the liability of the endorser dependent upon the occurrence or non-occurrence of an uncertain future event. Thus, the article does not cover other ways of excluding or limiting the liability as, for example, where an instrument is endorsed partially (article 18) or without recourse (article 40 (2)).

Article 18

An endorsement in respect of a part of the sum due under the instrument is ineffective as an endorsement.

Relevant legislation

BEA — section 32 (2).
UCC — section 3-202 (3).
ULB — article 12.

Cross references

Endorsement: article 13.
Sum payable: article 6.

Commentary

1. This article provides that an endorsement must be of the entire instrument; therefore, a partial endorsement is not effective as an endorsement. An endorsement is partial if, for example, it states "pay one half of the sum due to A" or "pay half of the sum due to A and half to B". However, an endorsement is not partial if, for example, it states "pay A and B" or "pay A or B" since the full sum due is then payable to the person(s) indicated. A special problem arises when an instrument has been paid in part. If in such a case an endorsement is limited to the part unpaid, it is "partial" in the sense of article 18 and therefore ineffective. If however the endorsement is not so qualified, it is a valid endorsement although in fact it is only for part of the sum, namely for the amount unpaid.

2. The "transferee" of an instrument endorsed as to part of the sum payable does not qualify as a holder since the endorsement is ineffective. However, article 18 does not prevent such person from acquiring rights under the partial endorsement under the applicable domestic law (e.g. by "partial" assignment).

Article 19

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the instrument.

Relevant legislation

BEA — section 32 (5).
UCC — section 3-414 (2).

Cross reference

Endorsement: article 13.

Commentary

The purpose of this article is to establish a presumption of fact as to the chronological order in which two or more endorsements were made. The article thereby establishes a presumption of rank for the purpose of the right of recourse by an endorser who paid the instrument against

prior endorsers. The article is also relevant for determining to what extent the discharge of one endorser discharges subsequent endorsers. Extrinsic evidence may be brought to rebut the presumption of fact and to prove the true order of endorsements.

Example. An instrument shows blank endorsements in the following order: (signed) payee; (signed) A; (signed) B. Upon dishonour of the instrument the holder C exercises his right of recourse against A. Payment by A discharges B. However, if A proves that he endorsed after B had endorsed, the presumption is rebutted. In such a case B is not discharged and A, upon payment, has a right of recourse against B.

Article 20

(1) When an endorsement contains the words "for collection", "for deposit", "value in collection", "by procuration", "pay any bank", or words of similar import, authorizing the endorsee to collect the instrument (endorsement for collection), the endorsee:

- (a) May only endorse the instrument for purposes of collection;
 - (b) May exercise all the rights arising out of the instrument;
 - (c) Is subject to all claims and defences which may be set up against the endorser.
- (2) The endorser for collection is not liable upon the instrument to any subsequent holder.

Relevant legislation

BEA – section 35.
UCC – sections 3-205 and 3-206.
ULB – article 18.

Cross references

Endorsement: article 13.
Claims and defences: article 25.

Commentary

1. A holder, in order to obtain payment, would normally present the instrument himself to the person liable. However, particularly in the international context, he will engage an agent (usually a bank) to do so on his behalf.

2. For that purpose, he may, for example, use the means of a regular endorsement, whether blank or special, accompanied by collecting instructions outside the instrument. He may, however, prefer an endorsement for collection as provided for in article 20 which would avoid certain risks inherent in the first approach. These risks arise from the fact that the agent for collection may disregard his instructions and further endorse the instrument to a person who may not know about the collection instructions and may thus qualify as a protected holder and exercise rights

of a protected holder against the endorser whose endorsement was intended only for collection purposes. These risks cannot materialize where an endorsement for collection is made in accordance with article 20.

Example A. The payee endorses the bill "for collection" to A. Fraudulently and without the permission of the payee the bill is sold (and endorsed in blank) by A to B. The acceptor refuses payment, and B brings an action against the payee. By virtue of paragraph (2) the payee is not liable to B. In that respect an endorsement for collection resembles an endorsement "without recourse" (see article 40 (2)).

3. Since the endorsee for collection acquires his rights through an endorsement, he is a holder if he is in possession of the instrument. Thus, he may exercise the rights, and is subject to the duties, of a holder.

Example B. By fraud the payee induces the drawer to draw a bill payable to the payee. The payee endorses the bill "for collection" to A. A brings an action on the bill against the drawer. By virtue of paragraph (1) (b) the drawer, since he may raise the defence of fraud against the payee, may raise it also against the payee's endorsee for collection.

4. However, the legal position of a holder under an endorsement for collection differs from that of a "normal" holder since the endorsee for collection acts as an agent of the endorser. The difference manifests itself in the following rules expressed in article 20:

(a) The endorsee for collection may not further endorse the instrument for any purpose other than for collection. Any subsequent endorsee will also be an agent for collection. This result obtains even though the subsequent endorsement is not made expressly for collection since the first endorsement controls.

(b) The endorsee for collection may exercise rights against any party who is liable to the endorser for collection, including the right to bring an action on the instrument. The endorsee for collection has no rights on the instrument against the endorser for collection since the purpose of the endorsement is to collect the instrument for the endorser and not from him. In this respect, an endorsement for collection is an endorsement that excludes the liability of the endorser and is thus similar to an express stipulation provided for in article 40 (2).

(c) The endorsee for collection cannot be a protected holder in his own right. However, if the endorser for collection is a protected holder, the transfer of the instrument to the agent for collection vests in him the rights on and to the instrument which the protected holder had (article 27). It follows that the endorsee for collection is subject only to those claims and defences which may be set up against the endorser.

5. It should be noted that the Convention does not deal with the legal relations between endorser and endorsee for collection outside the instrument, e.g. the circumstances

under which the underlying agency relationship is terminated. However, such termination may form the basis of a claim by the endorser for collection which, if asserted, may be set up as a defence against the holder (i.e. the ex-agent, see article 25 (3)) or may lead to the result that payment to the holder does not discharge the payer (cf. article 68 (3)).

Article 21

The holder of an instrument may transfer it to a prior party or the drawee in accordance with article 12; nevertheless, in the case where the transferee was a prior holder of the instrument, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

Relevant legislation

BEA — sections 37 and 59 (2) (b).
UCC — section 3-208.
ULB — article 50.

Cross references

Transfer: article 22.
Holder: articles 4 (6) and 14.

Commentary

1. An instrument may be transferred to a prior party (an endorser, the drawer, the acceptor or the maker) or to the drawee. If the prior party was a holder no endorsement is necessary. Therefore, transfer of the instrument to the drawer (i.e. transfer within the meaning of article 12) requires an endorsement unless the last endorsement is in blank. A prior party who is a holder may further transfer the instrument.

2. Article 21 also provides that a prior holder who acquires the instrument without an endorsement may strike out any endorsement which would prevent him from being a holder. Such striking out is not a material alteration.

Example. The payee endorses the instrument to A. A endorses to B. B endorses to C. C delivers the instrument to A upon payment by A. A may strike out his own endorsement to B and the endorsement of B to C.

Article 22

An instrument may be transferred in accordance with article 12 after maturity, except by the drawee, the acceptor or the maker.

Relevant legislation

BEA — section 36.
UCC — section 3-304 (3).
ULB — article 20.

Cross reference

Transfer: article 12.

Commentary

An instrument may be transferred before, at or after maturity, whether or not the instrument was dishonoured or protest made. However, if the instrument was transferred to the drawee, the acceptor or the maker it cannot be transferred by either of them after maturity.

Example. The drawee pays a bill on which the last endorsement is in blank. After maturity he delivers the bill to A. This is not a transfer under article 12 and A is not a holder.

Article 23

(1) If an endorsement is forged, any party has against the forger, and against the person to whom the instrument was directly transferred by the forger, the right to recover compensation for any damages that he may have suffered because of the forgery.

(2) The liability of a party or of the drawee who pays, or of an endorsee for collection who collects, an instrument on which there is a forged endorsement is not regulated by this Convention.

(3) For the purposes of this article, an endorsement placed on an instrument by a person in a representative capacity without authority or exceeding his authority has the same effects as a forged endorsement.

Relevant legislation

BEA — sections 24 and 59.
UCC — sections 3-404, 3-405 and 3-603.
ULB — articles 16 and 40.

Cross references

Forged signature: article 4 (10).
Transfer: article 12.
Endorsement for collection: article 20.
Endorsement by a person in a representative capacity: article 32.

Commentary

1. Where an endorsement on a bill of exchange or promissory note has been forged, one of the parties must bear the risk of loss. The problem of who should bear that risk is solved in a fundamentally different way in the common and civil law systems. The reasons for this divergence in approach are based on a different appreciation of what is commercially expedient and what policy considerations should prevail, even though the rationalization of certain aspects of the rule may have occurred after its formulation. While there are other issues of negotiable instruments law where the two systems are in sharp contrast, the rule on forged endorse-

ments can be said to present the most striking conflict between them.

2. The BEA, the UCC and the ULB all recognize the basic principle that a person whose signature is forged on an instrument is not liable thereon (BEA section 24; UCC section 3-404 (1); ULB article 7) and that the person who forges the signature of another person is liable on the instrument as if he had signed his own name. The basic point on which the two systems differ is the effect of the transfer of an instrument bearing a forged endorsement. Who is the owner of the instrument? What are the rights and liabilities of the various parties to the instrument and of the drawee who pays on a forged endorsement and the person whose endorsement was forged?

THE EXISTING LEGAL SYSTEMS

Anglo-American Law

3. Under the common law statutes a forged endorsement, subject to certain exceptions, is wholly inoperative "as that of the person whose name is signed" (UCC section 3-404 (1)) and "no right to retain the bill or to give discharge therefor or to enforce payment thereof against any party thereto can be acquired through or under that signature" (BEA section 24).

4. The effects of this basic rule are several. Since an order instrument is negotiated by delivery with any necessary endorsement and a forged signature is inoperative as an endorsement, without such negotiation the transferee does not become a holder. The same is true for any subsequent transferee, whether or not he acts in good faith. Because the endorsement is inoperative, it cannot make the instrument payable to bearer either. Possession of the instrument does not confer title to it nor the right to enforce it against parties who signed it prior to the forged endorsement. In respect of persons transferring the instrument subsequent to the forged endorsement, the UCC provides that such transferor, who receives consideration, "warrants to his transferee and if the transfer is by indorsement to any subsequent holder who takes the instrument in good faith that (a) he has a good title to the instrument or is authorized to obtain payment or acceptance on behalf of one who has a good title and the transfer is otherwise rightful; and (b) all signatures are genuine or authorized" (section 3-417 (2) (a) and (b)). A warranty of title runs also to a good faith payer or acceptor (section 3-417 (1) (a)). The BEA provides in this respect that an endorser is estopped from raising against subsequent transferees the fact that an endorsement was forged (section 55 (2) (c)). In the case of a bearer bill or note any person who negotiates it warrants to his immediate transferee for value that there are no prior forged endorsements (section 58 (3)).

5. Payment on a forged endorsement does not discharge the drawee's debt to the drawer since payment is not to the

holder. According to the BEA such payment does not qualify as payment in due course to the holder. As a result the drawer is entitled to demand that the drawee reverse the charge by recrediting his account. An exception to this rule is found in section 60 of the BEA in respect of bills drawn on a banker and payable to order on demand. If a banker pays such a bill in good faith and in the ordinary course of business it is not incumbent on him to show that any endorsement on the instrument was made by or under the authority of the person whose endorsement it purports to be; and he is deemed to have paid the bill in due course although the endorsement has been forged or made without authority. Under the UCC an instrument bearing a forged endorsement is not "properly payable" (section 4-401 (1)) and since the payee or the endorsee whose endorsement was forged has not signed, the drawee who pays does so without instructions and in violation of the drawer's order.

6. The payee or the endorsee whose signature is forged retains title to the instrument and the instrument remains payable to him. He may exercise his rights to it by an action for conversion outside the instrument or by an action on the instrument under the provisions of lost instruments. Thus if the drawee pays to someone else and receives the instrument he is liable for conversion to such payee or endorsee on an action in tort outside the instrument and the drawer may still be liable on the instrument to such payee or endorsee.

7. The drawee who paid the instrument in good faith may recover from the person paid. Under English common law, he may claim on the ground that money paid through a mistake of fact is recoverable. Under the UCC he may shift the loss to the person who received payment by a claim for breach of warranty of title (section 3-417 (1)(a)).

The Geneva Uniform Law

8. The approach of the ULB is fundamentally different from that of the common law. According to article 16 of that Law the person who is in possession of an instrument and establishes his title to it through an uninterrupted series of endorsements is considered to be the lawful holder (*porteur légitime*). These two conditions establish what is often referred to by civil law authors as *légitimation formelle*, a term for which there is no correct equivalent in the English language. They establish a presumption that the possessor of an instrument on which there appears an uninterrupted chain of endorsements has title to it and, as such, is entitled to exercise all rights derived therefrom. The presumption is rebuttable: the true owner may claim the instrument but will succeed only if he proves that the holder, though the conditions set forth in article 16 of the ULB may be met, acquired it in bad faith or in acquiring it has been guilty of gross negligence. In the context of forged endorsements this means that the status of lawful holder which article 16 bestows upon the possessor is not available if the possessor was aware or should have been aware that the endorser was

not the true owner of the instrument and that the endorsement was forged or made by an agent without authority.

9. Therefore, under the ULB a forged endorsement is, with respect to the rights of the taker from the forger, a valid endorsement provided that the taker meets the conditions set forth in article 16. It is also a valid endorsement with respect to the rights of subsequent endorsees even if they knew about the earlier forgery. The dispossessed owner may claim the instrument from the person who took it from the forger, but if such person is a lawful holder the dispossessed owner will succeed only if he proves bad faith or gross negligence. Since a lawful holder, in the absence of bad faith or gross negligence, is not bound to give up the instrument he may exercise the rights on the instrument. Parties to the instrument, whether they signed before or after the forgery, are liable to the lawful holder.

10. The presumption which article 16 establishes is also relevant in the context of discharge of the debtor who pays an instrument: he may act in reliance on the apparent title. According to article 40 of the ULB, payment to the possessor of an instrument who qualifies as a lawful holder under article 16 discharges the payer. The drawee need not investigate whether the person presenting the instrument for payment is the true owner and whether the signatures of the endorsers appearing on it are genuine. But there are some important exceptions to the rule. It does not apply if the drawee pays before maturity, in which case he pays at his own risk and peril (ULB article 40). Thus, the drawee cannot debit the account of the drawer if he paid before maturity to a holder who, although there is formal *légitimation* under article 16, is not the true owner even if there was absence of bad faith and gross negligence on the part of the holder when acquiring the instrument. He would be liable to pay a second time. Nor can the drawee debit the account of the drawer if, though paying at maturity, he has been guilty of "fraud or gross negligence". It is to be noted that the language of article 40 differs from that of article 16, where the status of lawful holder is denied to the possessor if he acquired the instrument in "bad faith" or with "gross negligence".

Who bears the risk of a forged endorsement?

11. The basic difference, in terms of bearing the risk of a forged endorsement, between the ULB and the BEA and UCC approach is the following: according to the ULB the risk of the forged endorsement rests upon the owner of the bill from whom it was stolen, whilst according to the BEA and the UCC the risk rests upon the person who took the bill from the forger. The different results under the two main systems are shown by the following two examples:

Example A. The drawer issues a bill to the payee (P). T steals the bill from P. The thief (T) forges P's signature and "endorses" the bill to A who takes it without knowledge of the theft and forgery. A endorses it to B who takes it without knowledge of the theft and forgery. B

receives payment from the drawee who pays without knowledge. The drawee debits the drawer's account.

Under the ULB, the payment by the drawee operates as a discharge of his debt to the drawer, and the drawee is entitled to debit the drawer's account (i.e., the risk is not upon the drawee). As the bill is paid to the person entitled to payment, the drawer discharges his obligation to the payee (i.e., the risk is not upon the drawer). The risk of forgery rests, therefore, according to the ULB, on the payee, the last owner before the forgery, who lost possession of the bill.

Under the BEA and UCC, payment by the drawee does not discharge his debt to the drawer. When the forgery is discovered, the drawee who paid must credit the account of the drawer. (As a result, the risk does not remain upon the drawer; on the other hand the drawer does not gain from the forgery since he is still liable on the bill to the payee). The drawee is entitled to recoup his loss, by shifting it to B, who in turn will shift it to A (i.e., the risk is not upon the drawee or the person paid by him). A cannot shift the risk back. He will bear it. Consequently, under the BEA and UCC the risk falls on the person who took the bill from the forger.

Example B. The drawer sends a bill by post to the payee (P). Before the bill reaches the payee, T steals it from the post. T forges P's signature and "endorses" the bill to A who takes it without knowledge of the theft or forgery. A endorses it to B who takes it without knowledge. B receives payment from the drawee; the drawee's payment is without knowledge. The drawee debits the drawer's account.

Under the ULB, the drawee is discharged (i.e., the risk is not upon the drawee). The drawee is thus entitled to debit the drawer's account. The drawer has not paid the payee since the bill has not reached the payee. It follows that the risk of the forgery is on the drawer, the owner of the bill from whom it was stolen and whose account was debited.

Under the BEA and UCC the drawee is not discharged. He is not entitled to debit the drawer's account with him, and he must reverse it (i.e., the risk is not upon the drawer; the drawer has not gained since he is still liable to the payee under the obligation for which the bill was drawn). The drawee is entitled to recoup his loss by shifting it to B who in turn will shift it to A (i.e., the risk is not upon the drawee or the person paid). A suffers the loss since he presumably gave goods or services to the forger without receiving payment. Thus the loss ultimately falls on the person who took the bill from the forger.

The advantages and disadvantages of the two approaches to forgery

12. The main advantages of the ULB, as compared to the BEA and UCC are said to be the following:

(a) The ULB promotes circulation and consequently easy financing of transactions by bills or notes, since any possessor without knowledge is assured that a previous forged endorsement has no effect on his rights to and upon the bill or note. Under the BEA and UCC, on the other hand, a person without knowledge may be hesitant in taking a bill or note since he may have no right to or upon the bill or the note if there is a previous forged endorsement;

(b) The ULB rule gives greater finality of payment. If a bill is given in payment of a debt the payment will be final once the bill is paid by the drawee and it is no longer necessary to inquire whether the transferor or the transferee had rights to or upon the bill. In that respect payment by way of a bill resembles payment by way of money. Under the ULB once the drawee paid the bill without fraud or gross negligence on his part, and provided the bill shows a regular series of endorsements, the payment is final. The relations between the drawer and the drawee, the payee and the drawer (if the bill was stolen from the payee), and the endorsees among themselves, are settled promptly and with finality. On the other hand, under the BEA and UCC, the transactions must be reopened;

(c) The ULB rule provides economy of remedies. Pursuant to the ULB, when the drawee pays and debits the drawer's account, the risk of the forgery is automatically imposed on the party who should, under the ULB, bear the risk (i.e., the last owner before the forgery). There is no need for any action or litigation in order to impose the risk on such party. On the other hand, according to the BEA and UCC, a series of actions or remedies may be necessary to transfer the loss to the one ultimately responsible (i.e., the person who took from the forger). One may envisage several actions (and therefore possible disputes) before the risk rests on the taker from the forger. The first is the recrediting of the drawer's account; the second is the recouping by the drawee of the money paid; the third is the claim by the person paid against previous endorsees; the fourth is the action between the true owner and the drawer; the fifth is the action between the true owner and the drawee or subsequent endorser. Not all of those actions will actually take place and some of them are in the alternative, but there is an inherent risk of multiplicity of actions and remedies.

13. The main advantages of the approach of the BEA and UCC, as compared to the ULB, are the following:

(a) It encourages the use of a bill or a note by the drawer as a means of payment or credit, since the drawer is assured that he will not bear the risk of any forgery of an endorsement. Especially, it encourages the use of the mail as a means to transfer bills or notes from the drawer to the drawee. Under the ULB, on the other hand, the potential drawer of a bill or the maker of a note may

be hesitant to issue the bill or note and to send it by post, since he may bear the risk if the bill or the note is stolen from the post before it reaches the payee;

(b) The BEA-UCC approach puts the risk of forgery on the person who dealt with the forger. That party ought to bear the risk since he can most easily prevent it. The endorsee should know his endorser. He should not take the bill or the note from a stranger. The ULB, on the other hand, imposes the risk of forgery on the owner of the bill or the note, who under normal and efficient procedures for handling bills or notes (including the use of mail) cannot prevent theft and forgery of the bill.

14. It is to be noted that the above-mentioned advantages that are said to be inherent in one or the other system do not appear, in actual practice, to be absolute. For instance, the principal reason advanced during the 1930 international conference in favour of articles 16 and 40 of the ULB was that only by protecting the possessor of a bill who took it in good faith would the bill be susceptible of easy circulation and that circulation would be impeded if one would oblige the endorsee or the drawee to verify the signature of all preceding endorsees who would be mostly unknown to him. However there is no proof that the common law rule has in any way impeded circulation or that bills subject to the rules of common law jurisdictions are in practice less negotiable. Nor, it would appear, has the alleged disadvantage of the ULB rule – that it discourages the use of a bill by the drawer because he bears the risk of the forgery of an endorsement – led to a decrease in the issuance of bills in countries operating under the ULB system. If bills are used to a lesser degree, the cause is probably that other methods of credit and payment have come to be preferred. The other objection that the ULB rule encourages laxity in bill transactions because there is little risk in buying a bill from a stranger, while the common law rule prevents this by imposing the risk on the purchaser, appears to be refuted by the near-absence of forged endorsements on bills in civil law countries.

15. There are other rationalizations of the rules on forged endorsements that concern their procedural effects. It is certainly true that the ULB achieves finality of payment in that, once the bill is paid by the drawee under the conditions laid down by article 40 of that Law, the drawee may debit the account of the drawer and his relations with the drawer are settled. But it is at least arguable whether this is the most appropriate solution and whether it is not preferable to protect the interests of the drawer by accepting the inconvenience of reopening the transaction.

16. It would thus appear that the so-called advantages of each legal system cannot provide absolute criteria for the formulation of new uniform rules.

Article 23 of the Convention

17. Article 23 attempts to bridge the basic differences between the common law rules and those of the ULB. The legal effects of this article and of article 14 are the following:

(a) A forged endorsement or an endorsement signed without authority is effective as an endorsement if it is part of an uninterrupted series of endorsements;

(b) Any party who suffered damages because of the forgery has a right for damages against the forger and against the person to whom the forger directly transferred the instrument.

18. As a result:

(a) The person who acquired the instrument through an uninterrupted series of endorsements is a holder even if one or more endorsements were forged. As a holder he has all the rights conferred on him by the Convention;

(b) The person who ultimately bears the risk of loss is the forger or, if he cannot be found or is insolvent, the person who took the instrument from the forger.

Example C. The drawer issues a bill to the payee (P) who receives it. T steals the bill from P. T forges P's signature and "endorses" the bill to A who takes it without knowledge of the forgery. B receives payment from the drawee. The drawee debits the drawer's account. Who bears the risk?

Payment by the drawee effects a discharge of his debt to the drawer (consequently the risk is not on the drawee). Since the bill was paid to the person entitled to payment the drawer discharges his obligation to the payee (consequently the risk is not on the drawer). The payee who lost his rights to and upon the bill is entitled to compensation from T and A for such loss. If T cannot be found or is insolvent A cannot shift the risk to anyone else. Therefore, the risk of the forgery rests on A who took the bill from the forger.

Example D. The drawer sends a bill by post to the payee (P). Before the bill reaches P it is stolen from the post. The thief forges P's signature and "endorses" the bill to A who takes it without knowledge of the forgery. A endorses the bill to B who takes it without knowledge of the forgery. B receives payment from the drawee. The drawee debits the drawer's account. Who bears the risk?

According to article 23 payment by the drawee entitles him to debit the drawer's account. The drawer — who still is liable on his underlying obligation to the payee — has lost ownership of the bill but has a right for compensation against T and A. If T cannot be found or is insolvent A cannot shift the risk to anyone else. Therefore, the risk of the forgery rests on A as the person who took the bill from the forger.

Rationale

19. As pointed out above, each solution to the "forged endorsement" problem, whether under the BEA, the UCC or the ULB, has its advantages and disadvantages. Theoretically, the best solution would be one which embodies all the advantages of these systems, without being subject to their disadvantages. This cannot be done since any "positive" aspect of an optimum solution is of necessity accompanied by a "negative" aspect. As has been noted, the elements of an optimum solution include: (a) finality of payment; (b) economy of remedies; (c) allocation of the risk of forgery to the person best able to guard against the risk; (d) encouragement of the use of bills and notes as payment, credit or security instruments. Article 23 offers a compromise solution; it attempts to embody the principal advantages of the existing legal systems, whilst avoiding or minimizing their main disadvantages.

20. *Finality of payment.* Under article 23 that advantage is substantially achieved; payment by the drawee is final. The legal relations between the drawee and the drawer, the payee and the drawer, the endorsee between themselves, the drawee and the person receiving payment are settled in a final way. The only "non-final" element is the rule that enables the person from whom the instrument was stolen to recover damages from the person who acquired the instrument from the forger.

21. *Economy of remedies.* Payment by a drawee effects a discharge of his obligation to the drawer; the drawee may debit the drawer's account. There is no occasion for further action between them. It follows that there is no need for further action between the drawee and the person receiving payment, or between him and previous endorsers. The person whose signature is forged (payee or endorsee) loses his right to act upon the instrument, and therefore there is no need for further action by him against the drawer, maker, drawee or any subsequent endorsee. All these potential actions are replaced by a single right of action of the owner of the instrument against the forger and the person who acquired the bill from the forger.

22. *The risk of forgery should be borne by the person who is best able to prevent the forgery.* It is the person who acquired the instrument from the forger who can best prevent the circulation of the instrument containing the forged endorsement. The endorsee should know his endorser. He should not take the instrument from a stranger. Article 23 encourages this by giving the owner a right of action against the person who took from the forger.

Paragraph (1)

23. The basic rule that a person to whom an instrument is transferred through an uninterrupted series of endorsements is a holder, even if any of the endorsements was forged or was signed by an agent without authority, follows

from article 14 (1) (b). This rule underlies the provision of paragraph (1). Consequently paragraph (1) does not apply to the case of a stolen bearer instrument.

24. Nothing in article 23 affects the rule that a forged signature does not impose any liability on the person whose signature was forged (cf. article 30). However there are cases in which such a person will nevertheless be liable (cf. article 30). In such cases paragraph (1) does not apply by reason of the fact that the person whose signature was forged is considered to be bound by it.

25. The liability of the forger and of the person to whom the instrument was directly transferred by the forger is a liability off the instrument. Paragraph (1) merely confers a statutory right for compensation upon the party who suffered damages because of a forged endorsement. Questions pertaining to the amount of damages, limitation of action for damages etc. are left to the applicable national law.

26. Article 23 confers a right for compensation on any party who suffered damages because of the forgery. That right is therefore not limited to the person whose endorsement was forged. Thus the drawer of a bill which was stolen from the post on its way to the payee may exercise the right if he suffered damages because of the forgery of the payee's signature.

27. The right to recover compensation may be exercised only against the forger and the immediate transferee of the forger. Thus if T forges the signature of the payee, transfers the instrument to A and A transfers to B, the payee who suffered damages because of his forged endorsement may not recover damages under article 23 (1) from B, even if B knew about the forgery.

Paragraph (2)

28. Under article 23, the right to recover compensation for damages suffered because of a forged endorsement is given against the forger and against the "person to whom the instrument was directly transferred by the forger". The rationale for the rule that the right to recover compensation may be exercised against the person to whom the instrument was directly transferred by the forger, by endorsement and delivery or by delivery alone if the last endorsement was in blank, is that the transferee should know the person who so transfers the instrument to him. Therefore, such transferee is liable for damages that any party may suffer because of a forged endorsement. Paragraph (2) makes clear that the Convention makes no rule in respect of the liability of a party or the drawee to whom the instrument is transferred consequent upon payment of it by him.

29. Paragraph (2) further lays down that the Convention does not deal with the liability of a person (usually a bank) to whom the forger has endorsed an instrument for collection and to whom it is subsequently paid.

Paragraph (3)

30. Paragraph (3) extends the rule laid down in paragraph (1) in respect of a forged endorsement to an endorsement made by an agent without authority or exceeding his authority.

CHAPTER FOUR. RIGHTS AND LIABILITIES

Section 1. The rights of a holder and of a protected holder

Article 24

(1) The holder of an instrument has all the rights conferred on him by this Convention against the parties to the instrument.

(2) The holder is entitled to transfer the instrument in accordance with article 12.

Relevant legislation

BEA — section 38.

UCC — sections 3-301 and 3-306.

ULB — article 16 and 17.

Cross references

Holder: articles 4 (6) and 14.

Party: article 4 (8).

Transfer: article 12.

Commentary

1. Article 24 is the introductory article to the articles governing the rights of a holder and of a protected holder. In order to exercise the rights on an instrument under this Convention a person must, as a general rule, be a holder. Special rules obtain if a holder is not in possession of the instrument because it is lost (see articles 74 to 79). As to the duties of a holder see Chapter Five of this Convention.

2. An instrument may be transferred only by a holder. If the transfer is in accordance with the provisions of article 12 the transferee is a holder.

Article 25

(1) A party may set up against a holder who is not a protected holder:

(a) Any defence available under this Convention;

(b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

(c) Any defence to contractual liability based on a transaction between himself and the holder;

(d) Any defence based on incapacity of such party to incur liability on the instrument or on the fact that such

party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a holder who is not a protected holder are subject to any valid claim to the instrument on the part of any person.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

(a) Such third person asserted a valid claim to the instrument; or

(b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft.

Relevant legislation

BEA – sections 36 (2) and (6), and 38 (2).

UCC – section 3-306.

ULB – articles 7, 16 and 17.

Cross references

Holder: articles 4 (6) and 14.

Protected holder: articles 4 (7) and 26.

Commentary

1. A person who signs an instrument (a “party”) is liable to the holder of it. The Convention makes a distinction between a “holder” and a “protected holder”. Article 25 deals with the rights of a holder who is not a protected holder.

2. The distinction between a holder and a protected holder is relevant only if the party liable on the instrument can set up a defence to his liability or has a claim to the instrument. If a holder is not a protected holder he is subject to any claim or defence of any party. As to the question whether payment by a party to a holder who is not a protected holder discharges that party, see Chapter Six.

Paragraph (1) (a)

3. The Convention sets forth various defences which a party may raise against the holder. Some of them may also be raised against a protected holder (see article 26 (1) (a) and commentary).

4. The following are examples of defences which may be set up against a holder.

Example A. The drawee of a bill refuses to pay it upon due presentment. The holder fails to protest the bill. Therefore the payee is not liable on the bill and, if recourse is exercised against him, may raise the defence of absence of liability consequent upon lack of due protest.

Example B. The drawer stipulates on the bill that it be presented for acceptance. The bill is not presented for acceptance and the holder, upon dishonour by non-payment, demands payment from the drawer. Under article 49 the drawer may raise as a defence the fact that his liability was conditional upon due presentment for acceptance.

Example C. The payee of a note payable on demand presents it for payment to the maker. The maker pays the note but does not request that it be handed over to him. Subsequently, the payee endorses the note to A who is not a protected holder. The maker may set up against A the defence of discharge because of payment (cf. article 68).

Paragraph (1) (b)

5. In addition to defences that are derived from the provisions of the Convention there are the defences, referred to in paragraph (1) (b), that are based on an underlying transaction or that arise “from the circumstances as a result of which [a person] became a party”. This type of defence may be illustrated by the following examples:

Example D. Pursuant to a contract of sale the buyer (drawer) issues a bill made payable to the seller (payee). The seller fails to deliver the goods under the sales contract and endorses the bill to A who is not a protected holder (for instance because A when taking the bill had knowledge of seller's failure to deliver and, consequently, of buyer's defence on the bill against seller; cf. article 4 (7) (a)). The drawer may set up the defence of non-delivery in an action on the bill by A, even though A is a person with whom the drawer has not dealt.

Example E. The payee by fraud induces the maker to make a note payable to the payee. The payee endorses the note to A who is not a protected holder. A brings an action on the note against the maker. The maker may raise against A the defence based on fraud as a result of which the maker became a party.

Paragraph (1) (c)

6. This subparagraph provides that a party may raise against a non-protected holder who is not a remote holder a defence to contractual liability that is based on a transaction between himself and such a holder.

Example F. A to whom the payee transferred the instrument brings an action on it against the payee. The payee may set up as a defence the fact that A has not delivered goods under a sales contract between himself and A.

Paragraph (1) (d)

7. This subparagraph sets forth two defences based on the fact that the party from whom payment is demanded was never liable on the instrument: he signed the instrument without capacity to incur liability on it or without know-

ledge that his signature made him a party to the instrument (the defence of *non est factum*).

8. The question whether a person has capacity to sign an instrument is left to national law. The defence of *non est factum* is available if the person signing is without knowledge of the fact that he signed an instrument and the absence of knowledge is not due to his being negligent.

Example G. X signs an instrument in the belief that it is a receipt. He does so without negligence. X is not liable on the instrument.

The defence on *non est factum* is not available if the person signing knows that he is signing an instrument but mistakenly erred as to its contents.

Paragraph (2)

9. Whereas a "defence" refers to a party's right to establish that he is free from liability on the instrument, a "claim" to an instrument refers to the assertion of a right to ownership or some other proprietary rights available under the applicable law. A holder who is not a protected holder is subject to such claims.

Example H. B obtains the instrument from A by fraud and transfers it to C who is not a protected holder because he knew about the fraud. A brings an action against C to recover possession of the instrument. A has a valid claim to the instrument against C.

Paragraph (3)

10. This paragraph deals with the so-called defence of *ius tertii*: a defence based on the claim of a third person and not on the absence of liability of the party from whom payment is demanded.

Example I. The drawer issues a bill made payable to the payee. By fraud A induces the payee to transfer the bill to him. A brings an action on the bill against the drawer. Pursuant to paragraph (3) only the drawer may raise the defence based on the fraud A practised on the payee if the payee asserts his claim to the bill.

The drawer may raise a defence based on *ius tertii* also if A acquired the instrument belonging to the payee by theft or if A had forged the signature of the payee or participated in the theft.

11. The main reasons for the rule set forth in paragraph (3) (a) are:

(a) The rule protects a party liable on the instrument since his liability will be discharged by his payment to the holder even if the party has knowledge of the claim of another person (cf. article 68 (3)).

(b) It is not proper to allow a party to raise a defence based on a claim which the person entitled to it does not

himself wish to raise. However, if such person asserts his claim the defence of *ius tertii* is available.

Thus, under article 68 (3), a party is not discharged of liability if, though knowing that a third person has asserted a valid claim to the instrument, he nevertheless pays it.

Article 26

(1) A party may not set up against a protected holder any defence except:

(a) Defences under articles 29 (1), 30, 31 (1), 32 (3), 49, 53 and 80 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;

(c) Defences based on the incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a protected holder are not subject to any claim to the instrument on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that person.

Relevant legislation

BEA — section 38.

UCC — sections 3-305 and 3-602.

ULB — articles 7, 16 and 17.

Cross reference

Protected holder: article 4 (7).

Commentary

1. As noted under article 4 (7), the main advantages of a negotiable instrument result from the strong legal position of a protected holder. He receives the instrument free from any defences of prior parties and free from claims to it by any person.

Example A. The payee by fraud induces the drawer to draw a bill payable to the payee. The payee transfers it to A, a protected holder. A demands payment from the drawer. Pursuant to paragraph (1) the drawer may not raise the defence of fraud against A.

Example B. The payee endorses the instrument in blank and mails it to A. It is stolen from the mail by X. X sells and delivers the instrument to B, a protected holder. The payee brings an action against B for recovery of the instrument

or its amount. Pursuant to paragraph (2) the claim of the payee to the instrument is not available against B.

Example C. The payee of a note payable on demand presents the note for payment to the maker. The maker pays the note but does not request that it be handed over to him. The payee subsequently endorses the note to A, a protected holder. The maker may not set up as a defence against A the fact that he is discharged of liability because of his having paid the note.

Example D. The payee endorses the bill to A and, off the bill, gives instructions to A to collect the bill for him. A in disregard of his instructions endorses the bill to B who is a protected holder. The payee may not set up against B the fact that the payee's endorsement was intended for purposes of collection only.

Example E. A demand bill is dishonoured by non-payment. The holder fails to protest the bill for dishonour and transfers it to A who is a protected holder. In an action on the bill by A against the drawer, the drawer may not raise the failure to protest as a defence to his liability.

2. The principal rule embodied in article 26, namely that the protected holder takes the instrument free from all defences and claims of any party, is subject to a number of important exceptions as provided in paragraph (1) (a), (b) and (c).

Paragraph (1) (a)

3. The protected holder does not take the instrument free from defences that are based on the provisions of the Convention listed in paragraph (1) (a). The defences are those based on the fact that the person from whom the protected holder demands payment has not signed the instrument (article 29 (1)); that that person's signature on the instrument was forged (article 30); that he signed the instrument before a material alteration of the instrument (article 31 (1)); that his signature was placed on the instrument in the conditions specified in article 32 (3); that the instrument which should have been presented for acceptance was not so presented (article 49); that the instrument was not duly presented for payment (article 53); and that a right of action on the instrument is prescribed under article 80.

Example F. The drawer draws a bill for 1,000 Swiss francs payable to the payee P. P fraudulently increases the amount of the bill to 2,000 Swiss francs and transfers it to A who is a protected holder. Upon dishonour of the bill by non-payment A brings an action on the bill against the drawer for the amount of the bill. The drawer may set up as a defence against A the fact that he signed the bill before the material alteration and is liable only for 1,000 Swiss francs (article 31 (1)).

Paragraph (1) (b)

4. The general rule that the protected holder takes the instrument free from defences and claims of prior parties

does not obtain if the defence is raised or the claim asserted by an immediate party.

Example G. A to whom the payee of a bill has transferred it is a protected holder. A delivers defective goods under a contract of sale between him and the payee in consideration of which the payee transferred the bill to A. Upon dishonour of the bill by the drawee A demands payment from the payee. The payee may raise as a defence the fact that A delivered defective goods. The payee may raise this defence because he and A are immediate parties. The defence could not be raised by the drawer since A is a protected holder and the transfer of the bill to A is not connected with an underlying transaction between the drawer and A.

5. Usually the holder of an instrument is not a protected holder if the transaction which led to the transfer of the instrument to him is defective in the sense that it entitles the transferor to a defence against his liability on the instrument. However, there may be cases where when the instrument was transferred the holder took it in good faith and the defect in the transaction occurred later.

Paragraph (1) (c)

6. Defences against liability obtaining under a simple contract cannot be raised against a protected holder (see example A above). However, the protected holder does not overcome defences based on the fact that the party signed the instrument without capacity or without knowledge that his signature made him a party to the instrument.

Example H. B asks A to sign a document as a witness. A, without negligence, signs what is in fact a bill. B transfers the bill to C, a protected holder. In an action on the bill by C against A, A has a valid defence.

Limitation or exclusion of liability

7. The rights of a protected holder on an instrument are determined by what is apparent *ex facie* the instrument. Therefore if a party has limited or excluded by a stipulation on the instrument the rights of a subsequent party or subsequent parties against him, as where an endorser has endorsed "without recourse" or has endorsed for collection or where a guarantor has guaranteed payment of only part of the sum payable, the protected holder cannot overcome such stipulation. Similarly where a party has paid part of the sum payable by the instrument – the instrument is then dishonoured by non-payment as to the amount unpaid (article 69 (3) (b)) – and such partial payment is stated on the instrument (article 69 (5)), the party who paid partially can successfully raise against a protected holder the fact that he is discharged of his liability on the instrument to the extent of the amount he paid.

Paragraph (2)

8. Whereas paragraph (1) dealt with defences against liability, paragraph (2) deals with a claim to the instru-

ment. The basic rule is that a protected holder is not subject to such claim (see example B). However, when a claim to the instrument arises in the circumstances in which a defence becomes available under paragraph (1) (b), the protected holder cannot overcome such claim. Thus, in example G above the payee has a claim to the instrument against A.

Article 27

(1) The transfer of an instrument by a protected holder vests in any subsequent holder the rights to and upon the instrument which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to, or a defence upon the instrument.

(2) If a party pays the instrument in accordance with article 66 and the instrument is transferred to him, such transfer does not vest in that party the rights to and upon the instrument which any previous protected holder had.

Relevant legislation

BEA — section 29 (3).

UCC — section 3-201.

Cross references

Transfer: article 12.

Holder: articles 4 (6) and 14.

Protected holder: article 4 (7).

Commentary

Paragraph (1)

1. According to article 27 a holder who is not a protected holder may nevertheless obtain the rights of a protected holder if the instrument is transferred to him by a protected holder. The purpose of this so-called "shelter rule" is to enable the protected holder to receive the full benefit of his protected status by being able freely to transfer the instrument. However, this rule is not intended, and should not be used, to permit any person who "participated in a transaction which gives rise to a claim to, or defence upon, the instrument" to wash the instrument clean by passing it into the hands of a protected holder. Consequently, under this paragraph, such a person is denied the benefit of the "shelter rule".

Example A. The payee by fraud induces the drawer to draw a bill payable to the payee (P). P endorses it to A who is a protected holder. A transfers the bill to B who knows that the bill was dishonoured. B brings an action against the drawer. Under article 27, the drawer is liable to B; the drawer has no defence against A since A is a protected holder. In the above facts the rights of A were transferred to B; therefore the drawer has no defence against B.

Example B. P and B by fraud induce the drawer to draw a bill payable to P. P endorses the bill to A who is a protected holder. A transfers the bill to B. B brings an action against the drawer. The drawer has a good defence. Though generally B acquires the same rights as A and A as a protected holder has a valid right against the drawer, article 27 (1) provides that this rule does not apply when the transferee was himself a party to the fraud.

However, it should be noted that the exception in article 27 (1) only applies where a person participated in the specified transaction and that mere knowledge is not sufficient. Thus if, in example B, B had not participated in the fraud, but only known about it, he would have had the rights of a protected holder.

Example C. In the fact situation described in example B, B transfers the bill to C who is not a protected holder in his own right because he knew about the participation of B in the fraud. Under article 27 (1) C acquires the same rights as A had and, thus, obtains the rights of a protected holder.

Paragraph (2)

2. The shelter rule applies irrespective of whether the subsequent holder to whom the instrument is transferred is a previous party to the instrument.

Example D. The payee P induces by fraud the drawer to draw a bill to P, which P transfers to A who knows about the fraud. A transfers to B who is a protected holder. B transfers to C and C to A. A acquires the rights of a protected holder according to article 27 (1) although as a previous party he was a holder against whom the drawer could have raised the defence of fraud.

However, a previous party may benefit from the shelter rule only if he obtains the instrument by transfer but not if he receives it against payment.

Article 28

Every holder is presumed to be a protected holder unless the contrary is proved.

Relevant legislation

BEA — section 30.

UCC — section 3-307 (3).

ULB — article 16.

Cross reference

Protected holder: article 4 (7).

Commentary

If a person is the holder of an instrument it is presumed that he is a protected holder. Therefore, if, in an action by the holder on the instrument against a party liable to him, such party brings a claim to the instrument or raises a defence against his liability, it is for the party bringing the

claim or raising the defence to prove that the holder is not a protected holder.

Section 2. *The liability of the parties*

A. GENERAL PROVISIONS

Article 29

(1) Subject to the provisions of articles 30 and 32, a person is not liable on an instrument unless he signs it.

(2) A person who signs an instrument in a name which is not his own is liable as if he had signed it in his own name.

Relevant legislation

BEA — section 23.

UCC — section 3-401.

Cross reference

Signature: article 4 (10).

Commentary

1. Article 29 embodies one of the basic principles of negotiable instruments law, namely that a person is liable on an instrument only if he signed it. Therefore, for example, the drawee is not liable on the instrument until he accepts it. Articles 30 to 32 set forth certain exceptions to this rule.

2. A person may have more than one name, e.g. a "private" name and a "business" or "trade" name. Paragraph (2) provides that the signature in any one of these names is sufficient to establish the signer's liability on the instrument. It is the fact of signing, not in which name is signed, that is the decisive factor. A person signing in a fictitious name is thus liable on the instrument he signed. It also follows from paragraph (2) that a person who forges the signature of another person is liable on the instrument as if he had signed in his own name.

Article 30

A forged signature on an instrument does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed the instrument himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own.

Relevant legislation

BEA — section 24.

UCC — sections 3-404 and 3-406.

Cross reference

Signature, forged signature: article 4 (10).

Commentary

1. In conformity with the generally prevailing rule that a person is not liable on an instrument unless he signs it (cf. article 29), article 30 provides that a forged signature (as defined in article 4 (10)) on an instrument does not impose liability on the person whose signature was forged, not even against a protected holder (cf. article 26 (1) (a)). However, article 30 sets forth two exceptions to this rule. Such person is liable if he accepts or adopts the forged signature as his own or if he represents, in writing or orally or by other conduct, that the forged signature is his own.

Example. The payee intends to endorse a bill to A. Before A takes the bill he asks the drawer whether the signature on the bill is his. The drawer mistakenly answers in the affirmative. It turns out that the drawer's signature was forged. Under article 30, the drawer is liable on the bill since he represented to A that the signature was his own.

2. For the purposes of this second exception, it is material whether the person to whom an affirmative representation is made knows of the forgery. If he does so, the person whose signature was forged is not liable since the rule on representation presupposes justified reliance on the representation.

3. It should be noted that the liability of persons other than the person whose signature was forged is not dealt with in article 30 but in other provisions (articles 23, 29).

Article 31

(1) If an instrument has been materially altered:

(a) Parties who have signed the instrument subsequent to the material alteration are liable thereon according to the terms of the altered text;

(b) Parties who have signed the instrument before the material alteration are liable thereon according to the terms of the original text. Nevertheless a party who has himself made, authorized, or assented to, the material alteration is liable on the instrument according to the terms of the altered text.

(2) Failing proof to the contrary, a signature is deemed to have been placed on the instrument after the material alteration.

(3) Any alteration is material which modifies the written undertaking on the instrument of any party in any respect.

Relevant legislation

BEA — sections 55 (2) (c) and 64.

UCC — sections 3-406 and 3-407.

ULB — article 69.

Cross reference

Signature: article 4 (10).

*Commentary***Paragraph (1)**

1. Article 31 deals with the material alteration of an instrument and not with forgery of the signature of a party, which is dealt with in article 30. It is irrelevant whether the material alteration is made by a party or a stranger.

2. The alteration does not discharge parties to the instrument of their liability. However, as to the extent to their liability it is relevant whether they signed before or after the alteration. A party who signs after the alteration is liable according to the terms of the altered text (subparagraph (a)). A party who signed before the alteration is liable according to the terms of the original text. The only exception to this rule is that such party is liable according to the terms of the altered text if he himself made, authorized, or assented to the alteration (subparagraph (b)).

Example. A bill which states the sum payable as X is accepted. The payee then raises the sum to Y and endorses the bill to A. A endorses the bill to B. By virtue of article 31, the acceptor is liable to B for X. If he dishonours the bill the drawer is liable to B for X. Pursuant to paragraph (1) (a) the payee and A are liable to B for Y.

3. The application of the above rules based on the time of the signature does not depend on whether the person claiming payment is with or without knowledge of the alteration or whether or not he is a protected holder. Thus, a party signing before the alteration is liable according to the original terms even if the holder had no knowledge of the alteration and even if he was a protected holder (cf. article 26 (1) (a)). Conversely, a party signing after the alteration is liable according to the altered terms even if the holder had knowledge of the alteration.

4. The rule in paragraph (1) places the risk of a material alteration on the person making the alteration and on the party who takes the instrument from that person. The same policy of risk allocation is adopted in the case of a forged endorsement (cf. article 23). In certain circumstances, this risk allocation may lead to the liability of an innocent person. Such potential hardship is unavoidable and seems justified by the fundamental principle "know your endorser".

5. It should be noted that the rule on material alteration laid down in article 31 deals only with the liability on the instrument. It does not prevent a person who suffered loss because of the alteration to claim damages under national law, for example from a drawer who facilitated the alteration by leaving open a space which enabled the payee to alter the figure and wording of the sum without it being apparent.

Paragraph (2)

6. In determining the liability of parties in a case of material alteration, the decisive factor is whether a party

signed before or after the alteration. Since the point of time at which the instrument was altered is in many cases difficult to determine, paragraph (2) establishes a rebuttable presumption that the alteration has been made before a signature was placed on the instrument. A party may rebut this presumption by proving that he signed before the alteration. Such proof may be extrinsic to the instrument.

Paragraph (3)

7. Paragraph (3) defines what constitutes material alteration. The test is whether there was any change in the "written undertaking on the instrument". For example, there is such a change and, consequently, a material alteration where the date of payment is altered or the sum payable is changed (whether increased or decreased). There is no such change if, for example, the sum is given in figures only and the corresponding amount is added in words, or if on a bill without a date of payment the words "on demand" are added.

8. A change in the "written undertaking on the instrument" is possible only where there was already an instrument. According to article 1 (2) and (3) a writing must comply with certain formal requisites in order to qualify as an instrument. Therefore, if one or more of the essential requisites are missing article 31 does not apply. If missing elements are added, this would be a case of completion of an instrument dealt with in article 11. However, if a writing is an instrument an alteration on it may pertain to an essential or to a non-essential requirement. The only question is whether it changes the "written undertaking on the instrument of any party".

9. There is one exception to this test: an alteration is not material if it is authorized by this Convention. For example, article 31 does not apply in the cases envisaged under article 15 (b) (conversion of blank endorsement into special endorsement) or article 21 (striking out of previous endorsements).

Article 32

(1) An instrument may be signed by an agent.

(2) The signature of an agent placed by him on an instrument with the authority of his principal and showing on the instrument that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the instrument by an agent with his authority, imposes liability on the principal and not on the agent.

(3) A signature placed on an instrument by a person as agent but without authority to sign or exceeding his authority, or by an agent with authority to sign but not showing on the instrument that he is signing in a representative capacity for a named person, or showing on the instrument that he is signing in a representative capacity

but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.

(4) The question whether a signature was placed on the instrument in a representative capacity may be determined only by reference to what appears on the instrument.

(5) A person who is liable pursuant to paragraph (3) and who pays the instrument has the same rights as the person for whom he purported to act would have had if that person had paid the instrument.

Relevant legislation

BEA — sections 25 and 26.

UCC — section 3-403.

ULB — article 8.

Cross reference

Signature: article 4 (10).

Commentary

Paragraph (1)

1. This provision makes it clear that a signature may be placed on an instrument by an agent for any party, i.e. for a maker or drawer, the acceptor, a guarantor or an endorser.

Paragraph (2)

2. If an instrument has been signed by an agent the question arises who is liable on the instrument, the agent or the principal. If an agent signs without authority, the answer of both agency law and negotiable instruments law is generally that the principal is not liable. If the agent signs with authority, the principal would be liable under agency law. However, in negotiable instruments law the liability of the principal depends on whether the instrument shows that the agent signing acted in a representative capacity for that principal. If it does not show that, the agent, though signing with authority, is liable and not the principal. The rationale of this rule is the fundamental principle of negotiable instruments law according to which a holder must be able to see from what appears on the instrument who is liable on it.

3. In conformity with these rules, paragraph (2) sets forth the cases in which the principal and not the agent is liable. One case is where an agent places his signature on an instrument with the authority of the principal and the instrument shows that he is signing in a representative capacity for that named principal. For example, A signs his name and adds the words "as agent of P" or "on behalf of P", or A writes P's name and signs "by A, agent". The

second case is where an agent places the signature of his principal on the instrument with his authority. For example, A places P's signature on the instrument without any indication that this signature was placed by him and not by P.

Paragraph (3)

4. Paragraph (3) sets forth the cases in which not the principal but the agent himself is liable on the instrument. One case is where an agent signs without, or exceeding his, authority irrespective of whether the instrument shows that he is acting in a representative capacity. If he would simply use his principal's signature without authority, this would be a case of forgery and he would be liable under article 29 (2). The second case is where an agent signs the instrument with authority but without showing that he signs in a representative capacity for a named person. Unlike in the first case, A signs with authority and he is liable only because he does not specify on the instrument that he signs on behalf of this principal as, for example, where A signs his own name. The third case is where an agent signs with authority indicating that he signs in a representative capacity but does not name the principal as, for example, where he simply signs "A, as agent".

Paragraph (4)

5. In the above cases where an agent signs with authority, it is important to determine whether or not he has acted in a representative capacity. Paragraph (4) emphasizes that such determination may be made only by what appears *ex facie* the instrument and not by any circumstances outside the instrument.

Example. A places his signature under a stamp of X Corporation which appears at the place where usually the signature of the drawer appears. The question whether A signed as an agent for X Corporation or as a co-drawer must be decided on the basis of what appears on the instrument (e.g. the distance between stamp and signature may be relevant) but not on the basis of evidence extrinsic to the instrument (e.g. the fact that A is director of X Corporation).

6. Since the only relevant factor is what appears *ex facie* the instrument, it is immaterial whether or not the holder had knowledge of the agent's authority or of his acting as agent. Furthermore, the above rules apply even if the holder is a protected holder (cf. article 26 (1) (a)).

Paragraph (5)

7. Under paragraph (3), a person may be liable although he purports to act for another person. If, accordingly, he pays the instrument, paragraph (5) accords him the same rights as the person for whom he purported to act would have obtained upon payment.

Article 33

The order to pay contained in a bill does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee.

Relevant legislation

BEA – section 53.

UCC – section 3-409.

ULB – article 16 of annex II to the Geneva Convention of 1930.

Commentary

Article 33 provides that the drawing of a bill does not of itself operate as an assignment to the payee of any funds made available for payment by the drawer with the drawee. Therefore the payee has no rights against the drawee (unless the drawee has accepted). However, nothing in this article prevents a drawer from assigning such funds to the payee by agreement. The effect of such an agreement would be governed by national law.

B. THE DRAWER*Article 34*

(1) The drawer engages that upon dishonour of the bill by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the bill in accordance with article 66, the amount of the bill, and any interest and expenses which may be recovered under article 66 or 67.

(2) The drawer may exclude or limit his own liability by an express stipulation on the bill. Such stipulation has effect only with respect to the drawer.

Relevant legislation

BEA – section 55 (1) (a).

UCC – sections 3-413 (2) and 3-502.

ULB – article 9.

Cross references

Dishonour by non-acceptance: article 50.

Dishonour by non-payment: article 54.

Necessary protest: article 55.

*Commentary***Paragraph (1)**

1. The drawer's liability is "secondary" to that of the acceptor. Only if the bill is dishonoured (by non-acceptance or non-payment) by the drawee or acceptor will the drawer be liable. The drawer's liability (unlike that of the acceptor and maker) is "conditional": it is subject to any necessary

presentment and protest. If the bill is not dishonoured, or if the bill is dishonoured but a necessary protest is not effected, the liability of the drawer has not crystallized. A distinction should be made between the absence of liability and discharge. The drawer is discharged of liability by payment or other occurrences provided in Chapter Six. Discharge assumes the existence of liability.

2. The engagement of the drawer is to pay the bill, upon dishonour and any necessary protest, to the holder or to any party subsequent to the holder who pays the bill in a recourse action. Thus, if the bill is paid by an endorser to the holder, and the bill is transferred to such endorser (with or without endorsement, cf. article 21) by the holder, the liability of the drawer is to pay the bill to such endorser.

3. It may be noted that the liability of the drawer is not subject to any notice of dishonour. This is in conformity with the policy of this Convention that notice of dishonour is not necessary in order to render a party liable on the instrument. Under article 64 failure to give due notice of dishonour renders a person who is required to give notice liable to the drawer for any damages that he may suffer from such failure.

4. Article 34 deals with the liability of the drawer. The rights of the drawer against the acceptor are dealt with in article 36 (2).

Paragraph (2)

5. Paragraph (2) allows the drawer to exclude or limit his own liability by an express stipulation on the bill. Under the Convention, such power is also given to the endorser (article 40 (2)) but not to the maker (article 35 (2)).

6. The words "his own liability" make it clear that only the drawer himself benefits from such an exclusion or limitation and not any other party from whom payment is claimed. The exclusion or limitation may be invoked by the drawer even against a remote protected holder.

7. Paragraph (2) deals only with a stipulation made expressly on the bill. It does not prevent a drawer from excluding or limiting his liability by an agreement outside the bill; in such a case he may invoke the exclusion or limitation as a defence against a holder in accordance with article 25 (1) unless that holder is a protected holder (cf. article 26 (1) (a)).

8. Paragraph (2) does not specify the wording that must be used to exclude or limit the liability. While the expression commonly used is "without recourse", the drawer may use other words for that purpose.

C. THE MAKER*Article 35*

(1) The maker engages that he will pay to the holder, or to any party who pays the note in accordance with article

66, the amount of the note in accordance with the terms of that note, and any interest and expenses which may be recovered under article 66 or 67.

(2) The maker may not exclude or limit his own liability by a stipulation on the note. Any such stipulation is without effect.

Relevant legislation

BEA – section 88.
UCC – section 3-413 (1).
ULB – article 78.

Commentary

Paragraph (1)

1. Article 35 states the basic rules on the liability of the maker of a note. The maker's liability, like that of the acceptor, is a primary liability in that his liability is not subject to presentment for payment or to any protest of dishonour for non-payment. According to paragraph (1), the maker engages to pay the amount of the note to the holder or to any party who pays the note in accordance with article 66.

2. The engagement of the maker is to pay the note to the holder or to any party who pays the note in a recourse action. Thus, if the note is paid by an endorser to the holder, and the note is transferred to such endorser (with or without endorsement, cf. article 21) by the holder, the liability of the maker is to pay the note to such endorser.

Paragraph (2)

3. The maker, since his liability is primary, may not exclude or limit his liability by a stipulation on the note. If, nevertheless, such a stipulation is made, it does not affect the validity of the note and is without effect.

4. However, nothing in this article prevents the maker from excluding or limiting his liability by a stipulation outside the note. If he does so, he may raise this as a defence against a holder in accordance with article 25 (1) but not against a protected holder (cf. article 26 (1) (a)).

D. THE DRAWEE AND THE ACCEPTOR

Article 36

(1) The drawee is not liable on a bill until he accepts it.

(2) The acceptor engages that he will pay to the holder, or to any party who pays the bill in accordance with article 66, the amount of the bill in accordance with the terms of his acceptance, and any interest and expenses which may be recovered under article 66 or 67.

Relevant legislation

BEA – sections 23 and 54.
UCC – sections 3-401, 3-409, 3-410, and 3-413 (1) and (3)
ULB – article 28.

Cross references

Form of acceptance: article 37.
Holder: articles 4 (6) and 14.

Commentary

Paragraph (1)

1. The rule expressed in this paragraph is common to all legal systems. Article 29 (1) provides that no person is liable on an instrument unless he signs it.

Paragraph (2)

2. The liability of the acceptor is a primary liability; it is not conditional upon presentment for payment (cf. article 53 (3)) and the making of a protest in the event of dishonour of the bill by him (cf. article 59 (3)).

3. The liability of the acceptor is to pay the bill at maturity to the holder. If the bill was paid to the holder by a party secondarily liable the acceptor must pay to that party.

Article 37

An acceptance must be written on the bill and may be effected:

- (a) By the signature of the drawee accompanied by the word "accepted" or by words of similar import; or
- (b) By the signature alone of the drawee.

Relevant legislation

BEA – section 17 (2) (a).
UCC – section 3-410.
ULB – article 25.

Cross reference

Signature – article 4 (10).

Commentary

The acceptance in order to be enforceable on the instrument must be in writing and must be signed by the drawee. The acceptance may be expressed by the word "accepted" or by words of similar import. However, the signature alone of the drawee, whether on the face or on the back of the bill, constitutes an acceptance.

Article 38

(1) An incomplete instrument which satisfies the requirements set out in article 1 (2) (a) may be accepted by the drawee before it has been signed by the drawer, or while otherwise incomplete.

(2) A bill may be accepted before, at or maturity, or after it has been dishonoured by non-acceptance or non-payment.

(3) When a bill drawn payable at a fixed period after sight, or a bill which must be presented for acceptance before a specified date, is accepted, the acceptor must indicate the date of his acceptance; failing such indication by the acceptor, the drawer or the holder may insert the date of acceptance.

(4) If a bill drawn payable at a fixed period after sight is dishonoured by non-acceptance and the drawee subsequently accepts it, the holder is entitled to have the acceptance dated as of the date on which the bill was dishonoured.

Relevant legislation

BEA — section 18.

UCC — section 3-410 (2) and (3).

ULB — article 25.

Cross references

Incomplete instrument: article 11.

Maturity: article 4 (9).

Dishonour by non-acceptance: article 50.

Dishonour by non-payment: article 54.

*Commentary**Paragraph (1)*

1. A bill may be accepted before it is issued by the drawer or even before it is signed by him or is incomplete in other respects. If an incomplete bill is signed by the drawee he will be liable on it under this Convention only when the writing he signs satisfies the requirements set out in article 1 (2) (a) and when the writing is completed in accordance with article 11. Therefore a signature of a purported drawee on a blank piece of paper can never be or become an acceptance under this Convention.

Paragraph (2)

2. A bill may be accepted also at or after maturity or after it has been dishonoured by non-acceptance or non-payment.

Paragraph (3)

3. A bill drawn payable at a fixed period after sight (i.e., at a fixed period after presentment for acceptance) must be presented for acceptance in order to determine

the date of payment (article 45 (2) (b)). It may happen that when such a bill is presented and accepted the acceptor omits to indicate the date of his acceptance. In such a case, the date of payment cannot be ascertained from the face of the bill, and the bill is incomplete. Paragraph (3) provides that in such a case, the drawer or the holder may insert the date of acceptance. This Convention, by giving the drawer or holder the right to insert the missing date, uses the approach that is applicable to any other completion of an incomplete instrument (cf. article 11).

4. Similarly when the drawer has stipulated on the bill that it is to be presented for acceptance before a specified date and the acceptor does not indicate the date of his acceptance the drawer or the holder may insert the date of acceptance.

Paragraph (4)

5. It occurs in practice that the drawee is prepared to accept an "after sight" bill which he had previously dishonoured by non-acceptance. In such a case the date of acceptance is important in order to determine the date of payment. Paragraph (4) provides that the holder is entitled to have the bill accepted not as from the date of the acceptance, but as from the date of the dishonour by non-acceptance. If the acceptor refuses to write the correct date, this would be a "qualified acceptance" dealt with in article 39 and the holder may refuse to take the "qualified" acceptance, and may treat the bill as dishonoured by non-acceptance.

Article 39

(1) An acceptance must be unqualified. An acceptance is qualified if it is conditional or varies the terms of the bill.

(2) If the drawee stipulates on the bill that his acceptance is subject to qualification:

(a) He is nevertheless bound according to the terms of his qualified acceptance;

(b) The bill is dishonoured by non-acceptance.

(3) An acceptance relating to only a part of the amount of the bill is a qualified acceptance. If the holder takes such an acceptance, the bill is dishonoured by non-acceptance only as to the remaining part.

(4) An acceptance indicating that payment will be made at a particular address or by a particular agent is not a qualified acceptance, provided that:

(a) The place in which payment is to be made is not changed;

(b) The bill is not drawn payable by another agent.

Relevant legislation

BEA — sections 19 and 44.

UCC — section 3-412.

ULB — article 26.

Cross reference

Dishonour by non-acceptance: article 50.

Commentary

1. The holder of a bill is entitled to an unqualified acceptance, i.e., the undertaking by the drawee to pay the bill according to its terms. Thus, any acceptance which is conditional (making payment dependent upon the fulfillment of a condition) or which varies the terms of the bill (e.g. partial as to the amount or qualified as to place or time) would not be an unqualified acceptance and the holder is not obliged to take it.

2. If the drawee signs an acceptance which is qualified he dishonours the bill by non-acceptance but is bound by the terms of his qualified acceptance (cf. article 50 (1) (a)). In such a case the holder may exercise an immediate right of recourse upon due protest. If the holder takes the qualified acceptance and does not protest the dishonour he has rights against the acceptor under the qualified acceptance but parties secondarily liable to the holder are not liable.

3. Paragraphs (3) and (4) set forth two exceptions to the above general rule. If the acceptance is qualified because the acceptance relates to only a part of the amount of the bill, the bill is considered to be dishonoured by non-acceptance only as to the part of the amount not accepted. If the acceptance indicates that payment will be made at a particular address or by a particular agent, the acceptance is an unqualified acceptance if it does not change the terms of the bill as to the place of payment and does not substitute another agent for the agent indicated by the drawer as the payer.

E. THE ENDORSER

Article 40

(1) The endorser engages that upon dishonour of the instrument by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the instrument in accordance with article 66, the amount of the instrument, and any interest and expenses which may be recovered under article 66 or 67.

(2) The endorser may exclude or limit his own liability by an express stipulation on the instrument. Such stipulation has effect only with respect to that endorser.

Relevant legislation

BEA — section 55 (2) (a).

UCC — section 3-414 (1).

ULB — article 15.

Cross references

Dishonour by non-acceptance: article 50.

Dishonour by non-payment: article 54.

Necessary protest: article 55.

Commentary

1. The endorsement may be a necessary element in the transfer of an instrument (cf. article 12 (a)) and serves the function of rendering the endorser liable on the instrument. This latter function is dealt with in article 40.

2. The endorser's liability is "secondary" to that of the acceptor or maker. Only if the bill is dishonoured (by non-acceptance or non-payment) by the drawee or acceptor or if the note is dishonoured (by non-payment) by the maker, will the endorser be liable. The endorser's liability is "conditional": it is subject to any necessary presentment and protest.

Paragraph (1)

3. According to paragraph (1), the engagement of the endorser is to pay the instrument, upon dishonour and any necessary protest, to the holder or to any subsequent party who pays the instrument in a recourse action. Thus, if an instrument endorsed by the payee to A and by A to B is paid by A to B, the payee's liability is to pay A. The liability of the endorser on the instrument is, thus, similar to the drawer's liability on the bill (see commentary to article 34, paragraphs 1-4).

Paragraph (2)

4. The endorser — like the drawer (article 34 (2)) but unlike the maker (article 35 (2)) — may exclude or limit his own liability by an express stipulation on the instrument. It should be noted that in the case of an endorsement for collection the exclusion of liability follows from the rule laid down in article 20 (2).

5. The words "his own liability" make it clear that only the endorser himself benefits from such an exclusion or limitation and not any other party from whom payment is claimed. The exclusion or limitation being *ex facie* the instrument may be invoked by the endorser even against a remote protected holder.

6. Paragraph (2) deals only with a stipulation made expressly on the instrument. It does not prevent an endorser from excluding or limiting his liability by an agreement outside the instrument; in such a case he may invoke the exclusion or limitation as a defence against a holder in accordance with article 25 (1) unless the holder is a protected holder (cf. article 26 (1) (a)).

7. Paragraph (2) does not specify the wording that must be used to exclude or limit the liability. While the expression commonly used is "without recourse", the endorser may use other words for that purpose.

Article 41

(1) Any person who transfers an instrument by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer:

- (a) A signature on the instrument was forged or unauthorized; or
- (b) The instrument was materially altered; or
- (c) A party has a valid claim or defence against him; or
- (d) The bill was dishonoured by non-acceptance or non-payment or the note was dishonoured by non-payment.

(2) The damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.

3. Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the instrument without knowledge of such defect.

Relevant legislation

BEA – section 58.
UCC – section 3-417 (2).

Cross references

Transfer: article 12.
Forged signature: articles 4 (10), 30.
Unauthorized signature: article 32 (3).
Material alteration: article 31.
Dishonour by non-acceptance: article 50.
Dishonour by non-payment: article 54.
Knowledge: article 5.

*Commentary**Paragraph (1)*

1. A person who transfers an instrument by mere delivery (cf. article 12 (b)) is not liable on the instrument since he has not signed it. However, such person may incur liability under article 41. Under this article, he is liable for any damages that a subsequent holder may suffer as a consequence of any of the circumstances referred to in subparagraphs (a) to (d) of paragraph (1).

2. The fact that the transferor did not know of any such circumstance, whether negligently or not, does not affect his liability under the article. Such liability benefits any subsequent holder who, when taking the instrument, has no knowledge of the deficiency. The liability under article 41 is off the instrument and, thus, presentment and protest are not conditions precedent to such liability. It materializes the moment the instrument is transferred, regardless of its date of maturity.

Example A. The maker issues a note to the payee (P) for the sum of 1,000 Swiss francs. P endorses the note in blank and delivers it to C who alters the sum payable

to 11,000 Swiss francs. C delivers the note to D who does not know about the alteration, and D delivers it to E who does not know about the alteration. E may claim from the maker and from P 1,000 Swiss francs under article 31 (1) (b). E has no right on the instrument against C or D since they have not endorsed it. However, E may recover from C or D, under article 41, 10,000 Swiss francs as compensation for the damages suffered by him.

3. A person who transfers an instrument by mere delivery and who has no knowledge of any circumstances giving rise to liability under article 41 may exclude or limit his liability by agreement off the instrument or by an express stipulation on the instrument. Although this faculty is not stated in article 41, it follows from the fact that it is liability off the instrument and for damages.

4. Under article 41 the holder may recover only those damages which he has suffered "on account of" any factor enumerated in paragraph (1). Consequently, insolvency of the drawer would not confer a right of action under article 41 on the transferee by mere delivery, since the transferor is not deemed, under the article, to have warranted the solvency of a secondary obligor.

5. The holder may recover only if, on account of the factors enumerated, he has in fact suffered damages. This is not the case where he has been paid the amount due, for example, by a person whose signature had been forged but who accepted it or represented it to be his own (cf. article 30). Another example is where an instrument which was dishonoured by non-payment was nevertheless paid.

Subparagraph (a)

6. According to article 30 a person whose signature has been forged is not liable on the instrument. A holder who takes the instrument without knowledge of the forgery may therefore suffer loss by relying on the liability of that person. Subparagraph (a) is intended to protect him against such risk. The same is true with regard to an unauthorized signature.

Example B. The maker issues a note which shows on it that he signs as agent, though he had no authority to sign. The payee endorses the note in blank to B who transfers it by delivery to C. Upon dishonour by non-payment, C has an action against B under article 41 (1) (a).

Subparagraph (b)

7. According to article 31 (1) (b) parties who have signed the instrument before a material alteration are liable according to the terms of the original text. This may cause loss to a holder who receives an instrument without knowledge of the alteration (cf. above example A, paragraph 2). Subparagraph (b) is intended to protect him.

Subparagraph (c)

8. The transferee may be subject to a valid claim against him and as a consequence may suffer loss.

Example C. The maker issues a note to the payee (P). The note is stolen and P's signature is forged by A who delivers the note to B. B endorses it in blank to C. C transfers it by mere delivery to D who is not a protected holder. D is subject to a valid claim to the instrument by P and may recover any ensuing damages from C under article 41 (1) (c).

Example D. The maker issues a note to the payee (P) who endorses it in blank. The note is stolen from P by T who transfers it to A who is not a protected holder. A transfers the note to B who is not a protected holder. The payee has a claim to the note against B and B may recover any damages from A (article 41 (1) (c)).

9. The same rule applies with regard to a valid defence which a party prior to the transferor may raise against the transferee.

Example E. The payee by fraud induces the maker to issue a note to him, the payee (P). P endorses the note in blank and transfers it to A who is not a protected holder. A transfers it to B who is not a protected holder. In an action by B against the maker, the maker may raise the defence of fraud. B has an action for damages against A.

Subparagraph (d)

10. This subparagraph protects the transferee against the risk that the bill was dishonoured by non-acceptance or non-payment or that the note was dishonoured by non-payment. The words "was dishonoured" make it clear that damages lie only if the instrument was dishonoured before the transfer. Thus transfer by mere delivery, unlike transfer by endorsement, does not provide a warranty of payment.

Paragraph (2)

11. Paragraph (2) limits the amount of damages to the amount of the instrument. Other questions concerning the extent of liability, such as mitigation of damages, limitation of action, are left to the applicable national law.

Paragraph (3)

12. Following the rationale of the liability rule in paragraph (1), i.e. to protect the innocent transferee, paragraph (3) specifies that only those transferees may recover who are without knowledge of the defect which causes the loss (as to the definition of "knowledge", see article 5).

F. THE GUARANTOR

Article 42

(1) Payment of an instrument, whether or not it has been accepted, may be guaranteed, as to the whole or part of its amount, for the account of a party or the drawee. A guarantee may be given by any person who may or may not already be a party.

(2) A guarantee must be written on the instrument or on a slip affixed thereto (*allonge*).

(3) A guarantee is expressed by the words "guaranteed", "*aval*", "good as *aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires:

(a) A signature alone on the front of the instrument, other than that of the drawer or the drawee, is a guarantee;

(b) The signature alone of the drawee on the front of the instrument is an acceptance; and

(c) A signature alone on the back of the instrument other than that of the drawee is an endorsement.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the acceptor or the drawee in the case of a bill, and the maker in the case of a note.

Relevant legislation

BEA — no relevant provision and see section 56.

UCC — no relevant provision and see sections 3-402, 3-415 and 3-416.

ULB — articles 30 and 31.

Cross reference

Party: article 4 (8).

Commentary

1. In addition to the liability incurred by the drawer, acceptor and endorser of a bill and the maker and endorser of a note the Convention recognizes the special liability of a person who signs an instrument as a "guarantor". The liability is a guarantee of payment of the whole or part of the amount of the instrument for the account of a party or the drawee. Such a guarantee may be given by a stranger or by someone who is already a party. The guarantee is "transferable" in nature in that it runs with the instrument.

2. The provisions of the Convention in respect of this liability of a guarantor follow in substance the provisions of the Geneva Uniform Law in respect of the giver of an *aval*.

3. The guarantee is given on the instrument itself, or on an *allonge* or slip affixed to the instrument, by

a signature accompanied by the words "guarantee", "payment guaranteed", "aval", "good as *aval*" or by words of similar import. However, if the guarantee is given on the face of the instrument a signature alone is sufficient to express the guarantee provided the signature is not that of the drawee (in which case it is an acceptance) or the drawer. A signature alone on the back of the instrument is an endorsement.

4. The person signing as guarantor may, but need not, indicate on the instrument for whose account he effects the guarantee. In the absence of such indication the guarantee is given for the acceptor or the drawee in the case of a bill and for the maker in the case of a note. This rule is justified by the fact that it is from the drawee, acceptor or maker that payment must initially be demanded.

5. Under the Convention a person may become a guarantor for the drawee and, indeed, if the guarantor has not specified the person for whom he has become a guarantor, the irrebuttable presumption is that he is the guarantor of the drawee (and if the drawee has accepted the bill, of the acceptor). In other words the essential liability of the guarantor of the drawee or the acceptor is to pay the bill when due: failure to present the bill for payment does not discharge him of liability (cf. article 53 (3)) nor does failure to protest dishonour (cf. article 59 (3)).

Article 43

(1) A guarantor is liable on the instrument to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the instrument.

(2) If the person for whom he has become guarantor is the drawee, the guarantor undertakes to pay the bill at maturity.

Relevant legislation

ULB – article 32.

Cross reference

Maturity: article 4 (9).

Commentary

1. Subject to the exception stated in paragraph (2) of this article the liability of a guarantor is of an accessory nature: if the liability of the party for whom the guarantee is given is a primary liability (as where that party is the maker or the acceptor) the liability of the guarantor is also primary. In such a case failure to present the instrument for payment does not discharge the guarantor (cf. article 53 (3)), nor does failure to protest dishonour (cf. article 59 (3)). Likewise if the liability of the party is secondary, the liability of the guarantor is also secondary

and due presentment for acceptance (where necessary) and due protest are, unless dispensed with, conditions precedent to his liability.

2. A further corollary of the rule stated in paragraph (1) is that the guarantor may base defences against his liability on the instrument on the defences which the party for whom he became guarantor may invoke. In addition the guarantor may set up defences which are personal to himself. On the other hand the guarantor is not entitled to the benefit of excussion: the holder or a party who has taken up and paid the instrument is not obliged to demand payment first from the person in favour of whom the guarantee was given. Therefore, the liability of the guarantor is not dependent on the refusal to pay by the person for whom he became guarantor. However the guarantor, other than the guarantor for the drawee, cannot be sued under the guarantee until the liability of the person for whom he became guarantor has materialized.

3. Under paragraph (1) the guarantor may "stipulate otherwise", i.e. the liability under a guarantee may be extended or restricted by the giver thereof. Such stipulation may relate to any possible element of the guarantor's liability in any possible way, including different time or place of payment and reduction or increase of the amount. For example, the guarantor may stipulate that the guarantee is given for part of the sum due or, where he is the guarantor of the drawee, that his liability is subject to due presentment and due protest, or that the guarantee is given for a limited time.

4. The rule in paragraph (1) that the liability of a guarantor is co-existent with the liability of the party for whom he has become guarantor does, for obvious reasons, not apply in the case where the guarantee is given for the drawee. The liability of the guarantor of the drawee is to pay the bill at maturity. Presentment of the bill for payment to the drawee is not necessary to make such guarantor liable on the bill.

Article 44

The guarantor who pays the instrument has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

Relevant legislation

ULB – article 32.

Cross reference

Party: article 4 (8).

Commentary

The guarantor upon payment of the instrument by him acquires rights on it against the party for whom he became guarantor and against those parties who are liable to that

party. The rights of the drawee's guarantor who pays the bill are not dealt with in this Convention. Any action by such guarantor against the drawee would be outside the bill. It may be noted that the guarantor has rights on the instrument against parties who are liable on it to the party for whom he became guarantor even if he is not a holder (as where the instrument was not transferred to him under article 12). A guarantor who is not a holder may not transfer the instrument.

CHAPTER FIVE. PRESENTMENT, DISHONOUR BY NON-ACCEPTANCE OR NON-PAYMENT, AND RECOURSE

Section 1. Presentment for acceptance and dishonour by non-acceptance

Article 45

- (1) A bill may be presented for acceptance.
- (2) A bill must be presented for acceptance:
 - (a) When the drawer has stipulated on the bill that it must be presented for acceptance;
 - (b) When the bill is drawn payable at a fixed period after sight; or
 - (c) When the bill is drawn payable elsewhere than at the residence or place of business of the drawee, except where such a bill is payable on demand.

Relevant legislation

BEA – section 39.
 UCC – section 3-501.
 ULB – articles 21 and 22.

Cross reference

Acceptance: article 37.

Commentary

1. The general rule embodied in this article is that presentment for acceptance is optional except in the cases stated in paragraph (2). The provisions of the Convention pertaining to presentment for acceptance apply only to bills of exchange, not to promissory notes. By accepting the bill the drawee becomes liable on it (articles 29 (1) and 36). Except in the case referred to in article 46 (1) refusal by the drawee of a bill to accept it gives rise to dishonour and entitles the holder, upon due protest (article 55), to exercise an immediate right of recourse against the drawer and any endorser and guarantor (article 50 (2)).

Paragraph (2)

2. In the three cases stated in paragraph (2) presentment for acceptance is a condition precedent to any right of action against the drawer, any endorser and guarantor.

As to when presentment for acceptance is dispensed with, see article 48.

Subparagraph (a)

3. An express stipulation on a bill that it must be presented for acceptance may be made only by the drawer and benefits any subsequent party.

4. The drawer may stipulate that the bill must be presented before a specified date (cf. articles 38 (3) and 47 (f)).

Subparagraph (b)

5. If a bill is drawn payable at a fixed period after sight (cf. article 8 (3) (b)) presentment for acceptance is necessary in order to determine the date of the instrument. If the acceptor of such a bill omits to indicate the date of his acceptance the holder may insert that date (cf. article 38 (3)).

Subparagraph (c)

6. The rationale of the requirement that a bill drawn payable elsewhere than at the residence or place of business of the drawee (a "domiciled" bill) must be presented for acceptance is founded upon the need to advise the drawee that a bill has been drawn upon him payable at a place other than his residence or place of business so as to enable him to provide his agent (usually a bank) with the necessary funds. However, the requirement of presentment for acceptance does not obtain in the case of a demand bill. The holder of such a bill is entitled to immediate payment and should not be required to present the bill first for acceptance.

Article 46

(1) Notwithstanding the provisions of article 45 the drawer may stipulate on the bill that it must not be presented for acceptance or that it must not be so presented before a specified date or before the occurrence of a specified event.

(2) If a bill is presented for acceptance notwithstanding a stipulation permitted under paragraph (1) and acceptance is refused, the bill is not thereby dishonoured.

(3) If the drawee accepts a bill notwithstanding a stipulation that it must not be presented for acceptance, the acceptance is effective.

Relevant legislation

ULB – article 22.

Cross reference

Dishonour by non-acceptance: article 50.

Commentary

1. This article deals with the express stipulation on a bill that it shall not be presented for acceptance. The legal effect of such a stipulation is that the holder may not exercise an immediate right of recourse for dishonour by non-acceptance. The drawer only may write such stipulation on the bill and the stipulation benefits any subsequent party.

Paragraph (1)

2. This paragraph permits a stipulation to the effect that the bill must not be presented for acceptance or that it must not be so presented before a date specified in the stipulation or before the occurrence of a specified event. Inquiries amongst banking and trade institutions have shown that stipulations requesting the holder not to present the bill before the occurrence of a specified event occur not infrequently. In some countries, particularly Latin American, it appears to be normal practice to delay presentment until the merchandise has arrived or (in some African countries) until after customs clearance. In some countries, drawees often refuse to accept documentary bills on the ground that the carrying vessel has not yet reached its destination point, and a bill may therefore direct a holder not to present it for acceptance until the vessel has arrived.

3. Such stipulation, if made on a bill drawn payable at a fixed period after sight, does not affect the validity of the instrument as an international bill of exchange on the ground that the instrument would no longer be payable at a definite time or would be "conditional". If the specified event did not occur, for instance the vessel suffered shipwreck before reaching its destination, presentment for acceptance as directed by the stipulation is obviously impossible and would be dispensed with under article 48 (b). In that case, the holder would acquire an immediate right of recourse (by virtue of article 50 (1) (b)). The bill is not made "conditional" by such a stipulation because the order to pay is not conditional.

Paragraph (2)

4. The purpose of this rule is to lay down that if a bill on which it is stipulated that it must not be presented for acceptance is nevertheless so presented and acceptance is refused, the refusal does not amount to a dishonour by non-acceptance. Consequently, a refusal to accept such a bill does not entitle the holder to an immediate right of recourse against prior parties and they can become liable only if the bill is dishonoured by non-payment.

Paragraph (3)

5. An acceptance is an engagement by the drawee that he will pay the bill to the holder or to any party who pays the bill in accordance with article 66. Accordingly, an acceptance even if made in the context of a stipulation

under paragraph (1) binds the drawee and benefits all parties.

Article 47

A bill is duly presented for acceptance if it is presented in accordance with the following rules:

(a) The holder must present the bill to the drawee on a business day at a reasonable hour;

(b) A bill drawn upon two or more drawees may be presented to any one of them, unless the bill clearly indicates otherwise;

(c) Presentment for acceptance may be made to a person or authority other than the drawee if that person or authority is entitled under the applicable law to accept the bill;

(d) If a bill is drawn payable on a fixed date, presentment for acceptance must be made before or on the date of maturity;

(e) A bill drawn payable on demand or at a fixed period after sight must be presented for acceptance within one year of its date;

(f) A bill in which the drawer has stated a date or time-limit for presentment for acceptance must be presented on the stated date or within the stated time-limit.

Relevant legislation

BEA — sections 40 and 41.

UCC — sections 3-503 and 3-504.

ULB — articles 2, 22 and 23.

Cross references

Acceptance: article 37.

Date or time-limit for acceptance: articles 45 and 46.

Bill drawn upon two or more drawees: article 9.

Commentary

1. In order to establish the liability of parties because of dishonour by non-acceptance, presentment for acceptance, whether optional or mandatory (cf. article 45), must be due presentment. Article 47 specifies what constitutes due presentment for acceptance.

Paragraph (a)

2. As elsewhere in this Convention, the word "holder" or "drawee" includes an authorized agent.

3. In contrast to presentment for payment, which is local, i.e. where the funds are, presentment for acceptance is personal. It must be made to the drawee or his authorized agent because he must write the acceptance. For this reason, it is not necessary to set forth rules as to the place of presentment for acceptance.

4. The requirement that presentment must be made "on a business day at a reasonable hour" refers to the business day and reasonable hour at the place of the drawee.

Paragraph (b)

5. This paragraph envisages the special case of bills drawn upon two or more drawees, and follows in this respect section 3-504 (3) (a) of the UCC which eliminates the requirement, found in section 41 (1) (b) of the BEA, that presentment be made to each of two or more drawees. Under paragraph (b), presentment is to be made to all drawees only when it is so indicated on the bill.

Paragraph (c)

6. This paragraph applies to cases where, for instance, the drawee of a bill is dead or insolvent or where he is incapable by reason of insanity, or where a body corporate is in liquidation or has ceased to exist. These circumstances excuse the holder from presentment for acceptance (article 48 (a)) and entitle him to treat the bill as dishonoured by non-acceptance. However, presentment to a person or authority entitled under the applicable law to accept the bill is, if the other requirements of article 47 are met, due presentment and an acceptance so obtained is a valid acceptance.

Paragraphs (d) and (e)

7. These provisions lay down rules as to the time of presentment for acceptance.

Paragraph (d)

8. Presentment for acceptance of a bill with a fixed maturity date must be made on or before the date the bill is payable. It may be noted that if acceptance is obtained after maturity the acceptance will bind the acceptor (cf. article 38 (2)), though in such a case the bill is not "duly presented for acceptance" for the purposes of article 47. If the bill was one which must be presented for acceptance under article 45 (2) the drawer, the endorser and the guarantors would not be liable on the bill (cf. article 49).

Paragraph (e)

9. A bill payable at a fixed period after sight must be presented for acceptance (cf. article 45 (2) (b)). Paragraph (e) follows the ULB by requiring that such a bill must be presented for acceptance within one year of its date. Under article 1 (2) (d) a bill must be dated. The BEA and UCC provide that an after sight bill must be either presented for acceptance or negotiated within a reasonable time. Since the concept of "reasonable time" with reference to negotiable instruments is unknown outside the common law countries and might lead to difficulties of application on universal level, it has not been retained in this Convention.

Paragraph (f)

10. This paragraph covers a bill on which the drawer has stipulated that it be presented for acceptance on a specified date or within a specified period of time. Such a stipulation benefits any subsequent party.

Article 48

A necessary or optional presentment for acceptance is dispensed with:

(a) If the drawee is dead or has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to incur liability on the instrument as an acceptor, or if the drawee is a corporation, partnership, association or other legal entity which has ceased to exist;

(b) When, with reasonable diligence, presentment cannot be effected within the time-limits prescribed for presentment for acceptance.

Relevant legislation

BEA — section 41 (2) and (3).

UCC — section 3-511.

ULB — article 54.

Cross references

Necessary or optional presentment for acceptance: article 45.

Time-limits for presentment for acceptance: article 47 (d) to (f).

Commentary

1. Article 48 states the cases in which presentment for acceptance is dispensed with. Under article 50 (1) (b) such cases constitute constructive dishonour and under article 50 (2) the holder may then, subject to any necessary protest, exercise an immediate right of recourse.

2. The common law system and the Geneva Uniform Law both recognize the existence of circumstances which excuse the holder from an obligation to present a bill for acceptance or for payment, or from drawing up a protest or giving a notice of dishonour. However, there are sharp differences as to the approach adopted, on the one hand, by the BEA and UCC and, on the other hand, by the ULB.

(a) Under the English and American statutes, circumstances beyond the control of the holder excuse delay in presentment, protest or notice of dishonour. Once the cause of delay has ceased to operate presentment or protest must be made with "reasonable diligence". Presentment or protest or notice of dishonour is dispensed with when, after the exercise of reasonable diligence, it cannot be effected. Under the ULB, the existence of an insurmountable obstacle ("vis major") extends the time-limits for presentment or

for protest. The holder must, on pain of losing his right of recourse against prior parties, present the bill or draw up protest "without delay" if the "*vis major*" ceases to operate within a period of 30 days after maturity, or, in respect of demand bills and after sight bills, within 30 days as from the date on which the holder has given notice of "*vis major*" to his endorser. The holder is dispensed from making presentment or protest if the "*vis major*" continues to operate beyond that period, and he is then permitted to exercise an immediate right of recourse;

(b) The grounds upon which presentment or protest is excused or dispensed with under the two systems also differ. The ULB mentions only "*vis major*", including the "legal prohibition (*prescription légale*) by any State", but excludes expressly "facts which are purely personal to the holder". Under the BEA and UCC, such "personal facts" can be a legitimate cause for delay or for dispensation;

(c) The BEA and UCC set forth grounds, excusing delay in presentment or protest or dispensing with these formalities, that are not expressly mentioned in the ULB, and vice versa.

3. Article 48 does not make provision for the excuse of delay. The Convention adopts a system of fixed time-limits for presentment for acceptance (article 47), as in the ULB, rather than the concept of reasonable time recognized under Anglo-American law. If by reasonable diligence presentment for acceptance cannot be made within the prescribed time-limits for such presentment, presentment is completely dispensed with.

4. If the drawee is dead, insolvent or without capacity to incur liability on the instrument as an acceptor, or is a body corporate in liquidation or having ceased to exist, the holder may either present the bill "to a person or authority other than the drawee if that person or authority is entitled under the applicable law to accept the bill" (article 47 (c)) or treat the bill as dishonoured and exercise an immediate right of recourse against prior parties. The question what constitutes insolvency or incapacity is left to the applicable national law.

5. If the drawee is a fictitious person the holder is entitled to treat the bill as dishonoured and exercise an immediate right of recourse. The fact that the drawee is a fictitious person does not violate the formal requisites under article 1 (2) (b).

Article 49

If a bill which must be presented for acceptance is not so presented, the drawer, the endorsers and their guarantors are not liable on the bill.

Relevant legislation

BEA — sections 39 (3) and (4), and 40.

UCC — sections 3-501 and 3-502.

ULB — article 53.

Cross reference

Bills that must be presented for acceptance: article 45 (2).

Commentary

If the bill is one which must be presented for acceptance (cf. article 45 (2)) due presentment for acceptance is a condition precedent to the liability of parties prior to the holder. If the bill is not so presented a refusal by the drawee to pay the bill does not constitute dishonour by non-payment and does not entitle the holder to a right of recourse against prior parties.

Article 50

(1) A bill is considered to be dishonoured by non-acceptance:

(a) When the drawee, upon due presentment, expressly refuses to accept the bill or acceptance cannot be obtained with reasonable diligence or when the holder cannot obtain the acceptance to which he is entitled under this Convention;

(b) If presentment for acceptance is dispensed with pursuant to article 48, unless the bill is in fact accepted.

(2) If a bill is dishonoured by non-acceptance the holder may:

(a) Subject to the provisions of article 55, exercise an immediate right of recourse against the drawer, the endorsers and their guarantors;

(b) Exercise an immediate right of recourse against the guarantor of the drawee.

Relevant legislation

BEA — sections 42 and 43.

UCC — sections 3-502 and 3-507.

ULB — article 53.

Cross references

Due presentment: article 47.

Presentment dispensed with: article 48.

Acceptance to which the holder is entitled: article 39.

Right of recourse: article 55.

Commentary

1. Pursuant to article 30 the holder of a bill is entitled to an unqualified acceptance; a qualified acceptance constitutes dishonour (cf. article 39).

2. The fact that a bill has been dishonoured by non-acceptance does not prevent the drawee from accepting it subsequently (cf. article 38 (2)).

3. Article 50 (1) lays down what constitutes dishonour by non-acceptance. Article 50 (2) states the legal effect of such dishonour. The exercise of the immediate right of recourse is subject to due protest (cf. article 55). In such a case presentment for payment is dispensed with (cf. article 52 (2)).

4. Pursuant to article 42 (1) payment of the bill may be guaranteed for the account of the drawee. If the guarantor of the drawee pays the bill the other parties are discharged.

Section 2. Presentment for payment and dishonour by non-payment

Article 51

An instrument is duly presented for payment if it is presented in accordance with the following rules:

(a) The holder must present the instrument to the drawee or to the acceptor or to the maker on a business day at a reasonable hour;

(b) A bill drawn upon or accepted by two or more drawees, or a note signed by two or more makers, may be presented to any one of them, unless the instrument clearly indicates otherwise;

(c) If the drawee or the acceptor or the maker is dead, presentment must be made to the persons who under the applicable law are his heirs or the persons entitled to administer his estate;

(d) Presentment for payment may be made to a person or authority other than the drawee, the acceptor or the maker if that person or authority is entitled under the applicable law to pay the instrument;

(e) An instrument which is not payable on demand must be presented for payment on the date of maturity or on the business day which follows;

(f) An instrument which is payable on demand must be presented for payment within one year of its date;

(g) An instrument must be presented for payment:

(i) At the place of payment specified on the instrument; or

(ii) If no place of payment is specified, at the address of the drawee or the acceptor or the maker indicated on the instrument; or

(iii) If no place of payment is specified and the address of the drawee or the acceptor or the maker is not indicated, at the principal place of business or habitual residence of the drawee or the acceptor or the maker;

(h) An instrument may be presented for payment at a clearing-house.

Relevant legislation

BEA — section 45.

UCC — sections 3-503 and 3-504.

ULB — articles 34 and 38.

Cross references

Holder: articles 4 (6) and 14.

Bill drawn upon two or more drawees: article 9 (1).

Note signed by two or more makers: article 9 (2).

Instrument payable on demand: article 8 (1) and (2).

Commentary

1. In order to establish the liability of parties because of dishonour by non-payment, presentment for payment must be due presentment. Article 51 specifies what constitutes due presentment for payment.

Paragraph (a)

2. As elsewhere in this Convention, the word "holder", "drawee", "acceptor" or "maker" includes an authorized agent.

3. The requirement that presentment must be made "on a business day at a reasonable hour" refers to the business day and reasonable hour at the place of the drawee, the acceptor or the maker, as the case may be.

Paragraph (b)

4. Under paragraph (b) presentment is to be made to all drawees or to all makers only when it is so indicated on the instrument. If a place of payment is specified on the instrument the holder must present it to the drawee, the acceptor or maker at that place, but if two or more drawees, acceptors or makers have their residence or place of business at that place the holder may present the instrument to any one of them.

Paragraph (c)

5. In contrast with presentment for acceptance (article 48 (a)) the death of the drawee or the acceptor or the maker does not dispense with presentment for payment but the holder must present the instrument for payment to the person who under the applicable law is his heir or the person administering his estate.

Paragraph (d)

6. This paragraph applies to cases where, for instance, the drawee, the acceptor or the maker is insolvent or where he is incapable by reason of insanity, or where a body corporate is in liquidation or has ceased to exist. These circumstances excuse the holder from presentment for payment (cf. article 52 (2) (d)) and entitle him to treat the instrument as dishonoured by non-payment. However,

presentment to a person or authority entitled under the applicable law to pay the instrument is due presentment.

Paragraphs (e) and (f)

7. These paragraphs set forth rules as to the time at which or within which presentment for payment must be made. Presentment for payment after the business day following the date of maturity (in the case of instruments payable at a definite time) or within one year of the date of the instrument (in the case of instruments payable on demand) deprives the holder of the right of recourse if the instrument is dishonoured and prior parties will not be liable to him on it. However, presentment for payment is unnecessary to render the acceptor liable (cf. article 36 (2)).

Paragraphs (g) and (h)

8. Since presentment for payment is "local" (cf. paragraph 3 of the commentary to article 47), paragraphs (g) and (h) set forth rules regarding the proper place of presentment for payment.

Article 52

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:

- (i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made:

(b) If an instrument is not payable on demand, and the cause of delay in making presentment continues to operate beyond 30 days after maturity;

(c) If an instrument is payable on demand, and the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment;

(d) If the drawee, the maker or the acceptor has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to make payment, or if the drawee, the maker or the acceptor is a corporation, partnership, association or other legal entity which has ceased to exist;

(e) If there is no place at which the instrument must be presented in accordance with article 51 (g).

(3) Presentment for payment is also dispensed with as regards a bill, if the bill has been protested for dishonour by non-acceptance.

Relevant legislation

BEA – section 46.

UCC – section 3-511.

ULB – articles 44 and 54.

Cross reference

Instrument payable on demand: article 8 (1) and (2).

Commentary

1. Article 42 provides for the excuse of delay in making presentment of an instrument for payment and states the grounds on which such presentment is dispensed with.

Paragraph (1)

2. When delay is excused the liability of parties prior to the holder is not affected on the ground that there was no due presentment for payment. Under paragraph (1) delay is excused when the holder is prevented from presenting the instrument for payment by circumstances beyond his control which he could neither avoid nor overcome. When the cause of delay ceases to operate presentment must be made with reasonable diligence. However, if such cause continues to operate beyond 30 days after maturity (in the case of instruments not payable on demand) or after the expiration of the time-limit for presentment for payment (in the case of instruments payable on demand) presentment is altogether dispensed with and a right of recourse may be exercised against parties secondarily liable on the instrument.

Paragraph (2)

3. Paragraph (2) states the cases where presentment for payment is dispensed with. Under article 54 (1) (b) such cases constitute constructive dishonour and under article 54 (2) the holder may then, subject to any necessary protest, exercise a right of recourse.

Subparagraph (a)

4. A waiver of presentment for payment may be stipulated expressly on the instrument or expressly or impliedly off the instrument. If waiver is on the instrument the dispensation is operative only as regards the party waiving presentment except if waiver is made by the drawer in which case the dispensation runs with the instrument and is operative as regards any party subsequent to the drawer. A waiver of presentment on the instrument

benefits any holder. If waiver is off the instrument, whether impliedly (as where payment is made after the date of maturity) or expressly, the dispensation is operative only as regards the party waiving presentment and benefits only a holder in whose favour there has been a waiver.

Subparagraph (d)

5. As noted in the commentary to article 51, the death of the drawee, the maker or acceptor is not a ground for dispensation and in such a case, the holder must present the instrument for payment to the deceased's heir or to the person administering the deceased's estate. However, insolvency of the drawee, the maker or the acceptor, or the fact that he is a fictitious person or is without capacity to pay an instrument, or the fact that the drawee etc. is a corporate body or other legal entity which has ceased to exist are grounds dispensing with the necessity for presentment for payment.

Paragraph (3)

6. Protest for dishonour by non-acceptance of a bill entitles the holder to an immediate right of recourse. Consequently, such protest dispenses with the necessity for presentment for payment. Paragraph (3) does not apply where the drawer has stipulated on the bill that it must not be presented for acceptance: refusal by the drawee to accept such a bill does not constitute dishonour (cf. article 46 (2)).

Article 53

(1) If a bill is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note is not duly presented for payment, the endorsers and their guarantors are not liable thereon.

(3) Failure to present an instrument for payment does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

Relevant legislation

BEA — section 45.

UCC — sections 3-501 and 3-502.

ULB — article 53.

Cross reference

Due presentment for payment: article 51.

Commentary

1. Presentment for payment of a bill is one of the conditions precedent to the liability of parties prior to the holder. Therefore, non-presentment or failure to present the bill in accordance with the requirements of due pre-

sentment (article 51) deprives the holder of his right of recourse against prior parties. The drawee may of course accept the bill after maturity, and such an acceptance will make him liable to the holder and any party subsequent to the holder (article 38 (2)). Presentment for payment is not necessary to render the acceptor liable (cf. article 36 (2)) or the guarantor of the drawee.

2. Presentment for payment of a note is not necessary in order to render the maker liable (cf. article 35 (1)) or his guarantor. However such presentment is a condition precedent to the liability of the endorsers and their guarantors.

Article 54

(1) An instrument is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment or when the holder cannot obtain the payment to which he is entitled under this Convention;

(b) If presentment for payment is dispensed with pursuant to article 52 (2) and the instrument is unpaid at maturity.

(2) If a bill is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the drawer, the endorsers and their guarantors.

(3) If a note is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the endorsers and their guarantors.

Relevant legislation

BEA — section 47.

UCC — section 3-507.

ULB — article 43.

Cross references

Due presentment for payment: article 51.

Dispensation of presentment for payment: article 52 (2).

Payment to which the holder is entitled: articles 69, 70 and 71.

Commentary

Paragraph (1)

1. Article 54 states when an instrument is dishonoured by non-payment. Paragraph 1 (a) deals with actual dishonour by non-payment: when payment is refused or the holder cannot obtain the payment to which he is entitled. Paragraph 1 (b) deals with constructive dishonour by non-payment: when presentment for payment is dispensed with under article 52 (2).

Payment to which the holder is entitled

2. Pursuant to articles 69 and 70 the holder may refuse to take partial payment and refuse to take payment in a place other than the place where the instrument was presented for payment in accordance with article 51. Therefore, the refusal by the holder to take such payment results in dishonour by non-payment.

3. Pursuant to article 71 the refusal of the holder to take payment of an instrument, denominated in foreign currency or to be paid in a specified currency, in local currency results in dishonour by non-payment.

Paragraphs (2) and (3)

4. The effect of dishonour by non-payment is that the holder is, subject to any necessary protest (cf. article 55), entitled to exercise a right of recourse against the drawer, the endorsers and the guarantors of the drawer and endorsers in the case of a bill and against the endorsers and the guarantors of the endorsers in the case of a note.

Section 3. Recourse

A. PROTEST

Article 55

If an instrument has been dishonoured by non-acceptance or by non-payment, the holder may exercise a right of recourse only after the instrument has been duly protested for dishonour in accordance with the provisions of articles 56 to 58.

Relevant legislation

BEA — sections 48 and 51 (2).

UCC — section 3-501 (2) and (3).

ULB — article 44.

Cross references

Dishonour by non-acceptance: article 50.

Dishonour by non-payment: article 54.

Holder: articles 4 (6) and 14.

Protest for dishonour: articles 56 to 58.

Commentary

1. The effect of dishonour by non-acceptance or by non-payment is that it entitles the holder to a right of recourse against the drawer, endorsers and guarantors. The making of a protest is necessary in order for the holder to be entitled to exercise that right. Protest where protest is necessary is a condition precedent to the liability of the drawer, endorsers and guarantors. The acceptor and his guarantor remain liable on a bill, and the maker and his guarantor on a note, irrespective of whether the bill or

note was presented for payment or protested for non-payment.

Protest and notice of dishonour

2. Under article 44 of the ULB, non-acceptance or non-payment must be evidenced by an authenticated act (protest for non-acceptance or non-payment). Questions as to the form of protest are left to the law of the place in which the protest must be drawn up. The Geneva Convention providing a Uniform Law for Bills of Exchange and Promissory Notes, in article 8 of annex II (reservations), permits a Contracting State to "prescribe that protest to be drawn up in its territory may be replaced by a declaration dated and written on the bill itself, and signed by the drawee, except where the drawer stipulates in the body of the bill of exchange itself for an authenticated protest".

3. Under Anglo-American law the exercise of the right of recourse consequent upon dishonour requires, as a general rule, notice of dishonour. If notice of dishonour is not given the drawer and endorsers in the case of a bill and the endorsers in the case of a note are discharged (cf. BEA section 48; UCC section 3-501, but see section 3-501 (2) (b) as regards the drawer). Protest is required only in the case of foreign bills of exchange (cf. BEA section 51 (1); UCC section 3-501 (3)).

4. Under this Convention the exercise of a right of recourse is conditional upon effectuating protest and failure to protest results in the discharge of any endorser of a bill or note, the drawer of a bill, and their guarantors. Notice of dishonour is, under this Convention, not a condition precedent to liability of parties secondarily liable but may give rise to an action for damages suffered by a party because of not having received notice (cf. article 64).

Article 56

(1) A protest is a statement of dishonour drawn up at the place where the instrument has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

(a) The person at whose request the instrument is protested;

(b) The place of protest; and

(c) The demand made and the answer given, if any, or the fact that the drawee or the acceptor or the maker could not be found.

(2) A protest may be made:

(a) On the instrument itself or on a slip affixed thereto (*allonge*); or

(b) As a separate document, in which case it must clearly identify the instrument that has been dishonoured.

(3) Unless the instrument stipulates that protest must be made, a protest may be replaced by a declaration written on the instrument and signed and dated by the drawee or the acceptor or the maker, or, in the case of an instrument domiciled with a named person for payment, by that named person; the declaration must be to the effect that acceptance or payment is refused.

(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purpose of this Convention.

Relevant legislation

BEA — section 51 (7).

UCC — section 3-509.

ULB — article 44; article 8 of annex II of the Geneva Convention of 1930.

Cross references

Protest as a condition precedent to the liability of parties: articles 55 and 59.

Dishonour: articles 50 and 54.

Commentary

1. Under article 56 protest may be made (a) in the form of a written statement, on the instrument itself or in a separate document, signed by a person authorized by the law of the place of dishonour to certify dishonour or (b) in the form of a written declaration on the instrument, signed by the person dishonouring it, to the effect that acceptance or payment mentioned under (a) above and paragraphs (3) and (4) with the declaration written on the instrument mentioned under (b) above.

2. The object of protest is to provide proof that the instrument was duly presented for acceptance or for payment and of dishonour by the drawee or the acceptor or the maker consequent upon such presentment. However, if presentment for acceptance or for payment is dispensed with under articles 48 or 52 (2), protest for dishonour by non-acceptance or non-payment is also dispensed with (cf. article 58 (2) (d)).

3. Pursuant to article 66 the holder in a recourse action may recover from any party liable any expenses of protest.

4. If the holder of a bill takes a partial acceptance (cf. article 39 (3)) he must protest the bill as to the balance of its amount. Similarly, if the holder of an instrument takes partial payment (cf. article 69 (2)) he must protest the instrument as to the balance of its amount.

5. Protest is unnecessary to render liable the acceptor of a bill (cf. article 36 (2)) or the maker of a note (cf. article 35 (1)), the guarantor of either (cf. article 43 (1)), or the guarantor of the drawee (cf. article 59 (3)).

Article 57

(1) Protest for dishonour of a bill by non-acceptance must be made on the day on which the bill is dishonoured or on one of the two business days which follow.

(2) Protest for dishonour of an instrument by non-payment must be made on the day on which the instrument is dishonoured or on one of the two business days which follow.

Relevant legislation

BEA — sections 51 (4) and 93.

UCC — section 3-509 (4) and (5).

ULB — article 44.

Cross references

Form of protest: article 56.

Dishonour by non-acceptance: article 50.

Dishonour by non-payment: article 54.

Commentary

Article 57 lays down the time-limits within which an instrument must be protested for dishonour. Failure to observe these time-limits deprives the holder of his right of recourse against parties other than the acceptor or the maker or their guarantors or the guarantor of the drawee.

Article 58

(1) Delay in protesting an instrument for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-acceptance or by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;

(c) As regards the drawer of a bill, if the drawer and the drawee or the acceptor are the same person;

(d) If presentment for acceptance or for payment is dispensed with in accordance with article 48 or 52 (2).

Relevant legislation

BEA – section 51 (9).
 UCC – section 3-511.
 ULB – article 54.

Cross reference

Time-limit within which protest must be made: article 57.

*Commentary***Paragraph (1)**

1. When delay in protesting an instrument for dishonour is excused the liability of parties is not affected on the ground that there was no protest. Delay is excused when the holder is prevented from effecting protest by circumstances beyond his control which he could neither avoid nor overcome. When the cause of delay ceases to operate protest must be made with reasonable diligence. However, if such cause continues to operate beyond 30 days from the date of dishonour, protest is altogether dispensed with and a right of recourse may be exercised against parties secondarily liable on the instrument.

Paragraph (2)

2. Paragraph (2) states the cases where protest is dispensed with. The effects of waiver of protest by the drawer, his endorser or guarantor on or off the instrument are, as regards the person or party waiving protest and the holder whom the waiver benefits, identical to the effects of a waiver of presentment for payment (see paragraph 4 of the commentary to article 52).

3. Where the drawer and the drawee or acceptor are the same person protest is dispensed with as regards the drawer by reason of the fact that the drawer having dishonoured the bill in his capacity as drawee or acceptor cannot require proof of the dishonour.

Article 59

(1) If a bill which must be protested for non-acceptance or for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note which must be protested for non-payment is not duly protested, the endorsers and their guarantors are not liable thereon.

(3) Failure to protest an instrument does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

Relevant legislation

BEA – section 51 (2).
 UCC – sections 3-501 (3) and (4), and 3-502.
 ULB – article 53.

Cross reference

Due protest: articles 56 and 57.

Commentary

1. Failure on the part of the holder to make due protest under articles 56 and 57, unless excused or dispensed with under article 58, results in the absence of liability of parties secondarily liable on the instrument.

2. The liability of the acceptor, the maker, their guarantors and the guarantor of the drawee is a primary liability and no protest is necessary to render any of them liable on the instrument.

B. NOTICE OF DISHONOUR*Article 60*

(1) The holder, upon dishonour of a bill by non-acceptance or by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.

(2) The holder, upon dishonour of a note by non-payment, must give notice of such dishonour to the endorsers and their guarantors.

(3) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the instrument.

(4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the instrument against the party notified.

Relevant legislation

BEA – section 49.
 UCC – sections 3-501 and 3-508.
 ULB – article 45.

Cross references

Dishonour by non-acceptance: article 50.
 Dishonour by non-payment: article 54.

Commentary

1. As noted in the commentary to article 55 (paragraphs 2-4), the Convention follows the approach of the ULB in considering protest as one of the conditions precedent to the liability of parties secondarily liable. In line with the ULB, the duty of the holder to give due notice of dishonour is not a condition precedent to the liability of the parties entitled to notice but the holder is liable for damages which such parties may have suffered as a consequence of his failure to give due notice. Article 60 should therefore be read in conjunction with article 64 which states the consequences of failure to give due notice of dishonour.

2. According to article 60 notice of dishonour must be given by the holder to any prior party secondarily liable and by any party, who has himself received notice, to the party immediately preceding him and liable on the instrument. However, the notice operates for the benefit of any party who has a right of recourse against the party who received notice of dishonour.

Example. The payee endorses the bill to A. A endorses it to B, B to C and C to D. Upon dishonour of the bill by the drawee, D must, under article 60, give notice of dishonour to the drawer, the payee, A, B and C and failure to do so will render D liable for damages to the party paying the bill. When C receives notice of dishonour from D, C, in turn, must give notice of dishonour to B. Notice sent by D to the drawer enures for the benefit of the payee, A, B and C.

3. The rule stated in paragraph (3) specifies that notice must be given to an immediately preceding party who is liable on the instrument. Therefore, in the example given above (paragraph 2), if B had endorsed the bill without recourse, C, having received notice from D, must now give notice to A.

Article 61

(1) Notice of dishonour may be given in any form whatever and in any terms which identify the instrument and state that it has been dishonoured. The return of the dishonoured instrument is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.

(2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.

(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

Relevant legislation

BEA — section 49 (5), (6), (7) and (15).
UCC — section 3-508 (3) and (4).
ULB — article 45.

Cross references

Notice of dishonour: articles 60 to 64.
Dishonour by non-acceptance: article 50.
Dishonour by non-payment: article 54.

Commentary

1. This article retains the substance of the relevant provisions of the BEA, UCC and ULB. It is not necessary that the notice be given in any particular form. It may be given in writing or orally provided that the communica-

tion identifies the instrument and conveys the fact that it has been dishonoured by non-acceptance or non-payment. The return of the dishonoured instrument with an indication on or off the instrument that it was dishonoured constitutes sufficient notice.

2. Written notice is duly given when it is sent even though it is not received by the addressee. However, the burden of proof that due notice has been given falls on the person who, under article 60, is obliged to give notice.

Article 62

Notice of dishonour must be given within the two business days which follow:

- (a) The day of protest or, if protest is dispensed with, the day of dishonour; or
- (b) The receipt of notice given by another party.

Relevant legislation

BEA — section 49 (12).
UCC — section 3-508 (2).
ULB — article 45.

Cross references

Time-limit for protest: article 57.
Protest dispensed with: article 58 (2).

Commentary

1. Article 62 sets forth the period of time within which notice of dishonour can duly be given. It is commercially desirable that parties liable on the instrument as a consequence of dishonour be advised without delay that they have become liable. Inquiries amongst banking and trade circles have led to the conclusion that a period of three days (i.e., the day of protest or, where protest is dispensed with, the day of dishonour, and the two business days that follow) is an adequate and practicable period in which to give notice; it will, in most cases, enable the holder's agent in a foreign country where the instrument was payable to inform his principal of the dishonour and will enable the holder to give notice to prior parties. Thus, if the instrument is payable on a Monday the holder may present it not only on that day but also on Tuesday (cf. article 51 (e)). According to article 57 protest must be made on the day on which the instrument is dishonoured (on Monday or Tuesday as the case may be) or on one of the two business days which follow (on Wednesday or Thursday at the latest as the case may be). Pursuant to article 62 notice of dishonour may duly be given on Wednesday or Thursday (in the above example) or within the two business days which follow, i.e. either Friday or Monday of the following week.

2. When a party secondarily liable has received notice he in turn may duly give notice on the day on which he

received notice or on one of the two business days which follow the day of receipt of notice.

Article 63

(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(2) Notice of dishonour is dispensed with:

(a) If after the exercise of reasonable diligence notice cannot be given;

(b) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:

- (i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;
- (iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made.

(c) As regards the drawer of the bill, if the drawer and the drawee or the acceptor are the same person.

Relevant legislation

BEA — section 50.

UCC — section 3-511.

Cross reference

Time-limit for giving notice: article 62.

Commentary

1. Paragraph (1) sets forth the ground justifying delay in giving notice of dishonour. The provision is similar to paragraph (1) of article 52 in respect of delay in making presentment for payment and paragraph (1) of article 58 in respect of delay in protesting an instrument. When delay is excused the liability of the person who is obliged to give notice (i.e. for damages, cf. article 64) is not affected on the ground that there was no due notice.

2. Paragraph (2) states the cases in which notice of dishonour is dispensed with. In such cases the person obliged to give notice is not liable for damages under article 64.

3. As to the legal effects of waiver on or off the instrument see the commentary to article 52 (paragraph 4).

Article 64

Failure to give notice of dishonour renders a person who is required to give such notice under article 60 to a party who is entitled to receive such notice liable for any damages which that party may suffer from such failure, provided that such damages do not exceed the amount referred to in article 66 or 67.

Relevant legislation

BEA — section 48.

UCC — section 3-501 (2).

ULB — article 45.

Cross references

By whom and to whom notice of dishonour must be given: article 60.

Form of notice: article 61.

When to give notice: article 62.

Delay in giving notice: article 63 (1).

Notice dispensed with: article 63 (2).

Commentary

1. The consequences of failure to give notice differ sharply between the Anglo-American law and the Geneva Uniform Law. Under the BEA and the UCC, the giving of notice of dishonour is necessary to charge parties and is thus a condition precedent to their liability on the bill to the holder or to any other party who has acquired a right of recourse against them. Under the ULB, failure to give notice does not discharge the drawer's or prior endorsers' liability on the bill, but merely makes the party who failed to give notice liable for the damages resulting from such failure. Under the ULB, therefore, a holder or any other party who acquires a right of recourse, but failed to give notice, may exercise such right of recourse upon due protest.

2. Article 64 follows the ULB approach. Due notice of dishonour is not a condition precedent to liability of secondary parties on the instrument but renders the person who failed to give notice liable for damages resulting from such failure. The amount of damages is limited to the amount of the instrument and may include the interest and expenses due under article 66 or 67.

Section 4. Amount payable

Article 65

The holder may exercise his rights on the instrument against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

Relevant legislation

ULB – article 47.

Cross references

Parties liable on the instrument: Section 2 of Chapter Four.

Liability of the drawer: article 34.

Liability of the maker: article 35.

Liability of the acceptor: article 36 (2).

Liability of the endorser: article 40.

Liability of the guarantor: article 43.

Commentary

The liability of the parties to an instrument and the conditions in which they become liable are stated in Section 2 of Chapter Four of this Convention. Article 65 is intended to make clear that the holder in exercising his rights on the instrument may proceed against all parties together or against all parties individually or against any individual party without being required to observe the order in which they have become liable. The right of recourse against the drawer, acceptor, endorsers and guarantors (in the case of a bill) and the maker, endorsers and guarantors (in the case of a note) is conditioned upon the holder's having duly presented the instrument and protested the dishonour, except in those cases where presentment and protest is dispensed with.

Article 66

(1) The holder may recover from any party liable:

(a) At maturity: the amount of the instrument with interest, if interest has been stipulated for;

(b) After maturity:

(i) The amount of the instrument with interest, if interest has been stipulated for, to the date of maturity;

(ii) If interest has been stipulated to be paid after maturity, interest at the rate stipulated, or in the absence of such stipulation, interest at the rate specified in paragraph (2), calculated from the date of presentment on the sum specified in paragraph (1) (b) (i);

(iii) Any expenses of protest and of the notices given by him;

(c) Before maturity:

(i) The amount of the bill with interest, if interest has been stipulated for, to the date of payment, subject to a discount from the date of payment to the date of maturity, calculated in accordance with paragraph (3);

(ii) Any expenses of protest and of the notices given by him.

(2) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the instrument is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the instrument is payable. In the absence of any such rates, the rate of interest shall be [] per cent per annum.

(3) The discount shall be at the official rate (discount rate) or other similar appropriate rate effective on the date when recourse is exercised at the place where the holder has his principal place of business, or if he does not have a place of business his habitual residence, or if there is no such rate then at the rate of [] per cent per annum.

Relevant legislation

BEA – section 57.

UCC – no equivalent provision, but see section 3-122.

ULB – article 48.

Cross references

Holder: articles 4 (6) and 14.

Maturity: article 4 (9).

Stipulation of interest: article 6.

Commentary

1. Article 66 lays down what sums of money are owed to the holder at maturity and what sums of money he may recover, in a recourse action upon dishonour, from a party liable to him, after maturity (upon dishonour by non-payment) and before maturity (upon dishonour by non-acceptance). At maturity the holder is entitled to be paid the amount of the instrument and any interest (cf. article 6). According to article 69 the holder is not obliged to take partial payment. Upon the dishonour of an instrument by non-acceptance or non-payment the holder may recover from any party liable on the instrument (cf. articles 50 (2) and 54 (2) and (3)). Paragraph (1) (b) and (c) lay down what the holder may recover in these cases. After maturity the holder may recover the amount payable at maturity; delay interest at the rate stipulated or, if not stipulated, at the rate specified in paragraph (2) calculated from the date of presentment on the amount payable at maturity; and any expenses consequent upon the making of protest and the giving of any notice of dishonour. Before maturity the amount of the instrument is subject to a discount but interest, if stipulated, runs to the date of payment.

2. The expenses referred to in paragraph (1) (b) (iii) and (1) (c) (ii) do not include bank charges, costs of collection and lawyer's fees but only any legitimate and

necessary expenses actually incurred with the making of protest or the giving of notice of dishonour.

3. Paragraphs (2) and (3) specify the rate at which interest is to be calculated when the holder recovers in a recourse action upon dishonour by non-payment. The actual percentage points are placed between brackets for further consideration at a future conference of plenipotentiaries which may be called to conclude a convention on the basis of the UNCITRAL draft Convention.

Article 67

A party who pays an instrument in accordance with article 66 may recover from the parties liable to him:

- (a) The entire sum which he was obliged to pay in accordance with article 66 and has paid;
- (b) Interest on that sum at the rate specified in article 66, paragraph (2), from the date on which he made payment;
- (c) Any expenses of the notices given by him.

Relevant legislation

BEA – section 57.

UCC – no equivalent provision, but see section 3-122.

ULB – article 49.

Commentary

1. Article 67 lays down what sums of money a party secondarily liable who has paid an instrument may recover from the acceptor or the maker, the drawer, prior endorsers, and their guarantors. Thus, if the drawer has taken up and paid a bill he may recover from the acceptor the sum the drawer was compelled to pay pursuant to article 66 and interest on that sum from the date on which he made payment.

2. For the purposes of this article it is not necessary that when the party paid the instrument it was endorsed to him or endorsed in blank (cf. article 21).

CHAPTER SIX. DISCHARGE

Section 1. Discharge by payment

Article 68

(1) A party is discharged of liability on the instrument when he pays the holder, or a party subsequent to himself who has paid the instrument and is in possession thereof, the amount due pursuant to article 66 or 67:

- (a) At or after maturity; or
 - (b) Before maturity, upon dishonour by non-acceptance.
- (2) Payment before maturity other than under paragraph (1) (b) of this article does not discharge the party making the payment of his liability on the instrument

except in respect of the person to whom payment was made.

(3) A party is not discharged of liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(4) (a) A person receiving payment of an instrument must, unless agreed otherwise, deliver:

- (i) To the drawee making such payment, the instrument;
- (ii) To any other person making such payment, the instrument, a receipted account, and any protest.

(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the instrument to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 54.

(c) If payment is made but the person paying, other than the drawee, fails to obtain the instrument, such person is discharged but the discharge cannot be set up as a defence against a protected holder.

Relevant legislation

BEA – sections 59 and 60.

UCC – section 3-603.

ULB – articles 39, 40 and 50.

Cross references

Maturity: articles 4 (9) and 8.

Dishonour by non-acceptance: article 50.

Knowledge: article 5.

Claim by third person: article 25 (2, 3).

Commentary

1. A person who signs an instrument assumes the obligation to pay the instrument if certain conditions are met (see Chapter Four, Section 2). If a party pays the instrument in accordance with his undertaking, he is discharged of his liability. Article 68 lays down when payment constitutes a discharge of liability.

Paragraph (1)

“Discharged of liability on the instrument”

2. “Discharge” is a technical term used in the Convention for the termination of an undertaking on the instrument. Thus, discharge presupposes liability of the person paying. There is therefore no discharge if the drawee pays since he is not liable on the bill. Also, there is no discharge if a party secondarily liable whose liability has not crys-

tallized for lack of presentment and protest pays the instrument.

3. The fact that a party is discharged of liability runs with the instrument and has effect against any person subsequent to him; however, the discharge cannot be invoked against a protected holder (cf. article 26 (1) (a)).

4. Payment discharges not only the payer of his liability but also, according to article 73 (1), all parties who have a right of recourse against him. A further effect is that any guarantor of the payer or of another party to whom the payer is liable is discharged to the same extent (cf. article 43 (1)).

5. Payment of an instrument is often intended to discharge an obligation underlying the instrument. Article 68 does not deal with the effect of payment of the instrument on the underlying transaction, nor does it deal with the effect of dishonour by non-payment on the underlying transaction. Article 68 only deals with the consequences of payment on the liability of parties on the instrument itself.

"Pays the holder"

6. Discharge under article 68 is consequent upon payment, i.e. by the payment of money as defined in article 4 (1). Thus, it would not suffice to pay in kind or to give another negotiable instrument.

7. Payment is to be made to the person who is the holder as defined in article 14. Thus, for example, payment to the payee in possession of the instrument is payment to the holder. The same is true in respect of payment to a person in possession of an instrument on which the last endorsement is in blank and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged. On the other hand, if an instrument on which the last endorsement is a special endorsement is delivered to a person other than the person to whom it is endorsed, payment to that person is not payment to the holder and therefore, does not discharge the payer under article 68.

8. There is one special set of circumstances where payment to a "non-holder" constitutes discharge of liability: if a holder has lost the instrument, he may nevertheless claim payment under certain conditions (see article 74), and payment to such ex-holder discharges the party paying (article 79). In this context, reference should be made to article 74 (2) (d), according to which, under certain conditions, payment may be effected by way of deposit with a court or other competent body.

"A party subsequent to himself who has paid the instrument and is in possession thereof"

9. The person receiving payment is usually the holder. If a bill is dishonoured by the drawee or acceptor, the holder has a right of recourse against the drawer, the

endorsers and their guarantors. Similarly, if a note is dishonoured by the maker, the holder has a right of recourse against the endorsers and the guarantors. When the drawer of a bill, or the guarantor of a party to a bill or a note, pays, the instrument must be delivered to the payer. In the absence of an endorsement to the payer — and such endorsement is not necessary — the payer, though in possession of the instrument, is not a holder. However, such payer, if in possession of the instrument, has a right to payment against prior parties. Article 68 provides that payment by such parties to him discharges the party paying of his liability on the instrument.

"At or after maturity" (subparagraph (a))

10. Since the undertaking of a party is to pay at maturity, he is, accordingly, discharged if he pays the amount then due at or after maturity.

"Before maturity" (subparagraph (b) and paragraph (2))

11. If a party pays an instrument before he is obliged to pay, i.e. before maturity, he is not discharged of his liability. However, such payment may be invoked against the person to whom payment was made.

12. If a bill was presented for acceptance and was dishonoured by non-acceptance, the holder has an immediate right of recourse against any party to the instrument. Paragraph (1) (b) provides that payment by such party discharges him of liability.

Paragraph (3)

13. Paragraph (3) deals with the question whether discharge may be affected or prevented by a claim of a third party. If the party paying had no knowledge of such claim, payment by such party constitutes discharge, provided that the other requirements of article 68 are met. Among other things the party must pay to the holder and not, for example, to a person in possession of an instrument on which there appears an interrupted series of endorsements. Even if the payer did not know that one of the endorsements was forged, he is not discharged since he did not pay to the holder. Thus, for there to be discharge, a party must examine the regularity of the endorsements but is not required to examine their genuineness.

14. If, on the other hand, the party paying had knowledge of a claim of a third party, the decisive factor is whether or not he was under an obligation to pay. Thus, he is discharged if he paid a protected holder under circumstances in which he, the payer, could not have raised the defence of *ius tertii* in an action on the instrument by the protected holder (cf. article 26 (2)).

15. In respect of payment of an instrument to which there is a claim by a third party, payment to the holder who is not a protected holder discharges the payer only if he

cannot raise the defence of *ius tertii* under article 25 (3) against such holder. This is so because in such a case the payer is obliged to pay and payment by him should therefore discharge him of liability.

Example A. The bill which the payee endorsed in blank is stolen from him. The thief is therefore a holder. Payment by the drawer to the thief with knowledge of the theft does not discharge the drawer.

Example B. A induces the payee to endorse the bill to A. A demands payment from the acceptor who knows about the fraud. The payee has not asserted a claim to the bill. Payment by the acceptor to A discharges the acceptor of liability.

Paragraph (4), subparagraph (a)

16. A holder who receives payment from a party or the drawee must deliver the instrument to the payer. The payer's right to possession is justified by the fact that, if the instrument remained in the hands of the person receiving payment and that person transferred the instrument to a protected holder, the payer, if a party, would be obliged to pay the instrument a second time upon presentment by the protected holder (cf. articles 26, 68 (4) (c)).

17. If the payer is a party, the person receiving payment must deliver, in addition to the instrument, a receipted account and any protest (subparagraph (ii)). These documents are necessary to enable the payer to exercise rights on the instrument against parties liable to him (cf. article 67).

Subparagraph (b)

18. The person from whom payment is demanded is not required to pay if the instrument is not delivered to him. Withholding payment in these circumstances does not constitute dishonour by non-payment. Consequently, in such a case the person who refuses to deliver the instrument would not be entitled to exercise a right of recourse against parties liable to him. However, if the instrument is not delivered because it has been lost, the special rules on lost instruments apply (articles 74-79).

Subparagraph (c)

19. If the person from whom payment is demanded pays the instrument although it is not delivered to him, such payment constitutes a discharge of liability on the instrument but such discharge may not be raised as a defence against a protected holder (cf. article 26).

Example C. The maker issues a note to the payee. The payee endorses the note to A who endorses it to B. B presents the note for payment to the maker who refuses payment. Upon protest, B asks payment from the payee. The payee pays but B retains the note. Subsequently, B requests payment from A. A may raise as a defence against B that

the instrument was paid by the payee, and that he therefore is discharged of liability on the note (cf. article 73).

Example D. The maker issues a note to the payee. The payee endorses it to A who endorses it to B. B presents the note for payment to the maker. The maker pays but B retains possession of the note. B endorses the note to C who is not a protected holder. C presents the note for payment to the maker. Because C is not a protected holder, the maker may raise the defence that he paid the note and that such payment constitutes a discharge. If, on the other hand, C is a protected holder, then payment by the maker cannot be raised as a defence, neither by the maker nor by parties prior to C.

Article 69

(1) The holder is not obliged to take partial payment.

(2) If the holder who is offered partial payment does not take it, the instrument is dishonoured by non-payment.

(3) If the holder takes partial payment from the drawee or the acceptor or the maker:

(a) The acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; and

(b) The instrument is to be considered as dishonoured by non-payment as to the amount unpaid.

(4) If the holder takes partial payment from a party to the instrument other than the drawee, the acceptor or the maker:

(a) The party making payment is discharged of his liability on the instrument to the extent of the amount paid; and

(b) The holder must give such party a certified copy of the instrument and of any authenticated protest.

(5) The drawee or a party making partial payment may require that mention of such payment be made on the instrument and that a receipt therefor be given to him.

(6) If the balance is paid, the person who receives it and who is in possession of the instrument must deliver to the payor the receipted instrument and any authenticated protest.

Relevant legislation

BEA — section 47.

UCC — section 3-507.

ULB — article 39.

Cross references

Discharge by payment: article 68.

Dishonour by non-payment: article 54.

Authenticated protest: article 56 (3).

Commentary

1. A party's undertaking is to pay the instrument in full as provided in articles 66 and 67. Accordingly, a holder is entitled to receive the full amount; he is not obliged to take partial payment which would impose on him the burden of having to claim the remaining part of the sum from another party.

2. Consequently, if he does not accept partial payment, the instrument is dishonoured by non-payment and the holder has rights against parties liable to him for the full amount. If, however, he elects to take partial payment, any party liable is discharged *pro tanto* (paragraphs (3) (a), (4) (a) and article 73) and the instrument is dishonoured to the extent of the amount unpaid (paragraph (3) (b)).

3. If partial payment is made the payer is not entitled to receive the instrument since the holder needs it in order to obtain payment of the amount unpaid. In order to give the payer the protection which he would have by receiving the instrument (article 68 (4)), he may require that his partial payment be stated on the instrument and that he be given a receipt for it. As regards payment of the remaining part of the instrument, the payer of it is entitled to receive the receipted instrument.

4. If partial payment is made by a person other than the acceptor, maker or drawee, that person has, as a party secondarily liable, a right of recourse. Since he does not receive the instrument (see above, paragraph 3), he needs some other document to exercise his right of recourse as to the amount paid by him. Therefore, the holder must give such party a certified copy of the instrument and of any protest, if protest was made as a separate document (paragraph (4) (b)).

Article 70

(1) The holder may refuse to take payment in a place other than the place where the instrument was presented for payment in accordance with article 51.

(2) If in such case payment is not made in the place where the instrument was presented for payment in accordance with article 51, the instrument is considered as dishonoured by non-payment.

Relevant legislation

BEA — section 45 (4).

UCC — section 3-504.

Cross references

Presentment for payment: article 51.

Dishonour by non-payment: article 54.

Commentary

Article 51 specifies the proper place for due presentment for payment (see paragraphs (g) and (h)). Since it is

commercially reasonable to require that payment be made at such place, article 70 provides that an offer to pay the instrument in some other place may be rejected by the holder, who may then treat the instrument as dishonoured by non-payment. However, if the holder accepts payment at another place, the payer is discharged of liability on the instrument according to article 68.

Article 71

(1) An instrument must be paid in the currency in which the amount of the instrument is expressed.

(2) The drawer or the maker may indicate on the instrument that it must be paid in a specified currency other than the currency in which the amount of the instrument is expressed. In that case:

(a) The instrument must be paid in the currency so specified;

(b) The amount payable is to be calculated according to the rate of exchange indicated on the instrument. Failing such indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of maturity:

(i) Ruling at the place where the instrument must be presented for payment in accordance with article 51 (g), if the specified currency is that of that place (local currency); or

(ii) If the specified currency is not that of that place, according to the usages of the place where the instrument must be presented for payment in accordance with article 51 (g);

(c) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the instrument, according to that rate;

(ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of dishonour or on the date of actual payment;

(d) If such an instrument is dishonoured by non-payment, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the instrument, according to that rate;

(ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of maturity or on the date of actual payment.

(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-acceptance or non-payment.

(4) The rate of exchange ruling at a certain date is the rate of exchange ruling, at the option of the holder, at the place where the instrument must be presented for payment in accordance with article 51 (g) or at the place of actual payment.

Relevant legislation

BEA — section 72 (4).
UCC — section 3-107 (2).
ULB — article 41.

Cross references

Currency: article 4 (11).
Rate of exchange indicated on the instrument: article 6 (d).
Dishonour by non-acceptance: article 50.
Dishonour by non-payment: article 54.

Commentary

1. This article lays down rules in respect of payment of an instrument denominated in a currency which is not that of the place of payment. In respect of such instruments the following questions arise:

(a) May a person liable on the instrument discharge that liability by paying in the currency of the place of payment or must he pay in the currency in which the amount of the instrument is expressed?

(b) If payment is made at maturity in local currency, what should be the rate of exchange between the currency in which the amount of the instrument is expressed and the currency of the place of payment?

(c) If the instrument is dishonoured and a change in the rate of the specified currency *vis-à-vis* the currency of the place of payment takes place after the date of dishonour, what are then the obligations of the parties liable on the instrument?

Paragraph (1)

2. When an instrument is drawn or made payable in a currency which is not that of the place of payment, in which currency ("foreign" or "local") should payment be made at maturity in order to discharge the payer of his liability on the instrument? In theory, one can envisage the following answers:

(a) The party liable must pay in the specified foreign currency. The rationale behind this approach is that when an instrument is drawn or made payable in a foreign currency, the parties manifest thereby their intention that the instrument be paid in that currency;

(b) The party liable must pay in local currency. The rationale behind this approach is that the mere specification of a foreign currency on an instrument does not necessarily

manifest an intention that the instrument should be paid in such currency. Such intention should be manifested by an express provision requiring payment in the specified foreign currency. According to this view, the specification of the amount of the instrument in a foreign currency serves only the purpose of providing a criterion according to which the value of a local currency is to be measured;

(c) The party liable has an option to pay in either local or foreign currency. The rationale behind this approach is that the fact that an instrument was drawn or made in a foreign currency should permit the person liable to pay either in that currency or in the currency of the place of payment.

(d) The holder has an option to demand payment in either local or foreign currency. The rationale is that the absence of a strong and clear indication of the obligation to pay in foreign currency should operate in favour of the holder.

(3) Paragraph (1) states the basic rule that an instrument drawn or made payable in a currency other than that of the place of payment is, in the absence of an express stipulation to the contrary, to be paid in that currency. Enquiries made amongst banking circles revealed that under current commercial and banking practices instruments are frequently paid in the currency in which the amount of an instrument is expressed even though it is not stipulated on the instrument that payment be made in such currency. The rule, it is submitted, is a most suitable one at a time of frequent fluctuations between currencies.

4. It follows from the rule stated in paragraph (1) that if a drawee accepts to pay the bill of exchange, denominated in a specified currency, in the currency of the place of payment such acceptance would be a qualified acceptance which the holder would be at liberty either to take or to refuse. In the latter case the bill would be dishonoured by non-acceptance. Similarly, the refusal by the holder to take payment of the bill in local currency would result in dishonour of the bill by non-payment.

5. The rule is subject to exchange control regulations imposing restrictions on payment in a currency other than that of the place of payment (cf. article 72).

Paragraph (2) (a) and (b)

6. The drawer of a bill or the maker of a note may stipulate on the instrument that it is to be paid in a specified currency other than the currency in which the amount of the instrument is expressed. In such a case the instrument is to be paid in the specified currency. Thus if a bill is denominated in Swiss francs and contains a stipulation that it is to be paid in rubles, the instrument must be paid in rubles. Under article 6 (e) the sum so payable is deemed to be a definite sum for the purposes of article 1. In such a case the question arises as to what rate of exchange should be applicable. If a rate of exchange is indicated on the instru-

ment the amount payable is to be calculated according to that rate. Under article 6 (d) the sum so payable is deemed to be a definite sum for the purposes of article 1. If no rate of exchange is indicated on the instrument the amount payable is to be calculated according to the rate of exchange for sight drafts (or, in the absence of such rate, according to the appropriate established rate of exchange) on the date of maturity. The rate of exchange is the rate ruling at the place where the instrument must be presented for payment in accordance with article 51 (g) (see paragraph (2) (b) (i) and (ii)).

Paragraph 2 (c) and (d)

7. Where an instrument is dishonoured by non-acceptance the holder has, upon due protest (cf. article 55), an immediate right of recourse against prior parties (cf. article 50 (2)) and the instrument becomes due before maturity. In such a case the question arises as to what rate of exchange should prevail; the rate specified on the instrument (if so specified), that ruling on the date of dishonour, on the date of maturity (if payment is made at or after maturity) or on the date of actual payment. Similar questions arise where an instrument is dishonoured by non-payment. In this event, the holder has a right of recourse against the acceptor or the maker and, upon due protest (cf. article 55), against prior parties (cf. article 54 (2) and (3)). Also here the question arises as to what rate of exchange should prevail when payment is made: the rate specified on the instrument (if so specified), the rate ruling on the date of maturity or on the date of actual payment. In respect of both dishonour by non-acceptance and by non-payment, the further question arises whether provision should be made for one or several possible rates of exchange or whether the holder or the payer should be entitled to exercise an option between two or more of these rates and, if so, under what circumstances. Yet another question is whether the rules applicable to the rate of exchange should be the same for all parties liable on the instrument or whether a distinction should be made between parties primarily liable and parties secondarily liable. Lastly, the question arises whether the rate of exchange should be that prevailing at the place where the instrument should have been paid upon due presentment for payment or that prevailing at the place where payment is actually made.

8. Subparagraphs (c) (i) and (d) (i) provide that, in both cases of dishonour, if a rate of exchange is indicated on the instrument that rate prevails. If the rate of exchange is not indicated on the instrument, subparagraph (c) (ii) provides that in the event of dishonour by non-acceptance the holder has the option of demanding that payment be made at either the rate of exchange ruling on the date of dishonour or on the date of actual payment. In the event of dishonour by non-payment the holder has the option of demanding that payment be made at either the rate of exchange ruling on the date of maturity or on the date of

actual payment. The holder is given the option of choosing between two rates of exchange in order to protect him against any loss he may suffer because of speculation by the party liable.

Paragraph (3)

9. Under certain legal systems a holder may be awarded damages compensating him for loss suffered because of fluctuations in rates of exchange if such loss is caused by dishonour by non-acceptance or by non-payment. Paragraph (3) preserves such right to damages which a holder may have under the applicable law. It must be noted, however, that paragraph (3) does not create a statutory right entitling a holder to damages in the event of his suffering loss because of fluctuations in rates of exchange.

Paragraph (4)

10. This paragraph sets forth a rule as to the place which determines the rate of exchange if the amount payable is to be calculated according to a rate prevailing at a given date. Upon dishonour the holder has the option of choosing between the rate of exchange ruling at the place where the instrument must be presented for payment under article 51 (g) and that ruling at the place of actual payment.

Article 72

(1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party.

(2) (a) If, by virtue of the application of paragraph (1) of this article, an instrument drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment ruling at the place where the instrument must be presented for payment in accordance with article 51 (g);

(b) (i) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated, at the option of the holder, at the rate of exchange ruling on the date of dishonour or on the date of actual payment;

(ii) If such an instrument is dishonoured by non-payment, the amount is to be calculated, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment;

(iii) Paragraphs (3) and (4) of article 71 are applicable where appropriate.

Cross references

Currency: article 4 (11).
 Dishonour by non-acceptance: article 50.
 Dishonour by non-payment: article 54.

*Commentary**Paragraph (1)*

1. As noted in the commentary to article 71 (paragraph 5), the provisions regarding payment in a currency that is not the currency of the place of payment are subject to exchange control regulations imposing restrictions on payment in such currency. Therefore, article 72 sets forth a general provision to this effect. The regulatory provisions referred to in this article are not only those of the Contracting State itself but include those which the Contracting State is bound to enforce by virtue of international agreements to which it is a party. An example of the latter type of regulatory provisions is Article VIII, section 2 (b), of the Articles of Agreement of the International Monetary Fund according to which "exchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with [the Fund] Agreement shall be unenforceable in the territories of any member".

Paragraph (2)

2. This paragraph envisages situations where in accordance with article 71 an instrument is to be paid in a currency which is not the currency of the place of payment but where by virtue of the application of paragraph (1) of article 72 it is to be paid in local currency. For these situations paragraph (2) sets forth rules regarding the rate of exchange to be applied and on which date that are similar to the rules set forth in article 71 (2), (3) and (4).

*Section 2. Discharge of a prior party**Article 73*

(1) When a party is discharged wholly or partly of his liability on the instrument, any party who has a right of recourse against him is discharged to the same extent.

(2) Payment by the drawee of the whole or a part of the amount of a bill to the holder, or to any party who has paid the bill in accordance with article 66, discharges all parties of their liability to the same extent.

Relevant legislation

BEA — section 37.
 UCC — section 3-208.
 ULB — article 50.

Cross reference

Discharge: article 68.

Commentary

1. The discharge of a party of his liability on the instrument affects also the rights of parties subsequent to him. When a party signed the instrument he was entitled to assume that, if he paid the instrument, he would have a right of recourse against prior parties. The discharge of a prior party impairs this right of recourse. It is reasonable therefore that in such a case parties subsequent to the party discharged are also discharged.

Example. The payee endorses a bill to A who endorses it to B. Payment by the acceptor to B operates as a discharge of the drawer, the payee and A. Payment by the drawer operates as a discharge of the payee and A. Payment by the payee operates as a discharge of A.

2. Similarly, payment by the drawee discharges all parties of their liability (paragraph (2)).

3. Where payment is made only in part, the discharge of the subsequent parties is to the extent of that partial payment.

CHAPTER SEVEN. LOST INSTRUMENTS

Article 74

(1) When an instrument is lost, whether by destruction, theft or otherwise, the person who lost the instrument has, subject to the provisions of paragraph (2) of this article, the same right to payment which he would have had if he had been in possession of the instrument. The party from whom payment is claimed cannot set up as a defence against liability on the instrument the fact that the person claiming payment is not in possession thereof.

(2) (a) The person claiming payment of a lost instrument must state in writing to the party from whom he claims payment:

- (i) The elements of the lost instrument pertaining to the requirements set forth in article 1 (2) or 1 (3); for this purpose the person claiming payment of the lost instrument may present to that party a copy of that instrument;
- (ii) The facts showing that, if he had been in possession of the instrument, he would have had a right to payment from the party from whom payment is claimed;
- (iii) The facts which prevent production of the instrument.

(b) The party from whom payment of a lost instrument is claimed may require the person claiming payment to give security in order to indemnify him for any loss which

he may suffer by reason of the subsequent payment of the lost instrument.

(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms.

(d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost instrument, and any interest and expenses which may be claimed under article 66 or 67, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

Relevant legislation

BEA – section 70.

UCC – section 3-804.

Cross references

Defences against liability: articles 25, 26.

Discharge by payment: article 68.

Commentary

1. Under the Convention the rights on an instrument are vested in the holder, i.e. the payee or endorsee who is in possession of the instrument (cf. articles 4 (6) and 14). Thus, a holder when losing possession of the instrument is no longer a holder. The question, then, is what are the rights of such an “ex-holder”?

2. Legal systems generally recognize that the loss of an instrument does not entail loss of the rights thereon. However, they differ as to the procedures and conditions under which the ex-holder may exercise his rights. Most legal systems of civil law tradition provide for a special cancellation procedure: upon request by the ex-holder, accompanied by a statement setting forth the essential elements of the lost instrument and the circumstances of its loss, the court may issue a cancellation order which terminates the validity and effect of the lost instrument and serves the ex-holder as a substitute for the lost instrument. On the other hand, under the BEA and the UCC, no such cancellation procedure is required. The ex-holder may maintain an action on the lost instrument but may be required to give security to the payer so as to cover the risk of the payer of having to pay twice, i.e. to the ex-holder and to a holder in due course of the lost instrument.

3. The latter approach has been adopted in the Convention which requires the giving of security and of a written statement by the ex-holder (article 74 (2)). The institution of cancellation, as embodied in national laws of civil law

tradition, seemed less appropriate in the context of an international negotiable instrument because cancellation takes place by a judicial decision which would not necessarily be known in countries other than the country in which it was rendered.

Paragraph (1)

4. Article 74, paragraph (1), expresses the idea, common to all systems, that the loss of an instrument does not result in loss of the rights on it. Loss of the instrument is to be understood in a wide sense. It includes, in addition to normal loss, any loss by destruction, theft or any other dispossession against the possessor's will.

5. Under paragraph (1), the ex-holder has, subject to the provisions of paragraph (2), the same right to payment as he would have had if he had been in possession of the instrument. Retention of his legal position means not only that he retains his rights on the instrument but also that he retains any burden, i.e. to make presentment (cf. article 53 (1), to make protest (cf. article 55), to give notice of dishonour (cf. article 60 (1)), and continues to be subject to the same claims and defences as before.

Example A. The drawer draws a bill payable to payee (P), P endorses it to A who loses it. Under article 74, paragraph (1), A has the right to claim payment from the drawer and P; but, before he may claim payment he must make presentment for payment and any necessary protest if payment is refused (article 77). In an action brought against the drawer and P, each party may raise any defence which he could raise if A would be in possession of the instrument. On the other hand, if the drawer or P pays, such payment constitutes a discharge and is a defence available against any holder who is not a protected holder.

6. The provisions on lost instruments are applicable only to situations where an ex-holder claims payment from a party, but not to cases where payment is sought from the drawee. This is clear from the use of the word “party” instead of “person”. The underlying reason is that, since a drawee is not liable on the instrument, payment by him would be at his own risk.

Paragraph (2)

7. According to paragraph (1), the ex-holder's exercise of his rights is subject to the provisions of paragraph (2) which lays down two requirements. The ex-holder must give security to the person from whom he claims payment as regulated in subparagraphs (b) and (c). An alternative method of security is envisaged in subparagraph (d). He must also supply that person with a written statement the contents of which are set forth in subparagraph (a). Such statement is intended to substitute for the lost instrument.

Subparagraph (a)

8. Under subparagraph (a), the ex-holder must state in writing certain elements of the lost instrument (i) and certain facts (ii, iii). If he does not do so, he may not exercise his rights under article 74. This would, for example, include the case where he does not remember the sum of the instrument or the date of issue or the date of payment.

9. The procedure under the provisions on lost instruments may only be used if the instrument at the time it was lost was a complete instrument, i.e. complied with the formal requisites set forth in article 1 (2) or (3). Therefore an instrument cannot be completed by the use of the written statement.

10. Subparagraph (ii) requires that the ex-holder show that he was a holder of the instrument. For example, he must show that, at the time of the loss of an order instrument he held it through an uninterrupted series of endorsements (cf. article 14 (1) (b)). Finally, subparagraph (iii) requires from the ex-holder to state that he lost the instrument and how.

Subparagraphs (b), (c) and (d)

11. In addition to the above written statement the ex-holder must give security to the person from whom he claims payment. This requirement arises from the fact that under the Convention a party must pay the ex-holder. However, the lost instrument may get into the hands of a protected holder against whom such party could not raise the first payment as a defence (cf. article 26 (1) (a)). The security is intended to provide for such contingency and to cover the risk of his being obliged to pay a second time.

Example B. In the situation described in example A (above, paragraph 5), the lost instrument is found by B who forges A's signature and endorses it to C. C endorses it to D. If D is a protected holder, he has a right to claim payment.

12. According to subparagraph (c), it is for the parties to settle the matters relating to the security, i.e. whether it is needed and, if so, its nature and terms. However, if the parties cannot agree, a court may make a determination. For example, it may decide, if security is needed, that a bank guarantee in a specified amount be given.

13. Subparagraph (d) provides an alternative way of covering the risk of double payment in those cases where security cannot be given. A court may order that the party from whom payment is claimed deposit the amount of the lost instrument and any interest and expenses recoverable under article 66 or 67 with the court or with another authority or institution which is competent under national law to receive and hold such deposit. According to subparagraph (d), the deposit is then to be considered as payment to the claimant. Such payment has the same legal effects under the Convention as any ordinary payment.

Example C. In the situation described in example A (above, paragraph 5), the drawer makes the deposit and is therefore discharged by payment. Such payment discharges also the payee (cf. article 73 (1)).

Article 75

(1) A party who has paid a lost instrument and to whom the instrument is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

(2) Such notification must be given on the day the instrument is presented or on one of the two business days which follow and must state the name of the person presenting the instrument and the date and place of presentment.

(3) Failure to notify renders the party who has paid the lost instrument liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 66 or 67.

(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost instrument and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

Commentary

Paragraph (1)

1. Article 75 imposes upon the party who has paid the instrument to the ex-holder the obligation to notify him of a subsequent presentment of the instrument for payment. The purpose of that notification is to enable the ex-holder to assert a claim to the instrument, to prevent a party from paying the instrument to a holder (cf. article 25 (3)) or to claim damages under article 23.

Paragraph (2)

2. Paragraph (2) sets forth the required particulars and the time-limit for the notification. Speedy notification is imperative in such situations where someone appears with the lost instrument since the surrounding circumstances normally make this a matter of urgency.

Paragraph (3)

3. If the party who paid the lost instrument fails to give the notification he is liable for damages which the ex-holder might suffer because of that failure. Damages may result, for example, from circumstances such as these: The payee

(P) loses the note and receives payment under article 74; the thief forges P's signature and endorses the note to A; A endorses the note to B who presents it for payment to the maker. Under paragraph (1) it is the duty of the maker to notify P that B has presented the note to him. Such notification may, for example, enable P to claim damages from A who, at the time of notification, is solvent. If the maker fails to notify and A becomes insolvent, P may claim damages from the maker to compensate him for not having been able to recover damages from A when he was still solvent.

4. Such action for damages based on failure to notify is an action off the instrument like, for example, the actions provided for under articles 23, 41 and 64.

Paragraphs (4) and (5)

5. Paragraphs (4) and (5) set forth the circumstances under which delay in giving notice is excused or under which notice is dispensed with, similar to the provisions of article 52.

Article 76

(1) A party who has paid a lost instrument in accordance with the provisions of article 74 and who is subsequently required to, and does, pay the instrument, or who, by reason of the loss of the instrument, then loses his right to recover from any party liable to him, has the right:

- (a) If security was given, to realize the security; or
- (b) If the amount was deposited with the court or other competent authority or institution, to reclaim the amount so deposited.

(2) The person who has given security in accordance with the provisions of paragraph (2) (b) of article 74 is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the instrument is lost.

Commentary

Paragraph (1)

1. This provision sets forth the circumstances under which a party who paid a lost instrument in accordance with article 74 may realize the security given to him or claim the amount deposited under article 74, paragraph (2) (d). The first of these situations is where a party had to pay a second time. The other situation is where a party who received security loses his right of recourse by reason of payment by a prior party. For example, an instrument endorsed by the payee to A and by A to B is lost by B. B asks payment from A under article 74 and is paid upon giving security to A. C acquires the lost instrument under circumstances which make him a protected holder. C demands payment from the drawer and is paid by him. Payment by the drawer discharges the payee. Therefore, because A loses

his right of recourse against the payee and the drawer, A may realize the security.

Paragraph (2)

2. This provision deals with the circumstances under which an ex-holder who gave security and received payment is entitled to obtain release of the security. He may do so when the party who paid and received the security is no longer at risk to be obliged to pay a second time. This is the case, for example, where the time periods provided in article 80 have expired or where proof is brought that the lost instrument was in fact destroyed.

Article 77

A person claiming payment of a lost instrument duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 74, paragraph (2) (a).

Cross reference

Protest: article 56

Commentary

1. The fact that the instrument is lost does not dispense the ex-holder of the obligation to protest the instrument in the event of dishonour by non-acceptance or by non-payment. Article 77 lays down rules as to how protest is to be effected in this case: it is to be effected by use of the same item as used for presentment, i.e. the written statement which satisfies the requirements of article 74, paragraph (2) (a), and, as provided therein, may be a copy of the lost instrument.

2. In the lost instrument situation, in general, the ordinary rules apply except for the replacement of the lost instrument by the written statement. Thus, e.g., a declaration made in accordance with article 56, paragraph (3), is deemed to be a protest for the purpose of the Convention (cf. article 56 (4)) also in the case of a lost instrument.

Article 78

A person receiving payment of a lost instrument in accordance with article 74 must deliver to the party paying the written statement required under article 74, paragraph (2) (a), receipted by him and any protest and a receipted account.

Cross reference

Payment: article 68

Commentary

Under article 68, paragraph (4), the person receiving payment must deliver the instrument (and any protest and

a receipted account) to the payer; if he does not do so, the person from whom payment is demanded may withhold payment. Article 78 makes it clear that the person obliged to pay may not withhold payment on the mere ground that the person claiming payment is unable to deliver the (lost) instrument; therefore, such withholding would constitute dishonour. However he must deliver the written statement which substitutes for the lost instrument.

Article 79

(1) A party who has paid a lost instrument in accordance with article 74 has the same rights which he would have had if he had been in possession of the instrument.

(2) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 78.

Cross reference

Right of recourse: article 67

Commentary

This provision establishes in respect of parties who took up and paid a lost instrument rights similar to those of the ex-holder under article 74. Thus, where an endorser, upon dishonour by the acceptor, pays the ex-holder, the endorser has in turn, against prior parties, those rights on the lost instrument which he would have had if he had acquired, upon payment, possession of the instrument.

CHAPTER EIGHT. LIMITATION (PRESCRIPTION)

Article 80

(1) A right of action arising on an instrument may no longer be exercised after four years have elapsed:

(a) Against the maker, or his guarantor, of a note payable on demand, from the date of the note;

(b) Against the acceptor or the maker or their guarantor of an instrument payable at a definite time, from the date of maturity;

(c) Against the acceptor of a bill payable on demand, from the date on which it was accepted;

(d) Against the drawer or an endorser or their guarantor, from the date of protest for dishonour by non-acceptance or non-payment or, where protest is dispensed with, from the date of dishonour.

(2) If a party has paid the instrument in accordance with article 66 or 67 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year from the date on which he paid the instrument.

Relevant legislation

UCC – section 3-122.

ULB – article 70.

Cross references

Note payable on demand: article 8.

Instrument payable at a definite time: article 8.

Maturity: article 4 (9).

Protest for dishonour by non-acceptance: article 57 (1).

Protest for dishonour by non-payment: article 57 (2).

Dispensation of protest: article 58 (2).

Exercise of right of recourse: article 55.

Commentary

1. This article lays down special rules in respect of the period or time within which an action arising on the instrument must be brought and the point of time from which such period starts to run. The article does not deal with actions off the instrument (e.g. those arising by virtue of articles 23, 41, 64 or 75 (3)) nor does the article deal with other aspects of limitation or prescription such as the causes of an interruption or suspension of the limitation period.

2. The general period of limitation is four years for actions against any party whether primarily or secondarily liable on the instrument. This period is, however, extended in those cases where an action may be brought by a party secondarily liable against a party liable to him.

Example A. A fixed term bill issued by the drawer to the payee is accepted by the drawee upon presentment by the payee. The payee transfers the bill to A who transfers it to B. Upon presentment for payment the bill is dishonoured by the acceptor. B, upon protesting the dishonour, exercises his right of recourse against A who pays the bill. Under article 80 B may (a) exercise his right on the instrument against the acceptor within four years from the date of maturity (paragraph (1) (b)); (b) exercise his right of recourse against A, the payee and the drawer within four years from the date of protest for dishonour by non-payment (paragraph (1) (d)). If B exercises his right of recourse against A within a period of three years, A in turn may exercise his right of recourse within the remaining period of time of four years. However, if B exercises his right of recourse against A after a period of three years has elapsed, A may exercise his right of recourse within a period of one year from the date on which he paid the bill to B.

Example B. In example A, B exercises his right of recourse against A after three and a half years from the date of protest for dishonour by non-payment. A who pays B may now exercise his right of recourse against the payee within one year from the date he paid the bill. If A should exercise his right of recourse against the payee after, say, nine months from the date he, A, paid the bill and the payee should pay, then the payee in turn would have one year from the date

he paid the bill within which he may bring an action on the bill against the drawer and the acceptor.

3. Article 80 sets forth rules regarding the point of time at which an action on the instrument accrues. The basic rule in this respect is that this point of time is the date on which a party became liable on the instrument. Thus an action

(a) Against the maker of a demand note accrues on the date of the note;

(b) Against the acceptor of a bill payable on demand accrues on the date of acceptance;

(c) Against the acceptor or the maker of an instrument payable at a definite time accrues on the date the instrument is to be paid;

(d) Against parties secondarily liable accrues on the date of protest for dishonour by non-acceptance or non-payment.

5. NOTE BY THE SECRETARIAT: DRAFT CONVENTION ON INTERNATIONAL CHEQUES: TEXT OF DRAFT ARTICLES AS ADOPTED BY THE WORKING GROUP ON INTERNATIONAL NEGOTIABLE INSTRUMENTS (A/CN.9/212* AND CORR. 1 SPANISH ONLY)

Draft Convention on International Cheques

CHAPTER ONE. SPHERE OF APPLICATION AND FORM OF THE CHEQUE

Article 1

(1) This Convention applies to international cheques.

(2) An international cheque is a written instrument which:

(a) Contains, in the text thereof, the words "international cheque (Convention of . . .)";

(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order or to bearer;

(c) Is drawn on a banker;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the cheque is drawn;

(ii) The place indicated next to the name or the signature of the drawer;

(iii) The place indicated next to the name of the drawee;

(iv) The place indicated next to the name of the payee;

(v) The place of payment;

(f) Is signed by the drawer.

(3) Proof that the statements referred to in paragraph (2) (e) of this article are incorrect does not affect the application of this Convention.

Article 2

This Convention applies without regard to whether the places indicated on an international cheque pursuant to

paragraph (2) (e) of article 1 are situated in Contracting States.

CHAPTER TWO. INTERPRETATION

Section 1. General provisions

Article 3

If a cheque is drawn against insufficient funds, it is nevertheless valid as a cheque.

Article 4

A cheque which bears a date other than the date on which it was drawn is nevertheless valid as a cheque.

Article 5

In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application.

Article 6

In this Convention:

(1) "Cheque" means an international cheque governed by this Convention;

(2) "Drawee" means the banker on whom a cheque is drawn;

(3) "Banker" includes any person or institution assimilated to a banker;

(4) "Payee" means the person in whose favour the drawer directs payment to be made;

(5) "Holder" means a person in possession of a cheque in accordance with article 16.

(6) "Protected holder" means the holder of a cheque which, when he became a holder, was complete and regular on its face, provided that:

* 18 February 1982.

(a) He was, at that time, without knowledge of a claim to or defence upon the cheque referred to in article 27 or of the fact that it was dishonoured by non-payment;

(b) The time-limit provided by article 43 for presentment of that cheque for payment had not then expired.

(7) "Party" means any person who has signed a cheque as drawer, endorser or guarantor.

(8) "Signature" includes a signature by stamp, symbol, facsimile, perforation or other mechanical means* and "forged signature" includes a signature by the wrongful or unauthorized use of such means.

(9) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution, even if intended by it to be transferable only in its records and between it and persons designated by it or between such persons.]

Article 7

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

Section 2. Interpretation of formal requirements

Article 8

The sum payable by a cheque is deemed to be a definite sum although the cheque states that it is to be paid:

(a) According to a rate of exchange indicated on the cheque or to be determined as directed by the cheque; or

(b) In a currency other than the currency in which the amount of the cheque is expressed.

Article 9

Any stipulation on a cheque that it is to be paid with interest is deemed not to have been written.

Article 10

(1) If there is a discrepancy between the amount of the cheque expressed in words and the amount expressed in figures, the amount of the cheque is the amount expressed in words.

(2) If the amount of the cheque is expressed in a currency having the same description as that of at least one

other State than the State where payment is to be made as indicated on the cheque and the specified currency is not identified as the currency of any particular State, the currency is to be considered as the currency of the State where payment is to be made.

Article 11

(1) A cheque is always payable on demand. It is so payable:

(a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or

(b) If no time of payment is expressed.

(2) A stipulation on a cheque that it is payable at a definite time is deemed not to have been written.

Article 12

(1) A cheque may:

(a) Be drawn by the drawer on himself or be drawn payable to his order;

(b) Be drawn by two or more drawers;

(c) Be payable to two or more payees.

(2) If a cheque is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the cheque may exercise the rights of a holder. In any other case the cheque is payable to all of them and the rights of a holder can only be exercised by all of them.

Section 3. Completion of an incomplete cheque

Article 13

(1) An incomplete cheque which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) of article 1 may be completed and the cheque so completed is effective as a cheque.

(2) When such a cheque is completed otherwise than in accordance with an agreement entered into:

(a) A party who signed the cheque before the completion may invoke the non-observance of the agreement as a defence against a holder, provided the holder had knowledge of the non-observance of the agreement when he became a holder;

(b) A party who signed the cheque after the completion is liable according to the terms of the cheque so completed.

* [Article (X)]

A Contracting State whose legislation requires that a signature on a cheque be handwritten may, at the time of signature, ratification or accession, make a declaration to the effect that a signature placed on a cheque in its territory must be handwritten. (Footnote in original.)

CHAPTER THREE. TRANSFER

Article 14

A cheque is transferred:

- (a) By endorsement and delivery of the cheque by the endorser to the endorsee; or
- (b) By mere delivery of the cheque if it is drawn payable to bearer or if the last endorsement is in blank.

Article 15

- (1) An endorsement must be written on the cheque or on a slip affixed thereto (*allonge*). It must be signed.
- (2) An endorsement may be:
 - (a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the cheque is payable to any person in possession thereof;
 - (b) Special, by a signature accompanied by an indication of the person to whom the cheque is payable.

Article 16

- (1) A person is a holder if he is:
 - (a) In possession of a cheque drawn payable to bearer; or
 - (b) The payee in possession of the cheque; or
 - (c) In possession of a cheque which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.
- (2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.
- (3) A person is not prevented from being a holder by the fact that the cheque was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon the cheque.

Article 17

The holder of a cheque on which the last endorsement is in blank may:

- (a) Further endorse the cheque either in blank or to a specified person; or
- (b) Convert the blank endorsement into a special endorsement by indicating therein that the cheque is payable to himself or to some other specified person; or
- (c) Transfer the cheque in accordance with paragraph (b) of article 14.

Article 18

When the drawer of a cheque payable to a payee or to his order has inserted in the cheque, or an endorser in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the transferee does not become a holder except for purposes of collection.

Article 19

- (1) An endorsement must be unconditional.
- (2) A conditional endorsement transfers the cheque whether or not the condition is fulfilled.

Article 20

An endorsement in respect of a part of the sum due under the cheque is ineffective as an endorsement.

Article 21

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the cheque.

Article 22

- (1) When an endorsement contains the words "for collection", "for deposit", "value in collection", "by procuration", "pay any bank", or words of similar import, authorizing the endorsee to collect the cheque (endorsement for collection), the endorsee:
 - (a) May only endorse the cheque for purposes of collection;
 - (b) May exercise all the rights arising out of the cheque;
 - (c) Is subject to all claims and defences which may be set up against the endorser;
- (2) The endorser for collection is not liable upon the cheque to any subsequent holder.

Article 23

- (1) The holder of a cheque may transfer it to a prior party in accordance with article 14; nevertheless, in the case where the transferee was a prior holder of the cheque, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.
- (2) The endorsement to the drawee operates only as an acknowledgement that the endorser has received from the drawee the amount of the cheque except in the case where the drawee has several establishments and the endorsement is made in favour of an establishment other than that on which the cheque has been drawn.

Article 24

A cheque may be transferred in accordance with article 14 after the expiration of the period of time for presentment.

Article 25

(1) If an endorsement is forged, any party has against the forger, and against the person to whom the cheque was directly transferred by the forger, the right to recover compensation for any damage that he may have suffered because of the forgery.

(2) Except to the extent provided in articles 70 and 72, the liability of a party or of the drawee who pays, or of an endorsee for collection who collects, a cheque on which there is a forged endorsement is not regulated by this Convention.

(3) For the purposes of this article, an endorsement placed on a cheque by a person in a representative capacity without authority or exceeding his authority has the same effects as a forged endorsement.

CHAPTER FOUR. RIGHTS AND LIABILITIES

*Section 1. The rights of a holder and of a protected holder**Article 26*

(1) The holder of a cheque has all the rights conferred on him by this Convention against the parties to the cheque.

(2) The holder is entitled to transfer the cheque in accordance with article 14.

Article 27

(1) A party may set up against a holder who is not a protected holder:

(a) Any defence available under this Convention;

(b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

(c) Any defence to contractual liability based on a transaction between himself and the holder;

(d) Any defence based on incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque, provided that such absence of knowledge was not due to his negligence.

(2) The rights to a cheque of a holder who is not a protected holder are subject to any valid claim to the cheque on the part of any person.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the cheque unless:

(a) Such third person asserted a valid claim to the cheque; or

(b) Such holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft.

Article 28

(1) A party may not set up against a protected holder any defence except:

(a) Defences under articles 31 (1), 32, 33 (1), 34 (3), 45 and 79 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that party;

(c) Defences based on the incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque provided that such absence of knowledge was not due to his negligence.

(2) The rights to a cheque of a protected holder are not subject to any claim to the cheque on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that person.

Article 29

(1) The transfer of a cheque by a protected holder vests in any subsequent holder the rights to and upon the cheque which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to, or a defence upon the cheque.

(2) If a party pays the cheque in accordance with article 59 and the cheque is transferred to him, such transfer does not vest in that party the rights to and upon the cheque which any previous protected holder had.

Article 30

Every holder is presumed to be a protected holder, unless the contrary is proved.

Section 2. The liability of the parties

A. General provisions

Article 31

(1) Subject to the provisions of articles 32 and 34, a person is not liable on a cheque unless he signs it.

(2) A person who signs a cheque in a name which is not his own is liable as if he had signed it in his own name.

Article 32

A forged signature on a cheque does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed the cheque himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own.

Article 33

(1) If a cheque has been materially altered:

(a) Parties who have signed the cheque subsequent to the material alteration are liable thereon according to the terms of the altered text;

(b) Parties who have signed the cheque before the material alteration are liable thereon according to the terms of the original text. Nevertheless, a party who has himself made, authorized, or assented to, the material alteration is liable on the cheque according to the terms of the altered text.

(2) Failing proof to the contrary, a signature is deemed to have been placed on the cheque after the material alteration.

(3) Any alteration is material which modifies the written undertaking on the cheque of any party in any respect.

Article 34

(1) A cheque may be signed by an agent.

(2) The signature of an agent placed by him on a cheque with the authority of his principal and showing on the cheque that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the cheque by an agent with his authority, imposes liability on the principal and not on the agent.

(3) A signature placed on a cheque by a person as agent but without authority to sign or exceeding his authority or by an agent with authority to sign but not showing on the cheque that he is signing in a representative capacity for a named person, or showing on the cheque that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the per-

son signing and not on the person whom he purports to represent.

(4) The question whether a signature was placed on the cheque in a representative capacity may be determined only by reference to what appears on the cheque.

(5) A person who is liable pursuant to paragraph (3) and who pays the cheque has the same rights as the person for whom he purported to act would have had if that person had paid the cheque.

Article 35

The order to pay contained in a cheque does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee.

Article 36

(1) Any statement written on a cheque indicating certification, confirmation, acceptance, visa or any other equivalent expression has only the effect to ascertain the existence of funds and prevents the withdrawal of such funds by the drawer, or the use of such funds by the drawee for purposes other than payment of the cheque bearing such a statement, before the expiration of the time-limit for presentment.

[(2) However, a Contracting State may provide that a drawee may accept a cheque and determine the legal effects thereof. Such acceptance must be effected by the signature of the drawee accompanied by the word "accepted".]

B. The drawer

Article 37

(1) The drawer engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the cheque in accordance with article 59, the amount of the cheque, and any interest and expenses which may be recovered under article 59 or 60.

(2) The drawer may not exclude or limit his own liability by a stipulation on the cheque. Any such stipulation is without effect.

C. The endorser

Article 38

(1) The endorser engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the cheque in accordance with article 59, the amount of the cheque, and any interest and expenses which may be recovered under article 59 or 60.

(2) The endorser may exclude or limit his own liability by an express stipulation on the cheque. Such stipulation has effect only with respect to that endorser.

Article 39

(1) Any person who transfers a cheque by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer:

- (a) A signature on the cheque was forged or unauthorized; or
- (b) The cheque was materially altered; or
- (c) A party has a valid claim or defence against him; or
- (d) The cheque was dishonoured by non-payment.

(2) The damages recoverable under paragraph (1) may not exceed the amount referred to in article 59 or 60.

(3) Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the cheque without knowledge of such defect.

D. The guarantor

Article 40

(1) Payment of a cheque may be guaranteed, as to the whole or part of its amount, for the account of a party by any person who may or may not have become a party.

(2) A guarantee must be written on the cheque or on a slip affixed thereto (*allonge*).

(3) A guarantee is expressed by the words: "guaranteed", "*aval*", "good as *aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires,

(a) A signature alone on the front of the cheque, other than that of the drawer, is a guarantee;

(b) A signature alone on the back of the cheque is an endorsement. A special endorsement of a cheque made payable to bearer does not convert the cheque into an order instrument.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the drawer.

Article 41

A guarantor is liable on the cheque to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the cheque.

Article 42

The guarantor who pays the cheque has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

CHAPTER FIVE. PRESENTMENT, DISHONOUR BY NON-PAYMENT, AND RECOURSE

Section 1. Presentment for payment and dishonour by non-payment

Article 43

A cheque is duly presented for payment if it is presented in accordance with the following rules:

(a) The holder must present the cheque to the drawee on a business day at a reasonable hour;

(b) A cheque must be presented for payment within 120 days of its stated date;

(c) A cheque must be presented for payment:

(i) At the place of payment specified on the cheque; or

(ii) If no place of payment is specified, at the address of the drawee indicated on the cheque; or

(iii) If no place of payment is specified and the address of the drawee is not indicated, at the principal place of business of the drawee;

(d) A cheque may be presented for payment at a clearing-house.

Article 44

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:

(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment.

Article 45

If a cheque is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon. However, if a cheque is not duly presented because of delay in making presentment, the drawer is not discharged of liability except to the extent of the loss suffered because of the delay.

Article 46

(1) A cheque is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment, or when the holder cannot obtain the payment to which he is entitled under this Convention, or as regards the drawer only, if presentment of the cheque, otherwise duly made, is delayed and payment is refused;

(b) If presentment for payment is dispensed with pursuant to article 44 (2) and the cheque is unpaid.

(2) If a cheque is dishonoured by non-payment, the holder may, subject to the provisions of article 48, exercise a right of recourse against the drawer, the endorsers and their guarantors.

Article 47

If a cheque is presented before its stated date, refusal by the drawee to pay does not constitute dishonour by non-payment under article 46.

*Section 2. Recourse**A. Protest**Article 48*

If a cheque has been dishonoured by non-payment, the holder may exercise a right of recourse only after the cheque has been duly protested for dishonour in accordance with the provisions of articles 49 to 51.

Article 49

(1) A protest is a statement of dishonour drawn up at the place where the cheque has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

- (a) The person at whose request the cheque is protested;
- (b) The place of protest; and
- (c) The demand made and the answer given, if any, or the fact that the drawee could not be found.

(2) A protest may be made:

- (a) On the cheque itself or on a slip affixed thereto (*allonge*); or

(b) As a separate document, in which case it must clearly identify the cheque that has been dishonoured.

(3) Unless the cheque stipulates that protest must be made, a protest may be replaced by a declaration written on the cheque and signed and dated by the drawee; the declaration must be to the effect that payment is refused.

(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purposes of this Convention.

Article 50

Protest for dishonour of a cheque by non-payment must be made on the day on which the cheque is dishonoured or on one of the two business days which follow.

Article 51

(1) Delay in protesting a cheque for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

- (i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;
- (iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;

(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person;

(d) If presentment for payment is dispensed with in accordance with article 44 (2).

Article 52

(1) If a cheque which must be protested for non-payment is not duly protested the drawer, the endorsers and their guarantors are not liable thereon.

(2) Delay in protesting a cheque for non-payment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered by the delay.

B. Notice of dishonour

Article 53

(1) The holder, upon dishonour of a cheque by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.

(2) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the cheque.

(3) Notice of dishonour operates for the benefit of any party who has a right of recourse on the cheque against the party notified.

Article 54

(1) Notice of dishonour may be given in any form whatever and in any terms which identify the cheque and state that it has been dishonoured. The return of the dishonoured cheque is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.

(2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.

(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

Article 55

Notice of dishonour must be given within the two business days which follow:

- (a) The day of protest, or, if protest is dispensed with, the day of dishonour; or
- (b) The receipt of notice given by another party.

Article 56

(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(2) Notice of dishonour is dispensed with:

- (a) If after the exercise of reasonable diligence notice cannot be given;
- (b) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:
 - (i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;
 - (ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made;

(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person.

Article 57

Failure to give notice of dishonour renders a person who is required to give such notice under article 53 to a party who is entitled to receive such notice liable for any damages which that party may suffer from such failure, provided that such damages do not exceed the amount referred to in article 59 or 60.

Section 3. Amount payable

Article 58

The holder may exercise his rights on the cheque against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

Article 59

(1) The holder may recover from any party liable the amount of the cheque.

(2) When payment is made after the cheque has been dishonoured, the holder may recover from any party liable the amount of the cheque with interest at the rate specified in paragraph (3) calculated from the date of presentment to the date of payment and any expenses of protest and of the notices given by him.

(3) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the cheque is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the cheque is payable. In the absence of any such rates, the rate of interest shall be [] per cent per annum.

Article 60

A party who pays a cheque in accordance with article 59 may recover from the parties liable to him:

- (a) The entire sum which he was obliged to pay in accordance with article 59 and has paid;
- (b) Interest on that sum at the rate specified in article 59, paragraph (3), from the date on which he made payment;
- (c) Any expenses of the notices given by him.

CHAPTER SIX. DISCHARGE

Section 1. Discharge by payment

Article 61

(1) A party is discharged of liability on the cheque when he pays the holder, or a party subsequent to himself who has paid the cheque and is in possession thereof, the amount due pursuant to article 59 or 60.

(2) A party is not discharged of liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the cheque or that the holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(3) (a) A person receiving payment of a cheque must, unless agreed otherwise, deliver:

- (i) To the drawee making such payment, the cheque;
- (ii) To any other person making such payment, the cheque, a receipted account and any protest;

(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the cheque to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 46.

(c) If payment is made but the person paying, other than the drawee, fails to obtain the cheque, such person is discharged but the discharge cannot be set up as a defence against a protected holder.

Article 62

(1) The holder is not obliged to take partial payment.

(2) If the holder who is offered partial payment does not take it, the cheque is dishonoured by non-payment.

(3) If the holder takes partial payment from the drawee, the cheque is to be considered as dishonoured by non-payment as to the amount unpaid.

(4) If the holder takes partial payment from a party to the cheque,

(a) The party making payment is discharged of his liability on the cheque to the extent of the amount paid; and

(b) The holder must give such party a certified copy of the cheque and of any authenticated protest.

(5) The drawee or a party making partial payment may require that mention of such payment be made on the cheque and that a receipt therefor be given to him.

(6) If the balance is paid, the person who receives it and who is in possession of the cheque must deliver to the payor the receipted cheque and any authenticated protest.

Article 63

(1) The holder may refuse to take payment in a place other than the place where the cheque was presented for payment in accordance with article 43.

(2) If in such case payment is not made in the place where the cheque was presented for payment in accordance with article 43, the cheque is considered as dishonoured by non-payment.

Article 64

(1) A cheque must be paid in the currency in which the amount of the cheque is expressed.

(2) The drawer may indicate on the cheque that it must be paid in a specified currency other than the currency in which the amount of the cheque is expressed. In that case:

(a) The cheque must be paid in the currency so specified;

(b) The amount payable is to be calculated according to the rate of exchange indicated on the cheque. Failing such an indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment:

(i) Ruling at the place where the cheque must be presented for payment in accordance with article 43 (c), if the specified currency is that of that place (local currency); or

(ii) If the specified currency is not that of that place, according to the usages of the place where the cheque must be presented for payment in accordance with article 43 (c);

(c) If such a cheque is dishonoured by non-payment, the amount payable is to be calculated;

(i) If the rate of exchange is indicated on the cheque, according to that rate;

(ii) If no rate of exchange is indicated on the cheque, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment at the place where the cheque must be presented for payment in accordance with article 43 (c) or at the place of actual payment.

(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-payment.

Article 65

(1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable

in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party.

(2) (a) If, by virtue of the application of paragraph (1) of this article, a cheque drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment ruling at the place where the cheque must be presented for payment in accordance with article 43 (c).

(b) If such a cheque is dishonoured by non-payment:

- (i) The amount is to be calculated, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment;
- (ii) Paragraph (3) of article 64 is applicable where appropriate.

Article 66

If the drawer countermands the order to the drawee to pay a cheque drawn on him, the drawee is under a duty not to pay.

Section 2. Discharge of a prior party

Article 67

(1) When a party is discharged wholly or partly of his liability on the cheque, any party who has a right of recourse against him is discharged to the same extent.

(2) Payment by the drawee of the whole or a part of the amount of the cheque to the holder, or to any party who has paid the cheque in accordance with article 59, discharges all parties of their liability to the same extent.

CHAPTER SEVEN. CROSSED CHEQUES AND CHEQUES PAYABLE IN ACCOUNT

Section 1. Crossed cheques

Article 68

(1) A cheque is crossed if it bears across its face two parallel transverse lines.

(2) A crossing is general if it consists of the two lines only or if between the two lines the word "banker" or an equivalent term or the words "and Company" or any abbreviation thereof is inserted; it is special if the name of a banker is so inserted.

(3) A cheque may be crossed generally or specially by the drawer or the holder.

(4) The holder may convert a general crossing into a special crossing.

(5) A special crossing may not be converted into a general crossing.

(6) The banker to whom a cheque is crossed specially may again cross it specially to another banker for collection.

Article 69

If a cheque shows on its face the obliteration either of a crossing or of the name of the banker to whom it is crossed, the obliteration is considered as not having taken place.

Article 70

(1) (a) A cheque which is crossed generally is payable only to a banker or to a customer of the drawee;

(b) A cheque which is crossed specially is payable only to the banker to whom it is crossed or, if such banker is the drawee, to his customer;

(c) A banker may not take a crossed cheque except from his customer or from another banker and may not collect such a cheque except for such a person.

(2) The drawee who pays, or the banker who takes or collects, a crossed cheque in violation of the provisions of paragraph (1) of this article incurs liability for any damages which a person may have suffered as a result of such violation, provided that such damages do not exceed the amount of the cheque.

Article 71

If the crossing on a cheque contains the words "not negotiable" the transferee becomes a holder but cannot become a protected holder. However, such transferee may acquire the rights of a protected holder under article 29.

Section 2. Cheques payable in account

Article 72

(1) (a) The drawer or the holder of a cheque may prohibit its payment in cash by writing transversally across the face of the cheque the words "payable in account" or words of similar import;

(b) In such case the cheque may only be paid by the drawee by means of a book-entry.

(2) The drawee who pays such a cheque otherwise than by means of a book-entry incurs liability for any damages which a person may have suffered as a result thereof, provided that such damages do not exceed the amount of the cheque.

(3) If a cheque shows on its face the obliteration of the words "payable in account", the obliteration is considered as not having taken place.

CHAPTER EIGHT. LOST CHEQUES

Article 73

(1) When a cheque is lost, whether by destruction, theft or otherwise, the person who lost the cheque has, subject to the provisions of paragraphs (2) and (3) of this article, the same right to payment which he would have had if he had been in possession of the cheque. The party from whom payment is claimed cannot set up as a defence against liability on the cheque the fact that the person claiming payment is not in possession thereof.

(2) (a) The person claiming payment of a lost cheque must state in writing to the party from whom he claims payment:

- (i) The elements of the lost cheque pertaining to the requirements set forth in article 1 (2); for this purpose the person claiming payment of the lost cheque may present to that party a copy of that cheque;
- (ii) The facts showing that, if he had been in possession of the cheque, he would have had a right to payment from the party from whom payment is claimed;
- (iii) The facts which prevent production of the cheque;

(b) The party from whom payment of a lost cheque is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost cheque;

(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms;

(d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost cheque, and any interest and expenses which may be claimed under article 59 or 60, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

(3) The person claiming payment of a lost cheque in accordance with the provisions of this article need not give security to the drawer who has inserted in the cheque, or to an endorser who has inserted in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import.

Article 74

(1) A party who has paid a lost cheque and to whom the cheque is subsequently presented for payment by another

person must notify the person to whom he paid of such presentment.

(2) Such notification must be given on the day the cheque is presented for payment or on one of the two business days which follow and must state the name of the person presenting the cheque and the date and place of presentment.

(3) Failure to notify renders the party who has paid the lost cheque liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 59 or 60.

(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost cheque and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

Article 75

(1) A party who has paid a lost cheque in accordance with the provisions of article 73 and who is subsequently required to, and does, pay the cheque, or who, by reason of the loss of the cheque, then loses his right to recover from any party liable to him, has the right:

(a) If security was given, to realize the security; or

(b) If the amount was deposited with the court or other competent authority or institution, to reclaim the amount so deposited.

(2) The person who has given security in accordance with the provisions of paragraph (2) (b) of article 73 is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the cheque is lost.

Article 76

A person claiming payment of a lost cheque duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 73, paragraph (2) (a).

Article 77

A person receiving payment of a lost cheque in accordance with article 73 must deliver to the party paying the written statement required under article 73, paragraph (2) (a), receipted by him and any protest and a receipted account.

Article 78

(1) A party who has paid a lost cheque in accordance with article 73 has the same rights which he would have had if he had been in possession of the cheque.

(2) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 77.

CHAPTER NINE. LIMITATION (PRESCRIPTION)

Article 79

(1) A right of action arising on a cheque can no longer be exercised after four years have elapsed:

(a) Against the drawer or his guarantor, from the date of the cheque;

(b) Against an endorser or his guarantor, from the date of protest for dishonour or, where protest is dispensed with, the date of dishonour.

(2) If a party has paid the cheque in accordance with article 59 or 60 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year from the date on which he paid the cheque.

6. REPORT OF THE SECRETARY-GENERAL: COMMENTARY ON DRAFT CONVENTION ON INTERNATIONAL CHEQUES (A/CN.9/214)*

Introduction

1. The United Nations Commission on International Trade Law (UNCITRAL), at its fifth session, after having taken note of the Secretary-General's report setting forth a draft uniform law on international bills of exchange accompanied by a commentary, entrusted its Working Group on International Negotiable Instruments with the preparation of a final draft uniform law and also requested the Group to consider the desirability of preparing uniform rules applicable to international cheques.¹

2. The Working Group, in the light of replies received to a questionnaire circulated to banking and trade institutions, concluded that the formulation of uniform rules for international cheques was desirable and the application of the draft Convention on International Bills of Exchange and International Promissory Notes could be extended to international cheques. The Commission at its twelfth session authorized the Working Group to proceed accordingly.²

3. The Working Group on International Negotiable Instruments adopted the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211)** and the draft Convention on International Cheques (A/CN.9/212)*** at the close of its eleventh session (August 1981), after a Drafting Group had reviewed both drafts and established corresponding language versions (in Chinese, English, French, Russian and Spanish).

4. The Commission at its fourteenth session requested the Secretary-General, after the completion of the texts by the Working Group, to circulate them, together with a commentary, to all Governments and interested international organizations for comments. At the request of the Secretariat the commentary on the two draft Conventions was prepared by Professor Aharon Barak and Professor Willem Vis who as former members of the Commission's Secretariat and subsequently as consultants assisted the Working Group on International Negotiable Instruments in the drawing up of the draft Convention. The commentary on the draft Convention on International Bills of Exchange and International Promissory Notes is set forth in document A/CN.9/213,* the commentary on the draft Convention on International cheques is set forth in the present report.

5. An account of the preparatory work on international negotiable instruments may be found in the introduction to the commentary on the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/213).*

Comparative table of the numbering of the articles of the draft Convention adopted by the Working Group and of the draft articles as considered by it

The articles of the Convention have been numbered consecutively only upon its adoption by the Working Group. Until then, the original numbering of the draft articles has generally been maintained throughout the various stages of the deliberations by the Working Group in order to facilitate reference to the relevant reports of the Working Group; where, exceptionally, draft provisions have been transferred or combined with other provisions, their previous location is also indicated in the following table.

The original numbering may also assist in a comparison between provisions on bills or notes and on cheques since each draft article on cheques had been numbered to correspond to the draft article on bills or notes which relates to the same or a similar issue.

* Reproduced in this volume, part two, II, A, 4.

* 27 May 1982.

** Reproduced in this volume, part two, II, A, 3.

*** Reproduced in this volume, part two, II, A, 5.

¹ Report of the Commission on the work of its fifth session (1972), *Official Records of the General Assembly, Twenty-seventh Session, Supplement No. 17* (A/8717), para. 61 (Yearbook ... 1972, part one, II, A).

² Report of the Commission on the work of its twelfth session (1979), *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 44 (5) (Yearbook ... 1979, part one, II, A).

Number of article in Convention	Number of previous draft article	Number of article in Convention	Number of previous draft article
1	1	37	34
2	3	38	41
3	<i>a</i>	39	42
4	<i>β</i> (1)	40	43
5	4	41	44
6	5	42	45
	(5(8) incorporating earlier 27 (3))	43	53
7	6	44	54
8	7	45	55
9	7 <i>bis</i>	46	56
10	8 (1, 2)	47	<i>β</i> (2)
11	9	48	57
12	10	49	58
13	11	50	59
14	13	51	61
15	New article (between 13 and 13 <i>bis</i>)	52	60
	13 <i>bis</i>	53	62
16	15	54	63
17	16	55	64
18	17	56	65
19	18	57	66
20	19	58	66 <i>bis</i>
21	20	59	67
22	21	60	68 (1)
23	21 <i>bis</i>	61	70
24	22	62	71
25	23	63	72
26	24	64	74
27	25	65	74 <i>bis</i>
28	25 <i>bis</i>	66	74 <i>ter</i>
29	(earlier 25 (4) and 68 (2))	67	78
	26	68	A
30	27 (1, 2)	69	B
31	28	70	C
32	29	71	E
33	30	72	F
34	30 <i>bis</i>	73	80
35	X	74	81
36	(between 34 and 41)	75	82
		76	83
		77	84
		78	85
		79	79

Abbreviations used in the commentary

BEA:	Bills of Exchange Act, 1882 (United Kingdom)
Cheques Act:	Cheques Act, 1957 (United Kingdom)
Convention:	Draft Convention on International Cheques, as adopted by the UNCITRAL Working Group on International Negotiable Instruments (A/CN.9/212)*
Geneva Convention of 1931:	Convention Providing a Uniform Law for Cheques (Geneva, 1931)
UCC:	Uniform Commercial Code (United States)
ULC:	Uniform Law on Cheques, set forth in annex I to the Geneva Convention of 1931

* Reproduced in this volume, part two, II, A, 5.

Commentary on draft Convention on International Cheques

CHAPTER ONE. SPHERE OF APPLICATION AND FORM OF THE CHEQUE

Article 1

(1) This Convention applies to international cheques.

(2) An international cheque is a written instrument which:

(a) Contains, in the text thereof, the words "international cheque (Convention of . . .)";

(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order or to bearer;

(c) Is drawn on a banker;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

(i) The place where the cheque is drawn;

(ii) The place indicated next to the name or the signature of the drawer;

(iii) The place indicated next to the name of the drawee;

(iv) The place indicated next to the name of the payee;

(v) The place of payment;

(f) Is signed by the drawer.

(3) Proof that the statements referred to in paragraph (2) (e) of this article are incorrect does not affect the application of this Convention.

Relevant legislation

BEA – sections 3 and 73.

UCC – section 3-103.

ULC – articles 1, 2, 3 and 5.

Cross references

Definite sum of money: article 8.

Payable on demand: article 11.

Payable at a definite time: article 11.

Money: article 6 (9).

Drawee: article 6 (2).

Banker: article 6 (3).

Commentary

1. This article provides the rules for determining when a written instrument qualifies as an "international cheque" under the Convention. If an instrument so qualifies the Convention is applicable. The definition of an international cheque is set forth in paragraph (2) which makes clear that

the use of an instrument governed by the provisions of this Convention is entirely optional. The initial choice to use a cheque subject to the Convention is exercised by the drawer. He may do so if certain international elements are present, but he is under no obligation to draw a cheque under the Convention. Persons other than the drawer are bound by the provisions of the Convention by virtue of their signature on the international cheque or by taking it up. As regards the applicability of this Convention, see also article 2.

Paragraph (1)

2. This paragraph is of a declaratory character.

Paragraph (2)

3. This paragraph defines an international cheque, i.e. it lays down the basic formal requisites with which a cheque must comply in order to be an international cheque governed by this Convention. Non-compliance of a cheque with these requisites makes the Convention inapplicable. However, it is to be noted that an incomplete cheque may be completed in accordance with article 13. The inapplicability of this Convention is the sole consequence of non-compliance with paragraph (2); such non-compliance does not interfere with the validity of the cheque under applicable national law (e.g., the law of the place of drawing or of the place of issuance).

"A written instrument"

4. The term "written" is not defined in the Convention. This term, in the context in which it is here used, would include any mode of representing or reproducing words in visible form, such as handwritten, typed or printed.

5. Subject to the requirements laid down in paragraph (2), the validity of a cheque as an international cheque is not dependent on the use of any specific wording or any specific language.

Formal requisites of an international cheque

6. Subparagraphs (a) to (f) set forth the formal requisites of a cheque.

Subparagraph (a)

7. An instrument is valid as an international cheque under the Convention only when the drawer, in the text thereof, has inserted the words "international cheque (Convention of . . .)". This designation, which expresses the intent of the parties that their liability on the cheque is governed by the Convention, must be incorporated "in the text" of the cheque. Such designation would not meet the requirement of subparagraph (a) if it appeared outside the text, as where it would be printed or stamped in the margin of the

cheque. The requirement is intended to guard against altering the character of a cheque after its issuance.

Subparagraph (b)

8. An international cheque must be an "unconditional order" (it must not be payable upon a contingency) to pay a "definite sum of money" (as defined in article 8). The sum is payable to the "payee" or to bearer.

9. The wording of subparagraph (b) permits a drawer to draw an international cheque on himself or to draw it payable to himself (see also article 12).

10. The words "or to his order" have been added after the words "to the payee" because of a well-established practice in certain common law countries to draw cheques "to the order of" a payee. However, the omission of the words "or to his order" does not prevent the cheque from being a negotiable instrument under this Convention. Therefore, an international cheque may be drawn "pay to X", "pay to the order of X", "pay to X or to his order", or "pay to bearer".

Subparagraph (c)

11. An instrument in order to be a cheque under this Convention must be drawn on a banker. Banker is defined in article 6 (3) as including any person or institution assimilated to a banker.

Subparagraph (d)

12. The date of the instrument is relevant in the context of other provisions of this Convention, such as article 43 (b).

Subparagraph (e)

13. International cheques are intended to be used in international payment transactions. Therefore, the Convention should be applicable only when elements are present evidencing the international character of the payment transaction. Consideration was given, during the preparatory stage of the work, to the feasibility of linking the test of internationality to the requirement that an international cheque be used solely to settle international transactions, such as an international sale of goods, or a test geared to potential conflict of law situations. These tests were not retained because they were considered impracticable and uncertain. Instead, preference was given to the approach reflected in subparagraph (e) which requires that the elements of internationality be apparent from the face of the instrument.

14. Subparagraph (e) requires that at least two of the following places indicated on the cheque be situated in different States: the place of drawing, the place indicated next to the name or the signature of the drawer, the place indicated next to the name of the drawee, the place indicated

next to the name of the payee, and the place of payment. The analysis of this test shows that it embraces the majority of cases in which there is an international payment transaction and also the principal situations in which conflicts of law may arise. Subparagraph (e) does not require that a street address and the name of a town appear on the cheque. For the purpose of internationality it suffices for the cheque to mention two different States. Thus a cheque drawn by J. Brown, Australia, made payable to A. Petrov, Bulgaria, would meet the requirement of subparagraph (e).

Subparagraph (f)

15. The order to pay, contained in the cheque, is an order that can only be given by the drawer. His signature is an indispensable element of the validity of a writing as a cheque. If the signature of the drawer is lacking, the writing cannot be made into a cheque by completion (cf. article 13).

16. A cheque may be drawn by two or more drawers (cf. article 12 (1) (b)).

Paragraph (3)

17. The security of transactions in connection with international cheques depends on a clear and indisputable identification of the legal regime. To this end, paragraph (2) (a) requires that the cheque contain in its text the words "international cheque", followed by the words "(Convention of . . .)". In addition, under paragraph (2) (e), a cheque, in order to be subject to this Convention, must show that at least two places, as specified, are situated in different States. The requisite of "internationality" consequently must appear from the statements made on the cheque. These rules are strengthened by the rule of paragraph (3) whereby the applicability of this Convention cannot be placed in doubt by controverting the statements made on the face of the cheque in conformity with paragraph (2) (e).

18. Paragraph (3) has the same effect as a provision that, for the purpose of application of the Convention, the appearance of international elements, required under paragraph (2) (e), constitutes an irrebuttable presumption. Therefore, an incorrect statement as to the place of drawing etc., so as to bring the cheque under the Convention, does not thereby make the cheque invalid as an international cheque, and cannot be a defence to be raised against a holder, even if the holder, when taking the cheque, had knowledge of the fact that a statement was incorrect. To provide otherwise would lend grounds for casting doubts on the applicability of the Convention, and would impair the circulation of the international cheque.

19. Incorrect or false statements made on a cheque as to the international elements may of course be considered by a State as violating its law.

Article 2

This Convention applies without regard to whether the places indicated on an international cheque pursuant to paragraph (2) (e) of article 1 are situated in Contracting States.

Cross reference

Definition of "international cheque": article 1 (2).

Commentary

1. The sole requirement for the Convention's applicability is that the cheque is an international cheque, i.e. a cheque which complies with the formal requirements laid down in article 1 (2). Under this test, the forum of a Contracting State would apply the Convention, and not its domestic law or the negotiable instruments law of a foreign State which, through the application of conflict rules, might otherwise be applicable.

2. The provision of article 2 may be illustrated by the following example. A cheque containing, in the text thereof, the words "international cheque (Convention of . . .)" (see article 1 (2) (a)) on its face shows that it is drawn in State X on a drawee-banker in State Y. Neither X nor Y is a Contracting State. The payee endorses the cheque to E. The drawee dishonours the cheque by non-payment and E requests the drawer to pay the cheque. The drawer asserts a defence (for instance, failure by E to observe applicable formalities as to protest), and the holder brings his claim before the court of a Contracting State. By virtue of article 2, the Convention is applicable, and the rights and liabilities of all parties to the cheque are governed by the Convention, irrespective of the place where each separate contract on the cheque was made, where the cheque was dishonoured, or where protest was made or should have been made. This rule on the applicability of the Convention thus supplants the various rules on conflict of laws that might otherwise be applicable.

3. In substance, article 2 gives effect to the intention of the parties that their legal relationships on the cheque are to be governed by the Convention, in accordance with the statement on the cheque. Thus parties signing an international cheque as drawer, endorser, or guarantor thereby manifest their intention that their liabilities on the cheque be governed by the Convention. The same may be said of a person who takes the cheque as transferee, holder or protected holder. The application of the Convention to legal relationships between parties to an international cheque on the sole ground that the cheque is an international cheque responds therefore to the reasonable expectations of the parties.

4. Of course, the obligation to apply the Convention in the circumstances defined in articles 1 and 2 is incumbent on Contracting States only. Consequently, whether the forum

of a non-contracting State would apply the Convention to a cheque that complies with the requirements set forth in article 1 (2) would depend on the conflict of law rules of that forum. Presumably, the forum of a non-contracting State would consider such a cheque to be an international cheque subject to the Convention if its conflict rules referred to the law of the country where the cheque was drawn and if that country is a Contracting State. But in other factual settings a non-contracting State may apply the rules of the national law rather than this Convention. In such cases, an instrument drawn as an international cheque under the Convention, might not qualify as a cheque under the applicable law. The Convention seeks to meet that potential problem by laying down, in article 1 (2), requisites that are in substance similar to those which in the principal legal systems are considered to be the minimum requirements for an instrument to qualify as a cheque. Hence, the presence on an instrument of the requisites under article 1 (2) will, in most cases, also qualify the instrument as a cheque under whatever national law may be applicable. Therefore, article 1 (2) helps to ensure that an instrument drawn pursuant to its provisions will qualify as a cheque even if the forum of a non-contracting State applies its own law or, by reason of its conflict rules, applies the law of another non-contracting State. However, there may be cases where an instrument that satisfies the requisites of article 1 (2) will not meet one of the requirements imposed by a national law.

5. Consideration has been given to adding a provision that the Convention would be applicable only if the instrument was drawn, or issued in a Contracting State. The principal effect of such a rule would be to discourage persons from drawing international cheques in non-contracting States and thereby reduce the complications that might result from the application of conflict rules by the fora of non-contracting States. Such a rule limiting the applicability of the Convention has not been incorporated in the Convention. Under this Convention a person is given the opportunity to draw, endorse or guarantee an international cheque without regard to whether it is drawn in a Contracting State or a non-contracting State, and a court in a Contracting State would give effect to his intent that the rules of the Convention should apply which was expressed on the face of the instrument and by the voluntary use thereof. Of course, the court of a non-contracting State may not give effect to this intent. This possibility, however, can be taken into account by the parties in deciding whether to employ the international cheque in the light of their expectations as to whether litigation would be brought in a Contracting or in a non-contracting State. Furthermore, the rule mentioned above would necessarily make the Convention inapplicable to an instrument drawn as an international cheque in a non-contracting State, even where the drawee is in a Contracting State, or the cheque is payable in a Contracting State, and litigation arises in a Contracting State. Such a

rule would unduly restrict the scope of application of the Convention.

6. The above problem, and others related to the application of uniform rules to rights and liabilities on an international instrument, are inherent in the process of adoption of uniform rules for as long as a Convention setting forth such rules is not universally adopted and applied.

CHAPTER TWO. INTERPRETATION

Section 1. General provisions

Article 3

If a cheque is drawn against insufficient funds, it is nevertheless valid as a cheque.

Relevant legislation

ULC – article 3.

Commentary

It is the assumption that if a drawer draws a cheque on his account with the banker the account contains funds sufficient for the payment of the cheque. Article 3 makes clear that if the account is insufficient for payment of the cheque the cheque is nevertheless a valid cheque under this Convention and upon dishonour the holder may exercise a right of recourse against the drawer and parties secondarily liable to him.

Article 4

A cheque which bears a date other than the date on which it was drawn is nevertheless valid as a cheque.

Relevant legislation

BEA – section 13 (2).

UCC – section 3-114 (3).

ULC – article 28 (2).

Commentary

Under paragraph (2) (d) of article 1, an instrument in order to qualify as an international cheque must be dated. Article 4 makes clear that the date appearing on the cheque need not, for purposes of validity, be the true or correct date.

Article 5

In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application.

Commentary

1. One of the important objectives of the article is to promote uniformity in the interpretation and application of

this Convention. To this end, the text of the Convention directs attention to its "international character"; due regard for the international character of the Convention would avoid interpreting its provisions by recourse to local (and varying) national concepts, rather than to the Convention's provisions read as an independent piece of international legislation. This article may also be helpful to encourage tribunals in one State to promote uniformity by interpreting the Convention with due regard to the interpretation given to it in other States.

2. The general principle with regard to the interpretation and application of the Convention, laid down in this article, is found in other Conventions that originated in the work of the United Nations Commission on International Trade Law (UNCITRAL); see article 7 of the Convention on the Limitation Period in the International Sale of Goods (1974),* article 3 of the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules),** and article 7 (1) of the United Nations Convention on Contracts for the International Sale of Goods (1980).***

Article 6

In this Convention:

(1) "Cheque" means an international cheque governed by this Convention;

(2) "Drawee" means the banker on whom a cheque is drawn;

(3) "Banker" includes any person or institution assimilated to a banker;

(4) "Payee" means the person in whose favour the drawer directs payment to be made;

(5) "Holder" means a person in possession of a cheque in accordance with article 16.

(6) "Protected holder" means the holder of a cheque which, when he became a holder, was complete and regular on its face, provided that:

(a) He was, at that time, without knowledge of a claim to or defence upon the cheque referred to in article 27 or of the fact that it was dishonoured by non-payment;

(b) The time-limit provided by article 43 for presentment of that cheque for payment had not then expired.

(7) "Party" means any person who has signed a cheque as drawer, endorser or guarantor.

(8) "Signature" includes a signature by stamp, symbol, facsimile, perforation or other mechanical means**** and

* Yearbook . . . 1974, part three, I, B.

** Yearbook . . . 1978, part three, I, B.

*** Yearbook . . . 1980, part three, I, B.

**** [Article (X)]

A Contracting State whose legislation requires that a signature on a cheque be handwritten may, at the time of signature, ratification or accession, make a declaration to the effect that a signature placed on a cheque in its territory must be handwritten. (Footnote in original.)

"forged signature" includes a signature by the wrongful or unauthorized use of such means.

[(9) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution, even if intended by it to be transferable only in its records and between it and persons designated by it or between such persons.]*

Commentary

Paragraph (1): "cheque"

1. Article 1 (1) of this Convention provides that the Convention applies to an international cheque. Article 1 (2) specifies the formal requisites with which an instrument must comply in order to be an international cheque. This Convention uses the expression "cheque" to replace the longer expression "international cheque".

Paragraph (2): "drawee"

2. The drawee can only be a banker (see definition of "banker" in paragraph (3)). Therefore, an instrument drawn upon a person other than a banker is not a cheque under this Convention even though it contains the words "international cheque (Convention of . . .)".

Paragraph (3): "banker"

3. The question whether any person or institution is a banker and the question whether such person or institution may be considered to be assimilated to a banker are to be determined by reference to the applicable national law.

Paragraph (4): "payee"

4. In a cheque, the payee is the specified person to whom payment must initially be made. A cheque may be made payable to two or more payees (cf. article 12 (1) (c)). In a cheque, the payee may be the drawer (cf. article 12 (1) (a)) or the drawee.

Paragraph (5): "holder"

Relevant legislation

BEA - section 2.

UCC - section 1-201 (20).

ULC - article 19.

Cross references

Holder: article 16.

Rights of a holder: articles 26 and 27.

5. The rights to and upon a cheque are vested in the holder. He has the right to receive payment, and payment

* Square brackets, used in the text of the Convention, indicate matters which have been reserved for further consideration and decision at a later stage. (Footnote in original.)

to him discharges the party paying (article 61). Being a "holder" is a necessary element for qualifying as a protected holder. Under Chapter Five of this Convention, the holder is to present the cheque for payment, and, in the event of dishonour, to protest the cheque and to give notice of dishonour.

6. Pursuant to article 16, in order to be a holder, a person must be the specified payee, the bearer, or the endorsee of a cheque and in possession of it, or a person in possession of a cheque on which the last endorsement is in blank. If a cheque shows more than one endorsement, there is the further requirement that the series of endorsements be uninterrupted.

Example A. The payee endorsed the cheque "to A" (a "special" endorsement) and delivered the cheque to A. A is the holder.

Example B. The payee endorsed the cheque "to A", and delivered the cheque to B. Neither A nor B is a holder.

Example C. The payee endorsed the cheque in blank and delivered it to A. A is the holder.

Example D. The payee endorsed the cheque in blank. The cheque was stolen by T. T is the holder. Since the payee is not "in possession" of the cheque, he is not the holder.

Example E. The drawer makes a cheque payable to bearer. Any person in possession of this cheque is a holder.

7. Under the definition of "holder", a drawer or a guarantor are not holders since they are neither a "payee" nor "endorsee". If the cheque is endorsed to them or if a bearer cheque is delivered to them, they are a holder.

Example F. The drawee dishonoured the cheque. The holder exercised his rights of recourse, and was paid by the drawer. The cheque was delivered to the drawer without an endorsement. The drawer is not the holder of the cheque.

8. A payee or endorsee may reacquire a cheque. Even though the cheque is not endorsed to them, in connection with the reacquisition, the "payee" or "endorsee" comply with the definition of "holder" (article 23).

9. If a holder parts with possession of the cheque he ceases to be a holder. If the lack of possession is caused by the loss of the cheque, his rights are determined by the rules on "lost cheques" (articles 73-78).

10. For the purposes of the definition of holder it is irrelevant whether the possession of the cheque is lawful or not. As seen from example D, even a thief may be a holder. Of course, if the possession is unlawful, there may be a defence on or a claim to the cheque pursuant to article 27.

11. To be a "holder" the possessor need not be the owner of the cheque. When a cheque is endorsed "for collection", the endorsee in possession is the holder of the cheque, although he may be only an agent of the endorser rather than the owner of it.

Paragraph (6): "protected holder"

Relevant legislation

BEA — section 29.

UCC — sections 3-302 and 3-304.

ULC — articles 21 and 22.

Cross reference

Protected holder: article 28.

12. The main advantages of a cheque result from the strong legal position of a protected holder: as a general rule, he takes the cheque free from claims of ownership third parties may have to the cheque and from defences to an action by him on the cheque (article 28).

"Was complete and regular on its face"

13. A person does not acquire the status of a protected holder if the cheque, on the face of it, is not complete and regular. For example, a cheque on which the sum payable is lacking is not complete even though a person may complete it in accordance with article 13. It may be noted that a person, upon so completing an incomplete cheque, may become a holder but cannot become a protected holder. A cheque is not regular if, for instance, the name of the first endorser does not correspond to the name of the payee. The expression "on its face" means that the holder need not look beyond the cheque, and refers to both the face and the back of the cheque.

"Without knowledge"

14. A holder does not qualify as a protected holder if, when taking the cheque, he knows about the existence of a claim or a defence affecting the cheque or about the fact that it was dishonoured. Such holder takes the cheque at his own risk, and it is not the policy of this Convention to protect him. However, it should be noted that under article 29 (the so-called "shelter-rule") the transfer of a cheque by a protected holder may vest in any subsequent holder the rights of the protected holder, even though the subsequent holder is not a protected holder in his own right as where, for instance, he knew of a claim or a defence.

15. For the definition of the expression "without knowledge", see article 7 and commentary.

"At that time"

16. A holder may be a protected holder even though he acquired knowledge of claims, defences or the fact that the cheque had been dishonoured after he became a holder.

17. A person may be a protected holder even though he has not given value or consideration for the cheque. This rule is consistent with some legal systems, notably those of civil law inspiration, and departs from others (e.g. BEA,

section 29 (1), and UCC, sections 3-302 (1) (a) and 3-303). The present approach was selected because of the problems of unifying the different approaches to the relevance of "value" or "consideration" by legal systems.

Paragraph (7): "party"

18. The Convention uses the term "party" to refer to a party to a cheque, i.e. a person who has signed a cheque. The drawer, endorser and guarantor are parties to a cheque. On the other hand, the payee is not a party to the cheque (unless he has endorsed it) and the drawee is not a party to the cheque.

Paragraph (8): "signature" and "forged signature"

19. This provision accommodates modern practice in respect of signatures on negotiable instruments. Therefore a signature need not be handwritten. A complete signature is not necessary.

20. Article (X) permits a Contracting State whose legislation requires that signatures on cheques be executed in handwriting to make, at the time of signing, ratifying or acceding to the Convention, a declaration derogating from the provision of paragraph (8) to the effect that a signature placed on an international cheque in its territory must be handwritten.

21. The term "forged signature" is relevant in the context of article 25, concerning the rights and liabilities of parties to a cheque on which an endorsement is forged, and article 31, concerning the liability of the person whose signature is forged. This paragraph makes articles 25 and 31 applicable where a cheque was signed by an agent without authority or was signed by the wrongful use of any means by which a signature may be made in accordance with the present provision.

Paragraph (9): "money" or "currency"

22. Amongst the formal requisites with which a written instrument must comply in order to qualify as an international cheque is the requisite that the instrument must contain "an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order or to bearer" (article 1 (2) (b)). The definition of "money" or "currency" set forth in paragraph (9) suggests that the Convention, in addition to providing the usual rule that a cheque is payable in a medium of exchange authorized or adopted by a Government as its official currency, should further provide that a cheque:

(a) May be made payable in other monetary units or units of account such as the special drawing rights (SDRs) of the International Monetary Fund, the European currency units (ECUs) of the European Economic Community and the transferable rouble of the International Bank for Economic Co-operation; and

(b) May call for payment in a specified currency but be denominated in such monetary units or units of account.

23. Whilst it is true that only a limited class (member States of the intergovernmental institution concerned and, exceptionally, certain other authorized holders who are not members) may hold or use the units referred to, their use in a variety of transactions is on the increase. There would appear to be no special reason not to permit the application of the Convention to a cheque payable in such units if the drawer (who must perforce belong to the limited class) should wish to make the cheque subject to the provisions of the Convention. Furthermore, private parties, as a safeguard against currency fluctuations, might wish to denominate the amount of the cheque in, say, SDRs and specify in the cheque the currency in which it is to be paid. Such a denomination would be a "definite sum of money" in that the valuation of an SDR against the specified currency would be available on the date when the cheque is payable.

24. Whether the application of the Convention should be extended in this manner will, in the last resort, depend on the desire of Governments to use the Convention for the above stated purposes. Consequently, the proposed definition of "money" or "currency" is placed between square brackets so as to indicate the tentative nature of the definition. If the views of Governments should be of a positive nature certain provisions of the Convention will have to be amended accordingly.

Article 7

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

Relevant legislation

BEA – sections 29 (1), 59 (1) and 90.

UCC – sections 1-201 (19) and (25), and 3-304.

ULC – articles 21 and 22.

Cross references

Knowledge of a fact: articles 6 (6), 13 (2) (a), 27 (1) (d), 28 (1) (c), 39 (3) and 61 (2).

Commentary

In several provisions of the Convention the rights and liabilities of a party are dependent on whether he took or paid the cheque without knowledge of a certain fact. Under this article the concept of "knowledge" covers (a) actual knowledge of a fact and (b) constructive knowledge, i.e. the person could not have been unaware of the existence of a fact.

Section 2. Interpretation of formal requirements

Article 8

The sum payable by a cheque is deemed to be a definite sum although the cheque states that it is to be paid:

(a) According to a rate of exchange indicated on the cheque or to be determined as directed by the cheque; or

(b) In a currency other than the currency in which the amount of the cheque is expressed.

Relevant legislation

BEA — section 9.

UCC — section 3-106.

ULC — article 36.

Cross references

Amount of the cheque: article 10.

Rate of exchange: article 64.

Commentary

1. The sum payable by a cheque is a definite sum only if its amount can be determined *ex facie* the instrument without reference to evidence or sources extrinsic to it.

2. Paragraphs (a) and (b) sanction the common practice of cheques drawn in a currency which is not the currency of the place of payment. If no rate of exchange is indicated on the cheque or the cheque contains no directions to that effect, article 64 applies.

3. Paragraph (a) is intended to cover cheques drawn, for example, as follows: "Pay £5,000 in Swiss francs at the rate of exchange of (x) Swiss francs to one pound sterling".

Article 9

Any stipulation on a cheque that it is to be paid with interest is deemed not to have been written.

Relevant legislation

BEA — section 9.

UCC — section 3-106.

ULC — article 7.

Commentary

A stipulation of interest on a cheque is deemed not to have been written, i.e. is invalid without affecting the validity of the cheque. The rationale underlying this provision is that the cheque is a payment instrument (for payment on demand) and that stipulation of interest might lead to undesired late presentment.

Article 10

(1) If there is a discrepancy between the amount of the cheque expressed in words and the amount expressed in figures, the amount of the cheque is the amount expressed in words.

(2) If the amount of the cheque is expressed in a currency having the same description as that of at least one other State than the State where payment is to be made as indicated on the cheque and the specified currency is not identified as the currency of any particular State, the currency is to be considered as the currency of the State where payment is to be made.

Relevant legislation

BEA — sections 9 (2) and (3), and 72 (4).

UCC — section 3-118 (c).

ULC — article 9.

Commentary

Paragraph (1)

1. The sum payable by a cheque may be expressed in words only, in figures only, or in words and figures. If both words and figures are used and there is a discrepancy between them, the words control. The paragraph follows in substance the relevant provisions of the principal legislations.

Paragraph (2)

2. This provision envisages the case where a cheque for X dollars is drawn in, say, Toronto, Canada, and made payable in Canberra, Australia. In the absence of any express indication to the contrary, the cheque is then payable in Australian dollars.

Article 11

(1) A cheque is always payable on demand. It is so payable:

(a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or

(b) If no time of payment is expressed.

(2) A stipulation on a cheque that it is payable at a definite time is deemed not to have been written.

Relevant legislation

BEA — sections 10 and 11.

UCC — sections 3-108 and 3-109.

ULC — article 28.

Commentary

1. Under the Convention, there is no formal requirement that the cheque expresses that it is payable on demand.

Article 11 sets forth the basic rule that a cheque is always payable on demand whether or not it so states.

2. If a cheque stipulates that it is payable at a definite time, the stipulation is deemed not to have been written and does not affect the validity of the instrument as a cheque nor does the stipulation detract from the basic rule that a cheque is payable on demand.

Article 12

(1) A cheque may:

(a) Be drawn by the drawer on himself or be drawn payable to his order;

(b) Be drawn by two or more drawers;

(c) Be payable to two or more payees.

(2) If a cheque is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the cheque may exercise the rights of a holder. In any other case the cheque is payable to all of them and the rights of a holder can only be exercised by all of them.

Relevant legislation

BEA — sections 5 and 32 (3).

UCC — sections 3-110 and 3-116.

ULC — article 6.

Commentary

Paragraph (1)

1. Under subparagraph (a) of this paragraph, the drawer of a cheque may address the order to pay to himself, and he may draw the cheque payable to himself or to his order. Therefore, one person may be both drawer and drawee, or both drawer and payee.

2. The purpose of subparagraphs (b) and (c) of this paragraph is to make clear that a written instrument is also a cheque if the direction to pay is made by more than one person or if the persons directed to receive payment are several.

Paragraph (2)

3. This paragraph deals with the case where a cheque is drawn payable to two or more payees. It provides a rule of interpretation whereby, if the cheque does not state expressly that such payees are in the alternative, it is payable to all of them and only all of them can exercise the rights of a holder.

Example. A cheque is drawn payable to A and B. A endorses the cheque to C. What are C's rights? If A has authority to endorse the cheque in the name of B, C is the holder, and has all the rights which a holder has under this

Convention. On the other hand, if A has no authority to endorse the cheque on behalf of B, his signature is not an "endorsement" since it is not signed by the proper persons, i.e., A and B together.

4. Where a cheque provides that it is payable to A or B, every one of them in possession of the cheque is its holder (see definition of holder in article 16); and every one of them in possession of the cheque may exercise the rights of a holder as provided by this Convention.

5. Where a cheque is drawn payable to A and/or B, it is considered to be payable to both A and B, and not any one of them.

Section 3. Completion of an incomplete cheque

Article 13

(1) An incomplete cheque which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) of article 1 may be completed and the cheque so completed is effective as a cheque.

(2) When such a cheque is completed otherwise than in accordance with an agreement entered into:

(a) A party who signed the cheque before the completion may invoke the non-observance of the agreement as a defence against a holder, provided the holder had knowledge of the non-observance of the agreement when he became a holder;

(b) A party who signed the cheque after the completion is liable according to the terms of the cheque so completed.

Relevant legislation

BEA — section 20.

UCC — sections 3-115 and 3-407.

ULC — article 13.

Cross references

Holder: articles 6 (5) and 16.

Knowledge: article 7.

Commentary

1. Article 13 deals with the completion of a writing which lacks one or more of the requirements set forth in article 1 (2) of this Convention: a definite sum of money, the name of the payee or the indication that it is payable to bearer, the name of the drawee, or one or more of the places referred to in article 1 (2) (e). However, the power conferred by article 13 does not include the power to insert: (a) the signature of the drawer and (b) the words "international cheque (Convention of . . .)". Therefore, only an instrument

on which such designation already appears and which is signed by the drawer may be completed as a cheque by inserting such other elements as are required by article 1 (2). The rationale underlying this rule is that only the drawer decides whether the instrument he issues is to be governed by the Convention. It may be noted that a writing which lacks the words "international cheque (Convention of . . .)" may be completed under the applicable national law but would, if completed, not be governed by the Convention.

2. If a writing lacks elements pertaining to one or more of the requirements set out in article 1 (2) it is not a cheque under this Convention and cannot be enforced as a cheque until completed. When the lacking elements have been inserted the writing becomes a cheque within the meaning of article 1 and the Convention is applicable.

3. Article 13 deals with the completion of a cheque which lacks elements that are required for purposes of validity under the Convention. The article does not apply to the alteration or correction of elements that appear on an incomplete or a complete cheque. In the latter case article 33 concerning material alterations applies.

4. The mere fact that a cheque was issued incomplete cannot be set up by a party as a defence against his liability on the cheque as completed. However, if an incomplete cheque is completed otherwise than in accordance with an agreement entered into, two situations affecting the liability of parties to that cheque are envisaged by paragraph (2):

(a) If a party signed the cheque before its completion he may raise the fact that it was completed otherwise than in accordance with the agreement entered into as a defence to his liability against any holder with knowledge of that fact;

(b) If a party signed the cheque after its completion, inobservance of the agreement entered into cannot be set up as a defence to his liability, not even against a holder with knowledge of such inobservance.

Example. An incomplete cheque, containing in the text thereof the words "international cheque (Convention of . . .)" and signed by the drawer is issued to the payee without the sum being stated. It is agreed between the drawer and the payee that the sum to be inserted should be "X". Contrary to this agreement the payee inserts sum "Y" and endorses the cheque to A. What are A's rights? If A took the cheque without knowledge of the inobservance of the agreement by the payee he has rights on the cheque, as completed, against the drawer and the payee. If A knew about the inobservance, the drawer may raise a defence based upon the fact that the incomplete cheque was completed contrary to the agreement between himself and the payee. This defence cannot be raised by the payee. If A with knowledge of the inobservance of the agreement transfers the cheque to B who is without knowledge of the inobservance, neither

the drawer nor the payee nor A may raise such inobservance as a defence against B even if B is not a protected holder.

CHAPTER THREE. TRANSFER

Article 14

A cheque is transferred:

(a) By endorsement and delivery of the cheque by the endorser to the endorsee; or

(b) By mere delivery of the cheque if it is drawn payable to bearer or if the last endorsement is in blank.

Relevant legislation

BEA — sections 22 (2) and 31.

UCC — section 3-202 (1).

ULC — article 14.

Cross reference

Endorsement: article 15.

Commentary

1. A negotiable instrument, by its nature, is transferable although parties may exclude or limit its transferability (see article 18). The transfer of an instrument is in some legal systems known as "negotiation".

2. Article 14 sets forth the ways in which a cheque may be transferred. It follows in substance the relevant provisions of the existing legal systems. A cheque is transferred when the holder endorses it, either specially or in blank, and delivers it to the endorsee (paragraph (a)) or, if the last endorsement is in blank, when the holder delivers the cheque (paragraph (b)).

3. When a cheque is transferred under this article, the transferee becomes a holder (cf. articles 6 (5) and 16 (1) (b)) and thus acquires the rights, and is subject to all the duties, of a holder.

Example A. The payee endorses the cheque specially to A and delivers it to A. By these acts the cheque is transferred to A and A becomes the holder of it.

Example B. The payee endorses the cheque specially to A but does not deliver it to A. Without further endorsement the payee delivers the cheque to B. The cheque is not transferred either to A or to B. Neither A nor B is a holder.

Example C. The payee endorses a cheque in blank and delivers it to A. The cheque is thereby transferred to A who becomes its holder. If A delivers the cheque to B, even without endorsement, the cheque is thereby transferred to B and B is the holder.

4. It should be noted that article 14 deals only with the transfer of a cheque by endorsement and delivery or, if the

last endorsement is in blank, by mere delivery. The article does not deal with other ways by which a person may acquire the rights to and upon a cheque, as where a person is the heir of the holder or where the holder assigns his rights on the cheque to another person. These questions are left to the applicable national law.

Article 15

(1) An endorsement must be written on the cheque or on a slip affixed thereto (*allonge*). It must be signed.

(2) An endorsement may be:

(a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the cheque is payable to any person in possession thereof;

(b) Special, by a signature accompanied by an indication of the person to whom the cheque is payable.

Relevant legislation

BEA — sections 2 and 32.

UCC — section 202 (2).

ULC — article 16.

Cross reference

Signature: article 6 (8).

Commentary

1. An endorsement serves two functions. It is a necessary element in the transfer of an order cheque (article 14 (a)), and it renders the endorser liable on the cheque as a party (article 38 (1)). In most cases, the endorsement is intended to serve both functions. However, the endorser may exclude or limit the liability function of the endorsement by an express stipulation on the cheque as provided in article 38 (2), e.g. by inserting the words "without recourse". Also the endorser can exclude or limit the transfer function as regards any possible transfer from his endorsee to others. For example, he may exclude the possibility that a person other than his endorsee becomes a holder except for purposes of collection. He would achieve this by inserting in his endorsement the words "not transferable", "pay (X) only" or words of similar import (article 18).

2. Article 15 explains what is meant by endorsement and how it is effected. An endorsement is effected by the signature of the person endorsing the cheque.

3. The endorsement may be a special or a blank endorsement. A special endorsement is effected by the signature of the endorser accompanied by an indication of the person to whom the cheque is payable (paragraph (2) (b)). A blank endorsement may be effected by the endorser's signature alone or by a signature combined with a statement to the effect that the cheque is payable to any person in possession thereof (paragraph (2) (a)).

Example. The payee signs "Pay A". This is a special endorsement to A. However, when the payee signs his name or accompanies his signature by such words as "Pay any person" or "Pay bearer", the endorsement is a blank endorsement.

4. It should be noted that a signature alone on the cheque is not necessarily a blank endorsement; it may be a guarantee (cf. article 40) or a certification (cf. article 36).

Article 16

(1) A person is a holder if he is:

(a) In possession of a cheque drawn payable to bearer; or

(b) The payee in possession of the cheque; or

(c) In possession of a cheque which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

(2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.

(3) A person is not prevented from being a holder by the fact that the cheque was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon the cheque.

Relevant legislation

BEA — section 2.

UCC — sections 1-201 (20) and 3-202 (1).

ULC — article 19.

Cross references

Holder: article 6 (5).

Payee: article 6 (4).

Endorsement: article 15.

Commentary

1. Under the Convention the concept of "holder" is relevant in, *inter alia*, the following contexts:

(a) Being a holder is a necessary element of the status of a protected holder (cf. article 6 (6));

(b) The holder may exercise all rights on the cheque against the parties to it (cf. article 26);

(c) A party to a cheque is discharged when he pays the holder (cf. article 61).

2. Pursuant to article 16 a person in order to be a holder:

(a) Must be in possession of the cheque; and

(b) Must be a payee, or a bearer, or a transferee under a special endorsement or an endorsement in blank.

Example A. The drawer issues a cheque and delivers it to the payee. The payee is a holder.

Example B. The payee lost the cheque. Not being in possession of the cheque he is not a holder (as to lost cheques see articles 73-78).

Example C. The payee endorses the cheque to A and delivers it to A. A is a holder.

Example D. The payee endorses the cheque to A and delivers it to B. Neither A nor B is a holder.

Example E. The payee endorses the cheque in blank and delivers it to A. A is a holder.

Example F. The drawer issues a cheque payable to bearer and delivers it to A. A is a holder. A delivers it to B. B is a holder.

Example G. The drawer issues a cheque made payable to bearer. It is stolen by T. T is a holder.

3. Under this Convention a drawer or a guarantor is not a holder even though he be in possession of the cheque unless he acquired the cheque under an endorsement in blank or the cheque has been drawn payable to bearer. However, these parties have rights to and upon the cheque by virtue of special provisions in this Convention.

Example H. The drawer of a cheque which is not made payable to bearer and on which the last endorsement is not in blank dishonours it by non-payment. The holder is paid by the drawer and delivers the cheque to him without an endorsement. The drawer, though in possession of the cheque, is not a holder.

4. A payee or an endorsee may reacquire the cheque by payment or otherwise. By virtue of article 23 such a payee or endorsee, even though the cheque is not endorsed to him, is a holder.

5. For the purposes of holder status it is irrelevant whether the possession of the cheque is lawful or not. As seen from example G above even a thief may be a holder. However, if the possession is unlawful the owner of the cheque has a valid claim to the cheque and such claim may be set up as a defence against liability (cf. article 27).

6. To be a holder the possessor of a cheque need not be the owner of it. Where a cheque is endorsed "for collection" the endorsee in possession is the holder of it even though he may be only an agent of the endorser rather than the owner of it.

"Uninterrupted series of endorsements"

7. The question whether the possessor of the cheque is a holder is to be determined only from what appears on the cheque. It is necessary, but it suffices, that the chain of endorsements: (a) is uninterrupted and (b) designates

the possessor as the last endorsee unless the last endorsement is in blank.

Example I. The cheque is stolen from the payee. T, the thief, forges the signature of the payee and endorses the cheque to A. A is a holder. However, the drawer may raise the defence of forgery against A (cf. article 27). Such a defence would not prevail if A is a protected holder (cf. article 28). The payee may claim the cheque from A (cf. article 27 (2)) unless A is a protected holder.

Example J. The payee delivers the cheque to A without an endorsement. A endorses the cheque to B. B is not a holder because the endorsement that is necessary for the establishment of an uninterrupted chain of endorsements (the endorsement of the payee to A) is lacking.

Paragraph (2)

8. The provision of paragraph (2) may be illustrated by the following example:

Example K. The payee endorses the cheque to A and delivers it to him. A endorses the cheque in blank and delivers it to B. B endorses the cheque specially to C or in blank and delivers it to C. Under article 16 (2), B is deemed to be the endorsee of A by his endorsement in blank. It follows that C is a holder since he received the cheque under an uninterrupted series of endorsements.

Paragraph (3)

9. The purpose of this paragraph is to provide that the transferee is a holder even though the transferor is a person without legal capacity, or the endorsement or delivery was obtained by fraud or other illegal means. The main importance of this provision lies in the fact that such transferee, being a holder, may qualify himself in proper circumstances as a protected holder. Even if such holder is not a protected holder he may transfer the cheque to a person who may take it in proper circumstances as a protected holder.

10. This paragraph does not deal with the question of liability upon a cheque of the party transferring it, nor does it deal with the rights of a person to the cheque. The party transferring the cheque may assert any defence or any claim available to him under articles 27 and 28 of this Convention.

11. Paragraph (3) does not impose any liability on a party who signed the cheque under the circumstances mentioned in the paragraph. The question whether such party may raise the defence of *ius tertii* is governed by article 27 (3).

Example L. A induces the payee by way of fraud to endorse to him a cheque owned by the payee. Pursuant to article 16 A is a holder of the cheque. The consequences are shown by the following examples.

Example M. The same facts as in example *L*. A brings an action against the payee (P). Nothing in this article makes the payee (P) liable to A in spite of the fraud practised by A on P. Pursuant to article 27 the payee has a valid defence to A's action.

Example N. The same facts as in example *L*. The payee (P) brings an action against A to recover the cheque or to prohibit A from transferring the cheque. The payee (P) will succeed if remedies of this type are permitted under the law of the place where the transfer took place.

Example O. The same facts as in example *L*. A brings an action against the drawer. This question is not solved by article 16. The answer to this question is to be found in article 27.

Example P. By fraud A induces the payee (P) to transfer to him a cheque owned by P. A transfers the cheque to B, who takes it as a protected holder. P brings an action against B for conversion of the cheque. P's action fails. According to article 16 A is a holder, and the cheque was transferred to B in circumstances that make B a protected holder. According to article 28 P's claim fails against a protected holder.

Example Q. The same facts as in example *P*. B brings an action against the drawer and the payee (P). According to article 28 the defences of the drawer and the payee are not available against B, a protected holder.

Article 17

The holder of a cheque on which the last endorsement is in blank may:

- (a) Further endorse the cheque either in blank or to a specified person; or
- (b) Convert the blank endorsement into a special endorsement by indicating therein that the cheque is payable to himself or to some other specified person; or
- (c) Transfer the cheque in accordance with paragraph (b) of article 14.

Relevant legislation

BEA — section 34 (4).
UCC — section 3-204.
ULC — article 17.

Cross references

Holder: article 16.
Endorsement: article 15.
Transfer: article 14.

Commentary

1. If the last endorsement on a cheque is in blank and the holder transfers the cheque, several situations may arise

which in various ways determine whether the transferor is liable on the cheque, as shown by the following examples.

Example A. The holder A delivers the cheque to B. This is a proper transfer (cf. article 14 (b)) and B is a holder under article 16 (1) (b). A is not liable on the cheque because he has not signed it (cf. article 31). However, he may be liable off the instrument under article 39. The instrument remains an instrument payable to bearer.

Example B. A, the holder, delivers the cheque to B after endorsing it in blank. This is a proper transfer under article 14 (b) and B is a holder. A is liable on his signature as an endorser. It may be noted that A's signature is not required for the purpose of transferring the cheque to B (the cheque is a bearer cheque by reason of the blank endorsement). The effect of A's blank endorsement is to render A liable on the cheque and this may be commercially expedient.

Example C. A, the holder, delivers the cheque to B after having converted the blank endorsement into a special endorsement (by indicating in that endorsement that the cheque is payable to B). This is a proper transfer under article 14 (a) and B is a holder. A is not liable on the cheque because he has not signed it (cf. article 31). The conversion of a blank endorsement into a special endorsement is authorized under article 17 (b) and is therefore not a material alteration under article 33.

2. It should be noted that a special endorsement of a cheque made payable to bearer does not convert the cheque into an order instrument. Thus, a bearer cheque with such a special endorsement may be transferred by mere delivery.

Article 18

When the drawer of a cheque payable to a payee or to his order has inserted in the cheque, or an endorser in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the transferee does not become a holder except for purposes of collection.

Relevant legislation

BEA — sections 8 (1) and 35.
UCC — sections 3-205, 3-206 and 3-805.
ULC — article 18.

Cross references

Holder: article 16.
Endorsement: article 15.
Transfer: article 14.
Collection: article 22.

Commentary

1. Under article 18 the transfer of a cheque in accordance with article 14 may be excluded or limited by the

drawer or an endorser by using such words as "not negotiable", "not transferable" or words of similar import. The drawer must insert these words in the cheque, and the endorser would have to insert them in his endorsement.

2. The purpose of such insertion is to ensure that payment of the cheque may only be claimed by the payee or the endorsee or the agent for collection, as the case may be. This insertion does not affect the character of the instrument as a cheque but the endorsee does not become a holder except for purposes of collection. He may not further transfer the cheque, not even for purposes of collection; he would have this latter power only if the endorsement to him would have been made expressly for purposes of collection (cf. article 22).

3. Under article 1 (2) of this Convention a cheque need not be made payable to "the order" of the payee. Therefore, a mere omission of the words "to order" does not prevent further transfer, and where a cheque lacking that expression is transferred by the payee in accordance with article 14 the transferee is a holder and may in turn further transfer the cheque.

4. If the words "not negotiable" are inserted in a crossed cheque, the effects of the insertion are different. Under article 71 the transferee of such a cheque does become a holder and may transfer the cheque further. However, the transferee cannot become a protected holder in his own right.

Article 19

- (1) An endorsement must be unconditional.
- (2) A conditional endorsement transfers the cheque whether or not the condition is fulfilled.

Relevant legislation

BEA – section 33.
UCC – section 3-202.
ULC – article 15.

Cross references

Transfer: article 14.
Endorsement: article 15.

Commentary

1. Article 19 expresses the fundamental policy of the Convention that an endorsement may not be made subject to a condition (paragraph (1)).

2. If an endorsement contains a condition the endorsement is a valid endorsement for purposes of transferring the cheque and the transferee is a holder whether or not the condition has been fulfilled. Furthermore, the condition to the extent that it affects the liability of the endorser is to be disregarded. However, the fact that a condition was

not fulfilled is not necessarily irrelevant. It may, for example, form the basis of a claim or defence under article 27 if the condition relates to the underlying transaction. For that reason, the same result would obtain if the condition had not been included in the endorsement but was only expressed in the agreement of the underlying transaction.

3. It should be noted that article 19 deals only with conditions in the proper sense of the term, i.e. making the liability of the endorser dependent upon the occurrence or non-occurrence of an uncertain future event. Thus, the article does not cover other ways of excluding or limiting the liability as, for example, where a cheque is endorsed partially (article 20) or without recourse (article 38 (2)).

Article 20

An endorsement in respect of a part of the sum due under the cheque is ineffective as an endorsement.

Relevant legislation

BEA – section 32 (2).
UCC – section 3-202 (3).
ULC – article 15.

Cross references

Endorsement: article 15.
Sum payable: article 8.

Commentary

1. This article provides that an endorsement must be of the entire cheque; therefore, a partial endorsement is not effective as an endorsement. An endorsement is partial if, for example, it states "Pay one half of the sum due to A" or "Pay half of the sum due to A and half to B". However, an endorsement is not partial if, for example, it states "Pay A and B" or "Pay A or B" since the full sum due is then payable to the person(s) indicated. A special problem arises when a cheque has been paid in part. If in such a case an endorsement is limited to the part unpaid, it is "partial" in the sense of article 20 and therefore ineffective. If however the endorsement is not so qualified, it is a valid endorsement although in fact it is only for part of the sum, namely for the amount unpaid.

2. The "transferee" of a cheque endorsed as to part of the sum payable does not qualify as a holder since the endorsement is ineffective. However, article 20 does not prevent such person from acquiring rights under the partial endorsement under the applicable domestic law (e.g. by "partial" assignment).

Article 21

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the cheque.

Relevant legislation

BEA – section 32 (5).
UCC – section 3-414 (2).

Cross reference

Endorsement: article 15.

Commentary

The purpose of this article is to establish a presumption of fact as to the chronological order in which two or more endorsements were made. The article thereby establishes a presumption of rank for the purpose of the right of recourse by an endorser who paid the cheque against prior endorsers. The article is also relevant for determining to what extent the discharge of one endorser discharges subsequent endorsers. Extrinsic evidence may be brought to rebut the presumption of fact and to prove the true order of endorsements.

Example. A cheque shows blank endorsements in the following order: (signed) Payee; (signed) A; (signed) B. Upon dishonour of the cheque the holder C exercises his right of recourse against A. Payment by A discharges B. However, if A proves that he endorsed after B had endorsed, the presumption is rebutted. In such a case B is not discharged and A, upon payment, has a right of recourse against B.

Article 22

(1) When an endorsement contains the words “for collection”, “for deposit”, “value in collection”, “by procuration”, “pay any bank”, or words of similar import, authorizing the endorsee to collect the cheque (endorsement for collection), the endorsee:

- (a) May only endorse the cheque for purposes of collection;
 - (b) May exercise all the rights arising out of the cheque;
 - (c) Is subject to all claims and defences which may be set up against the endorser.
- (2) The endorser for collection is not liable upon the cheque to any subsequent holder.

Relevant legislation

BEA – section 35.
UCC – sections 3-205 and 3-206.
ULC – article 23.

Cross references

Endorsement: article 15.
Claims and defences: article 27.

Commentary

1. A holder, in order to obtain payment, would normally present the cheque himself to the person liable. However, particularly in the international context, he will engage an agent (usually a bank) to do so on his behalf.

2. For that purpose, he may, for example, use the means of a regular endorsement, whether blank or special, accompanied by collecting instructions outside the cheque. He may, however, prefer an endorsement for collection as provided for in article 22 which would avoid certain risks inherent in the first approach. These risks arise from the fact that the agent for collection may disregard his instructions and further endorse the cheque to a person who may not know about the collection instructions and may thus qualify as a protected holder and exercise rights of a protected holder against the endorser whose endorsement was intended only for collection purposes. These risks cannot materialize where an endorsement for collection is made in accordance with article 22.

Example A. The payee endorses the cheque “for collection” to A. Fraudulently and without the permission of the payee the cheque is sold (and endorsed in blank) by A to B. The drawee refuses payment, and B brings an action against the payee. By virtue of paragraph (2) the payee is not liable to B. In that respect an endorsement for collection resembles an endorsement “without recourse” (see article 38 (2)).

3. Since the endorsee for collection acquires his rights through an endorsement, he is a holder if he is in possession of the cheque. Thus, he may exercise the rights, and is subject to the duties, of a holder.

Example B. By fraud the payee induces the drawer to draw a cheque payable to the payee. The payee endorses the cheque “for collection” to A. A brings an action on the cheque against the drawer. By virtue of paragraph (1) (b) the drawer, since he may raise the defence of fraud against the payee, may raise it also against the payee’s endorsee for collection.

4. However, the legal position of a holder under an endorsement for collection differs from that of a “normal” holder since the endorsee for collection acts as an agent of the endorser. The difference manifests itself in the following rules expressed in article 22:

(a) The endorsee for collection may not further endorse the cheque for any purpose other than for collection. Any subsequent endorsee will also be an agent for collection. This result obtains even though the subsequent endorsement is not made expressly for collection since the first endorsement controls;

(b) The endorsee for collection may exercise rights against any party who is liable to the endorser for collection, including the right to bring an action on the cheque. The endorsee for collection has no rights on the cheque against the endorser for collection since the purpose of the

endorsement is to collect the cheque for the endorser and not from him. In this respect, an endorsement for collection is an endorsement that excludes the liability of the endorser and is thus similar to an express stipulation provided for in article 38 (2);

(c) The endorsee for collection cannot be a protected holder in his own right. However, if the endorser for collection is a protected holder, the transfer of the cheque to the agent for collection vests in him the rights on and to the cheque which the protected holder had (article 29). It follows that the endorsee for collection is subject only to those claims and defences which may be set up against the endorser.

5. It should be noted that the Convention does not deal with the legal relations between endorser and endorsee for collection outside the cheque, e.g. the circumstances under which the underlying agency relationship is terminated. However, such termination may form the basis of a claim by the endorser for collection which, if asserted, may be set up as a defence against the holder (i.e. the ex-agent, see article 27 (3)) or may lead to the result that payment to the holder does not discharge the payer (cf. article 61 (2)).

Article 23

(1) The holder of a cheque may transfer it to a prior party in accordance with article 14; nevertheless, in the case where the transferee was a prior holder of the cheque, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

(2) The endorsement to the drawee operates only as an acknowledgement that the endorser has received from the drawee the amount of the cheque except in the case where the drawee has several establishments and the endorsement is made in favour of an establishment other than that on which the cheque has been drawn.

Relevant legislation

BEA – sections 37 and 59 (2) (b).
UCC – section 3-208.
ULC – articles 15 and 47.

Cross references

Transfer: article 14.
Holder: articles 6 (5) and 16.

Commentary

Paragraph (1)

1. A cheque may be transferred to a prior party (an endorser or the drawer) or to the drawee. If the prior party was a holder no endorsement is necessary. Therefore, transfer of the cheque to the drawer (i.e. transfer within the meaning of article 14) requires an endorsement unless the last

endorsement is in blank. A prior party who is a holder may further transfer the cheque.

2. Paragraph (1) also provides that a prior holder who acquires the cheque without an endorsement may strike out any endorsement which would prevent him from being a holder. Such striking out is not a material alteration.

Example. The payee endorses the cheque to A. A endorses to B. B endorses to C. C delivers the cheque to A upon payment by A. A may strike out his own endorsement to B and the endorsement of B to C.

Paragraph (2)

3. If, upon payment, the holder of a cheque "endorses" it, either specially to the drawee or in blank, the drawee does not thereby become a holder. Thus, he may not further transfer the cheque and he does not have the rights of a holder. Under paragraph (2), such an endorsement operates only as a receipt.

4. Paragraph (2) states as an exception to the rule that the endorsement to the drawee is no endorsement the case where payment is made by an establishment of the drawee other than the establishment of the drawee on which the cheque was drawn. In such a case, the endorsement is an endorsement in favour of the establishment of the drawee which paid the cheque and that establishment will thus be a holder.

Article 24

A cheque may be transferred in accordance with article 14 after the expiration of the period of time for presentment.

Relevant legislation

BEA – section 36.
UCC – section 3-304 (3).
ULC – article 24.

Cross reference

Transfer: article 14.

Commentary

If a cheque is transferred after the period of time for presentment has expired, the transferee under article 24 is a holder. This rule stresses the essential characteristic of a cheque, namely its transferability.

Article 25

(1) If an endorsement is forged, any party has against the forger, and against the person to whom the cheque was directly transferred by the forger, the right to recover compensation for any damage that he may have suffered because of the forgery.

(2) Except to the extent provided in articles 70 and 72, the liability of a party or of the drawee who pays, or of an endorsee for collection who collects, a cheque on which there is a forged endorsement is not regulated by this Convention.

(3) For the purposes of this article, an endorsement placed on a cheque by a person in a representative capacity without authority or exceeding his authority has the same effects as a forged endorsement.

Relevant legislation

BEA — sections 24, 59 and 60; Cheques Act — sections 1 and 4.

UCC — sections 3-404, 3-405 and 3-603; 4-207 and 4-212.

ULC — articles 15, 34 and 35.

Cross references

Forged signature: article 6 (8).

Transfer: article 14.

Endorsement for collection: article 22.

Endorsement by a person in a representative capacity: article 34.

Commentary

1. Where an endorsement on a cheque has been forged, one of the parties must bear the risk of loss. The problem of who should bear that risk is solved in a fundamentally different way in the common and civil law systems. The reasons for this divergence in approach are based on a different appreciation of what is commercially expedient and what policy considerations should prevail, even though the rationalization of certain aspects of the rule may have occurred after its formulation. While there are other issues of negotiable instruments law where the two systems are in sharp contrast, the rule on forged endorsements can be said to present the most striking conflict between them.

2. The BEA, the UCC and the ULC all recognize the basic principle that a person whose signature is forged on a cheque is not liable thereon (BEA section 24; UCC section 3-404 (1); ULC article 10) and that the person who forges the signature of another person is liable on the cheque as if he had signed his own name. The basic point on which the two systems differ is the effect of the transfer of a cheque bearing a forged endorsement. Who is the owner of the cheque? What are the rights and liabilities of the various parties to the cheque and of the drawee who pays on a forged endorsement and the person whose endorsement was forged?

THE EXISTING LEGAL SYSTEMS

Anglo-American Law

3. Under the common law statutes a forged endorse-

ment, subject to certain exceptions, is wholly inoperative "as that of the person whose name is signed" (UCC section 3-404 (1)) and "no right to retain the bill or to give discharge therefor or to enforce payment thereof against any party thereto can be acquired through or under that signature" (BEA section 24).

4. The effects of this basic rule are several. Since an order instrument is negotiated by delivery with any necessary endorsement and a forged signature is inoperative as an endorsement, without such negotiation the transferee does not become a holder. The same is true for any subsequent transferee, whether or not he acts in good faith. Because the endorsement is inoperative, it cannot make the cheque payable to bearer either. Possession of the cheque does not confer title to it nor the right to enforce it against parties who signed it prior to the forged endorsement. In respect of persons (including collecting banks) that transfer the cheque subsequent to the forged endorsement, the UCC provides for a warranty given by such transferor, who receives consideration, "that (a) he has a good title to the item or is authorized to obtain payment or acceptance on behalf of one who has a good title and the transfer is otherwise rightful; and (b) all signatures are genuine or authorized" (UCC section 4-207 (2) (a) and (b)). This warranty runs to the immediate transferee and to any subsequent collecting bank who takes the item in good faith. A warranty of title runs also to the "payor bank or other payor who in good faith pays or accepts the item" (UCC section 4-207 (1) (a)). The BEA provides in this respect that an endorser is estopped from raising against subsequent transferees the fact that an endorsement was forged (section 55 (2) (c)). In the case of a bearer cheque any person who negotiates it warrants to his immediate transferee for value that there are no prior forged endorsements (section 58 (3)).

5. Payment on a forged endorsement does not discharge the drawee's debt to the drawer since payment is not to the holder. According to the BEA such payment does not qualify as payment in due course to the holder. As a result the drawer is entitled to demand that the drawee reverse the charge by recrediting his account. An exception to this rule is found in section 60 of the BEA in respect of cheques (see also section 1 of the Cheques Act, 1957). If a banker pays a cheque in good faith and in the ordinary course of business it is not incumbent on him to show that any endorsement on the cheque was made by or under the authority of the person whose endorsement it purports to be; and he is deemed to have paid the cheque in due course although the endorsement has been forged or made without authority. Therefore, such payment discharges the cheque and the banker is entitled to debit the drawer's account. Under the UCC a cheque bearing a forged endorsement is not "properly payable" (section 4-401 (1)) and since the payee or the endorsee whose endorsement was forged has not signed, the drawee who pays does so without instructions and in violation of the drawer's order.

6. The payee or the endorsee whose signature is forged retains title to the cheque and the cheque remains payable to him. He may exercise his rights to it by an action for conversion outside the cheque or, alternatively, by an action on the cheque under the provisions of lost cheques. Thus if the drawee pays to someone else and receives the cheque he is liable for conversion to such payee or endorsee on an action in tort outside the cheque and the drawer may still be liable on the cheque to such payee or endorsee. In this respect, the Cheques Act sets forth an exception: a collecting bank which receives payment for its customer is not liable for conversion if it collects the cheque in good faith and without negligence (section 4). Similarly, if a drawee-bank pays a cheque on which there is a forged endorsement in good faith and in the ordinary course of business it is deemed to have paid the cheque in due course and is therefore not liable for conversion.

7. Under the UCC, the drawee who paid the cheque in good faith may recover from the person paid. Under section 4-207 (1) (a), the drawee may shift the loss to the person who received payment by a claim for breach of warranty of title. Under the BEA, if a banker pays a cheque drawn on him in good faith and in the ordinary course of business, such payment is payment in due course and he may debit the account of the drawer. Therefore, he may not opt to recover, instead, the money paid from the person who received payment.

The Geneva Uniform Law

8. The approach of the ULC is fundamentally different from that of the common law. According to article 19 of that law the person who is in possession of an endorsable cheque and establishes his title to it through an uninterrupted series of endorsements is considered to be the lawful holder (*porteur légitime*). These two conditions establish what is often referred to by civil law authors as *légitimation formelle*, a term for which there is no correct equivalent in the English language. They establish a presumption that the possessor of a cheque on which there appears an uninterrupted chain of endorsements has title to it and, as such, is entitled to exercise all rights derived therefrom. The presumption is rebuttable: the true owner may claim the cheque but will succeed only if he proves that the holder, though the conditions set forth in article 19 of the ULC may be met, acquired it in bad faith or in acquiring it has been guilty of gross negligence. In the context of forged endorsements this means that the status of lawful holder which article 19 bestows upon the possessor is not available if the possessor was aware or should have been aware that the endorser was not the true owner of the cheque and that the endorsement was forged or made by an agent without authority.

9. Therefore, under the ULC a forged endorsement is, with respect to the rights of the taker from the forger, a valid endorsement provided that the taker meets the conditions

set forth in article 19. It is also a valid endorsement with respect to the rights of subsequent endorsees even if they knew about the earlier forgery. The dispossessed owner may claim the cheque from the person who took it from the forger, but if such person is a lawful holder the dispossessed owner will succeed only if he proves bad faith or gross negligence. Since a lawful holder, in the absence of bad faith or gross negligence, is not bound to give up the cheque he may exercise the rights on the cheque. Parties to the cheque, whether they signed before or after the forgery, are liable to the lawful holder.

10. The presumption which article 19 establishes is also relevant in the context of payment of the cheque by the drawee (or by any party liable): he may act in reliance on the apparent title. If the holder establishes his title to the cheque through an uninterrupted series of endorsements, the drawee who pays in reliance on such series of endorsements may debit the account of the drawer. The drawee (or the party who pays the cheque) is not bound to verify the signatures of the endorser (article 35).

Who bears the risk of a forged endorsement?

11. The basic difference, in terms of bearing the risk of a forged endorsement, between the ULC and the BEA and UCC approach is the following: according to the ULC the risk of the forged endorsement rests upon the owner of the cheque from whom it was stolen, whilst according to the BEA and the UCC the risk rests upon the person who took the cheque from the forger. The different results under the two main systems are shown by the following example:

Example A. The drawer issues a cheque to the payee (P). T steals the cheque from P. The thief (T) forges P's signature and "endorses" the cheque to A who takes it without knowledge of the theft and forgery. A endorses it to B who takes it without knowledge of the theft and forgery. B endorses the cheque for collection to bank C which receives payment from the drawee-bank which pays without knowledge. The drawee debits the drawer's account.

Under the ULC, the payment by the drawee operates as a discharge of his debt to the drawer, and the drawee is entitled to debit the drawer's account (i.e., the risk is not upon the drawee). As the cheque is paid to the person entitled to payment, the drawer discharges his obligation to the payee (i.e., the risk is not upon the drawer). The risk of forgery rests, therefore, according to the ULC, on the payee, the owner of the cheque who lost possession of it and who has no rights against A, B, the collecting bank C, and the drawee.

Under the UCC, payment by the drawee does not discharge his debt to the drawer and the drawee is not entitled to debit the drawer's account. The drawee has not properly paid the cheque (section 4-401) since he has not paid it in accordance with the instructions of the drawer: he has not paid to the holder. As a result the risk does not

rest with the drawer. However, the drawer does not gain from the forgery since he is still liable on the cheque to the payee. The drawee is entitled to recoup his loss by shifting it to the collecting bank C, and C in turn may shift the loss to B, and B to A (i.e., the risk is not upon the drawee, the collecting bank C, or B). A cannot shift the risk back.

Under the BEA, as under the UCC, the risk of forgery falls on A; however, this result is achieved by a different approach since under the BEA the drawee-bank is not liable for conversion if it paid the cheque in good faith and in the ordinary course of business and the collecting bank is not liable if it collected the cheque in good faith and without negligence (Cheques Act section 4). Thus, under the BEA payment by the drawee to the collecting bank is payment in due course and the drawee is entitled to debit the drawer's account with him (i.e., the risk is not upon the drawee or the drawer). The risk at this point is on the payee who has no right on the cheque against the drawer. However, the payee may shift the risk to B who is liable to the payee for converting the cheque. B is entitled to recoup his loss by shifting it to A (i.e., the risk is not upon B). A cannot shift the risk back. He will bear it. Consequently, under the BEA, as under the UCC, the risk falls on the person who took the cheque from the forger.

Identical results are reached under the ULC, the UCC and the BEA if a cheque is stolen from the post before it reaches the payee.

The advantages and disadvantages of the two approaches to forgery

12. The main advantages of the ULC, as compared to the BEA and UCC, are said to be the following:

(a) The ULC promotes circulation and payment of transactions by cheques, since any possessor without knowledge is assured that a previous forged endorsement has no effect on his rights to and upon the cheque. Under the BEA and UCC, on the other hand, a person without knowledge may be hesitant in taking a cheque since he may have no right to or upon it if there is a previous forged endorsement;

(b) The ULC rule gives greater finality of payment. If a cheque is given in payment the payment will be final once the cheque is paid by the drawee and it is no longer necessary to inquire whether the transferor or the transferee had rights to or upon the cheque. In that respect payment by way of a cheque resembles payment by way of money. Under the ULC once the drawee paid the cheque without fraud or gross negligence on his part, and provided the cheque shows a regular series of endorsements, the payment is final. The relations between the drawer and the drawee, the payee and the drawer (if the cheque was stolen from the payee), and the endorsees amongst themselves, are settled promptly

and with finality. On the other hand, under the BEA and UCC, the transactions must be reopened;

(c) The ULC rule provides economy of remedies. Pursuant to the ULC, when the drawee pays and debits the drawer's account, the risk of the forgery is automatically imposed on the party who should, under the ULC bear the risk (i.e., the owner of the cheque). There is no need for any action or litigation in order to impose the risk on such party. On the other hand, according to the BEA and UCC, a series of actions or remedies may be necessary to transfer the loss to the one ultimately responsible (i.e. the person who took from the forger). One may envisage several actions (and therefore possible disputes) before the risk rests on the taker from the forger.

13. The main advantages of the approach of the BEA and UCC, as compared to the ULC, are the following:

(a) It encourages the use of a cheque by the drawer as a means of payment, since the drawer is assured that he will not bear the risk of any forgery of an endorsement. Especially, it encourages the use of the mail as a means to transfer cheques from the drawer to the drawee. Under the ULC, on the other hand, the potential drawer of a cheque may be hesitant to issue it and to send it by post, since he may bear the risk if the cheque is stolen from the post before it reaches the payee;

(b) The BEA-UCC approach puts the risk of forgery on the person who dealt with the forger. That party ought to bear the risk since he can most easily prevent it. The endorsee should know his endorser. He should not take the cheque from a stranger. The ULC, on the other hand, imposes the risk of forgery on the owner of the cheque, who under normal and efficient procedures for handling cheques (including the use of mail) cannot prevent theft and forgery of the cheque.

14. It is to be noted that the above-mentioned advantages that are said to be inherent in one or the other system do not appear, in actual practice, to be absolute. For instance, the principal reason advanced during the 1931 international conference in favour of articles 19 and 35 of the ULC was that only by protecting the possessor of a cheque who took it in good faith would the cheque be susceptible of easy circulation and that circulation would be impeded if one would oblige the endorsee or the drawee to verify the signature of all preceding endorsers who would be mostly unknown to him. However there is no proof that the common law rule has in any way impeded circulation or that cheques subject to the rules of common law jurisdictions are in practice less negotiable. Nor, it would appear, has the alleged disadvantage of the ULC rule — that it discourages the use of a cheque by the drawer because he bears the risk of the forgery of an endorsement — led to a decrease in the issuance of cheques in countries operating under the ULC system. The other objection is that the ULC rule encourages laxity in cheque transactions because there is little risk in buying

a cheque from a stranger, while the common law rule prevents this by imposing the risk on the purchaser, appears to be refuted by the near-absence of forged endorsements on instruments in civil law countries.

15. There are other rationalizations of the rules on forged endorsements that concern their procedural effects. It is certainly true that the ULC achieves finality of payment in that, once the cheque is paid by the drawee under the conditions laid down by article 35 of that Law, the drawee may debit the account of the drawer and his relations with the drawer are settled. But it is at least arguable whether this is the most appropriate solution and whether it is not preferable to protect the interests of the drawer by accepting the inconvenience of reopening the transactions.

16. It would thus appear that the so-called advantages of each legal system cannot provide absolute criteria for the formulation of new uniform rules.

Article 25 of the Convention

17. Article 25 attempts to bridge the basic differences between the common law rules and those of the ULC. The legal effects of this article and of article 16 are the following:

(a) A forged endorsement or an endorsement signed without authority is effective as an endorsement if it is part of an uninterrupted series of endorsements;

(b) Any party who suffered damages because of the forgery has a right for damages against the forger and against the person to whom the forger directly transferred the cheque.

18. As a result:

(a) The person who acquired the cheque through an uninterrupted series of endorsements is a holder even if one or more endorsements were forged. As a holder he has all the rights conferred on him by the Convention;

(b) The person who ultimately bears the risk of loss is the forger or, if he cannot be found or is insolvent, the person who took the cheque from the forger.

Example B. The drawer issues a cheque to the payee (P) who receives it. T steals the cheque from P. T forges P's signature and "endorses" the cheque to A who takes it without knowledge of the forgery. A endorses it to B who takes it without knowledge of the forgery. B endorses it for collection to bank C. Bank C receives payment from the drawee. The drawee debits the drawer's account. Who bears the risk?

Payment by the drawee effects a discharge of his debt to the drawer (consequently the risk is not on the drawee). Since the cheque was paid to the person entitled to payment the drawer discharges his obligation to the payee (consequently the risk is not on the drawer). The payee who lost his rights to and upon the cheque is entitled to compensation from T and A for such loss. If T cannot be found or is insol-

vent A cannot shift the risk to anyone else. Therefore, the risk of the forgery rests on A who took the cheque from the forger.

Rationale

19. As pointed out above, each solution to the "forged endorsement" problem, whether under the BEA, the UCC or the ULC, has its advantages and disadvantages. Theoretically, the best solution would be one which embodies all the advantages of these systems, without being subject to their disadvantages. This cannot be done since any "positive" aspect of an optimum solution is of necessity accompanied by a "negative" aspect. As has been noted, the elements of an optimum solution include: (a) finality of payment; (b) economy of remedies; (c) allocation of the risk of forgery to the person best able to guard against the risk; (d) encouragement of the use of cheques as payment instruments. Article 25 offers a compromise solution; it attempts to embody the principal advantages of the existing legal systems, whilst avoiding or minimizing their main disadvantages.

20. *Finality of payment.* Under article 25 that advantage is substantially achieved: payment by the drawee is final. The legal relations between the drawee and the drawer, the payee and the drawer, the endorsees between themselves, the drawee and the person receiving payment are settled in a final way. The only "non-final" element is the rule that enables the person from whom the cheque was stolen to recover damages from the person who acquired the cheque from the forger.

21. *Economy of remedies.* Payment by a drawee effects a discharge of his obligation to the drawer; the drawee may debit the drawer's account. There is no occasion for further action between them. It follows that there is no need for further action between the drawee and the person receiving payment, or between him and previous endorsees. The person whose signature is forged (payee or endorsee) loses his right to act upon the cheque, and therefore there is no need for further action by him against the drawer, drawee or any subsequent endorsee. All these potential actions are replaced by a single right of action of the owner of the cheque against the forger and the person who acquired the cheque from the forger.

22. *The risk of forgery should be borne by the person who is best able to prevent the forgery.* It is the person who acquired the cheque from the forger who can best prevent the circulation of it. The endorsee should know his endorser. He should not take the cheque from a stranger. Article 25 encourages this by giving the owner a right of action against the person who took from the forger.

Paragraph (1)

23. The basic rule that a person to whom a cheque is transferred through an uninterrupted series of endorsements

is a holder, even if any of the endorsements was forged or was signed by an agent without authority, follows from article 16 (1) (b). This rule underlies the provision of paragraph (1). Consequently paragraph (2) does not apply to the case of a stolen bearer cheque.

24. Nothing in article 25 affects the rule that a forged signature does not impose any liability on the person whose signature was forged (cf. article 32). However, there are cases in which such a person will nevertheless be liable (cf. article 32). In such cases paragraph (1) does not apply by reason of the fact that the person whose signature was forged is considered to be bound by it.

25. The liability of the forger and of the person to whom the cheque was directly transferred by the forger is a liability off the instrument. Paragraph (1) merely confers a statutory right for compensation upon the party who suffered damages because of a forged endorsement. Questions pertaining to the amount of damages, limitation of action for damages, etc. are left to the applicable national law.

26. Article 25 confers a right for compensation on *any* party who suffered damages because of the forgery. That right is therefore not limited to the person whose endorsement was forged. Thus the drawer of a cheque which was stolen from the post on its way to the payee may exercise the right if he suffered damages because of the forgery of the payee's signature.

27. The right to recover compensation may be exercised only against the forger and the immediate transferee of the forger. Thus if T forges the signature of the payee, transfers the cheque to A and A transfers to B, the payee who suffered damages because of his forged endorsement may not recover damages under article 25 (1) from B, even if B knew about the forgery.

Paragraph (2)

28. Under article 25, the right to recover compensation for damages suffered because of a forged endorsement is given against the forger and against the "person to whom the cheque was directly transferred by the forger". The rationale for the rule that the right to recover compensation may be exercised against the person to whom the cheque was directly transferred by the forger, by endorsement and delivery or by delivery alone if the last endorsement was in blank, is that the transferee should know the person who so transfers the cheque to him. Therefore, such transferee is liable for damages that any party may suffer because of a forged endorsement. Paragraph (2) makes clear that the Convention makes no rule in respect of the liability of a party or the drawee to whom the cheque is transferred consequent upon payment of it by him.

29. Paragraph (2) further lays down that the Convention does not deal with the liability of a bank to which

the forger has endorsed a cheque for collection and to which it is subsequently paid.

Paragraph (3)

30. Paragraph (3) extends the rule laid down in paragraph (1) in respect of a forged endorsement to an endorsement made by an agent without authority or exceeding his authority.

CHAPTER FOUR. RIGHTS AND LIABILITIES

Section 1. *The rights of a holder and of a protected holder*

Article 26

(1) The holder of a cheque has all the rights conferred on him by this Convention against the parties to the cheque.

(2) The holder is entitled to transfer the cheque in accordance with article 14.

Relevant legislation

BEA – section 38.

UCC – sections 3-301 and 3-306.

ULC – article 19.

Cross references

Holder: articles 6 (5) and 16.

Party: article 6 (7).

Transfer: article 14.

Commentary

1. Article 26 is the introductory article to the articles governing the rights of a holder and of a protected holder. In order to exercise the rights on a cheque under this Convention a person must, as a general rule, be a holder. Special rules obtain if a holder is not in possession of the cheque because it is lost (see articles 73 to 78). As to the duties of a holder see Chapter Five of this Convention.

2. A cheque may be transferred only by a holder. If the transfer is in accordance with the provisions of article 14 the transferee is a holder.

Article 27

(1) A party may set up against a holder who is not a protected holder:

(a) Any defence available under this Convention;

(b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;

(c) Any defence to contractual liability based on a transaction between himself and the holder;

(d) Any defence based on incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque, provided that such absence of knowledge was not due to his negligence.

(2) The rights to a cheque of a holder who is not a protected holder are subject to any valid claim to the cheque on the part of any person.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the cheque unless:

(a) Such third person asserted a valid claim to the cheque; or

(b) Such holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft.

Relevant legislation

BEA — sections 36 (2) and (6), and 38 (2).

UCC — section 3-306.

ULC — articles 10, 19 and 22.

Cross references

Holder: articles 6 (5) and 16.

Protected holder: articles 6 (6) and 28.

Commentary

1. A person who signs a cheque (a "party") is liable to the holder of it. The Convention makes a distinction between a "holder" and a "protected holder". Article 27 deals with the rights of a holder who is not a protected holder.

2. The distinction between a holder and a protected holder is relevant only if the party liable on the cheque can set up a defence to his liability or has a claim to the cheque. If a holder is not a protected holder he is subject to any claim or defence of any party. As to the question whether payment by a party to a holder who is not a protected holder discharges that party, see Chapter Six.

Paragraph (1) (a)

3. The Convention sets forth various defences which a party may raise against the holder. Some of them may also be raised against a protected holder (see article 28 (1) (a) and commentary).

4. The following are examples of defences which may be set up against a holder.

Example A. The drawee of a cheque refuses to pay it upon due presentment. The holder fails to protest the cheque.

Therefore the payee is not liable on the cheque and, if recourse is exercised against him, may raise the defence of absence of liability consequent upon lack of due protest.

Example B. The payee of a cheque presents it for payment to the drawee. The drawee pays the cheque but does not request that it be handed over to him. Subsequently, the payee endorses the cheque to A who is not a protected holder. The drawer may set up against A the defence of discharge because of payment (cf. article 61).

Paragraph (1) (b)

5. In addition to defences that are derived from the provisions of the Convention there are the defences, referred to in paragraph (1) (b), that are based on an underlying transaction or that arise "from the circumstances as a result of which [a person] became a party". This type of defence may be illustrated by the following examples:

Example C. Pursuant to a contract of sale the buyer (drawer) issues a cheque made payable to the seller (payee). The seller fails to deliver the goods under the sales contract and endorses the cheque to A who is not a protected holder (for instance because A when taking the cheque had knowledge of seller's failure to deliver and, consequently, of buyer's defence on the cheque against seller; (cf. article 6 (6) (a)). The drawer may set up the defence of non-delivery in an action on the cheque by A, even though A is a person with whom the drawer has not dealt.

Example D. The payee by fraud induces the drawer to make a cheque payable to him, the payee. The payee endorses the cheque to A who is not a protected holder. Upon dishonour by non-payment, A brings an action on the cheque against the drawer. The drawer may raise against A the defence based on fraud as a result of which the drawer became a party.

Paragraph (1) (c)

6. This subparagraph provides that a party may raise against a non-protected holder who is not a remote holder a defence to contractual liability that is based on a transaction between himself and such a holder.

Example E. A to whom the payee transferred the cheque upon dishonour by non-payment brings an action on it against the payee. The payee may set up as a defence the fact that A has not delivered goods under a sales contract between himself and A.

Paragraph (1) (d)

7. This sub-paragraph sets forth two defences based on the fact that the party from whom payment is demanded was never liable on the cheque: he signed the cheque without capacity to incur liability on it or without knowledge that his signature made him a party to the cheque (the defence of *non est factum*).

8. The question whether a person has capacity to sign a cheque is left to national law. The defence of *non est factum* is available if the person signing is without knowledge of the fact that he signed a cheque and the absence of knowledge is not due to his being negligent.

Example F. X signs a cheque in the belief that it is a receipt. He does so without negligence. X is not liable on the cheque.

The defence of *non est factum* is not available if the person signing knows that he is signing a cheque but mistakenly erred as to its contents.

Paragraph (2)

9. Whereas a "defence" refers to a party's right to establish that he is free from liability on the cheque a "claim" to a cheque refers to the assertion of a right to ownership or some other proprietary right available under the applicable law. A holder who is not a protected holder is subject to such claims.

Example G. B obtains the cheque from A by fraud and transfers it to C who is not a protected holder because he knew about the fraud. A brings an action against C to recover possession of the cheque. A has a valid claim to the cheque against C.

Paragraph (3)

10. This paragraph deals with the so-called defence of *ius tertii*: a defence based on the claim of a third person and not on the absence of liability of the party from whom payment is demanded.

Example H. The drawer issues a cheque made payable to the payee. By fraud A induces the payee to transfer the cheque to him. Upon dishonour by non-payment A brings an action on the cheque against the drawer. Pursuant to paragraph (3) the drawer may raise the defence based on the fraud A practised on the payee only if the payee asserts his claim to the cheque.

The drawer may raise a defence based on *ius tertii* also if A acquired the cheque belonging to the payee by theft or if A had forged the signature of the payee or participated in the theft.

11. The main reasons for the rule set forth in paragraph (3) (a) are:

(a) The rule protects a party liable on the cheque since his liability will be discharged by his payment to the holder even if the party has knowledge of the claim of another person (cf. article 61 (2));

(b) It is not proper to allow a party to raise a defence based on a claim which the person entitled to it does not himself wish to raise. However, if such person asserts his claim the defence of *ius tertii* is available.

Thus, under article 61 (2), a party is not discharged of liability if, though knowing that a third person has asserted a valid claim to the cheque, he nevertheless pays it.

Article 28

(1) A party may not set up against a protected holder any defence except:

(a) Defences under articles 31 (1), 32, 33 (1), 34 (3), 45 and 79 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that party;

(c) Defences based on the incapacity of such party to incur liability on the cheque or on the fact that such party signed without knowledge that his signature made him a party to the cheque provided that such absence of knowledge was not due to his negligence.

(2) The rights to a cheque of a protected holder are not subject to any claim to the cheque on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the cheque of that person.

Relevant legislation

BEA — section 38.

UCC — sections 3-305 and 3-602.

ULC — articles 10, 19 and 22.

Cross reference

Protected holder: article 6 (6).

Commentary

1. As noted under article 6 (6), the main advantages of a negotiable instrument result from the strong legal position of a protected holder. He receives the instrument free from any defences of prior parties and free from claims to it by any person.

Example A. The payee by fraud induces the drawer to draw a cheque payable to the payee. The payee transfers it to A, a protected holder. Upon dishonour by non-payment, A demands payment from the drawer. Pursuant to paragraph (1) the drawer may not raise the defence of fraud against A.

Example B. The payee endorses an order cheque in blank and mails it to A. It is stolen from the mail by X. X sells and delivers the cheque to B, a protected holder. The payee brings an action against B for recovery of the cheque or its amount. Pursuant to paragraph (2) the claim of the payee to the cheque is not available against B.

Example C. The payee of a cheque presents it for payment to the drawee. The drawee pays the cheque but does not request that it be handed over to him. The payee subsequently endorses the cheque to A, a protected holder. The cheque is dishonoured by non-payment. The drawer may not set up as a defence against A the fact that he is discharged of liability because of the cheque having been paid.

Example D. The payee endorses the cheque to A and, off the cheque, gives instructions to A to collect the cheque for him. A in disregard of his instructions endorses the cheque to B who is a protected holder. The payee may not set up against B the fact that the payee's endorsement was intended for purposes of collection only.

Example E. A cheque is dishonoured by non-payment. The holder fails to protest the cheque for dishonour and transfers it to A who is a protected holder. In an action on the cheque by A against the drawer, the drawer may not raise the failure to protest as a defence to his liability.

2. The principal rule embodied in article 28, namely that the protected holder takes the cheque free from all defences and claims of any party, is subject to a number of important exceptions as provided in paragraph (1) (a), (b) and (c).

Paragraph (1) (a)

3. The protected holder does not take the cheque free from defences that are based on the provisions of the Convention listed in paragraph (1) (a). The defences are those based on the fact that the person from whom the protected holder demands payment has not signed the cheque (article 31 (1)); that that person's signature on the cheque was forged (article 32); that he signed the cheque before a material alteration of the cheque (article 33 (1)); that his signature was placed on the cheque in the conditions specified in article 34 (3); that the cheque was not duly presented for payment (article 45); and that a right of action on the cheque is prescribed under article 79.

Example F. The drawer draws a cheque for 1,000 Swiss francs payable to the payee P. P fraudulently increases the amount of the cheque to 2,000 Swiss francs and transfers it to A who is a protected holder. Upon dishonour of the cheque by non-payment A brings an action on the cheque against the drawer for the amount of the cheque. The drawer may set up as a defence against A the fact that he signed the cheque before the material alteration and is liable only for 1,000 Swiss francs (article 33 (1)).

Paragraph (1) (b)

4. The general rule that the protected holder takes the cheque free from defences and claims of prior parties does not obtain if the defence is raised or the claim asserted by an immediate party.

Example G. A to whom the payee of a cheque has transferred it is a protected holder. A delivers defective goods under a contract of sale between him and the payee in consideration of which the payee transferred the cheque to A. Upon dishonour by non-payment by the drawee A demands payment from the payee. The payee may raise as a defence the fact that A delivered defective goods. The payee may raise this defence because he and A are immediate parties. The defence could not be raised by the drawer since A is a protected holder and the transfer of the cheque to A is not connected with an underlying transaction between the drawer and A.

5. Usually the holder of a cheque is not a protected holder if the transaction which led to the transfer of the cheque to him is defective in the sense that it entitles the transferor to a defence against his liability on the cheque. However, there may be cases where when the cheque was transferred the holder took it in good faith and the defect in the transaction occurred later.

Paragraph (1) (c)

6. Defences against liability obtaining under a simple contract cannot be raised against a protected holder (see example A above). However, the protected holder does not overcome defences based on the fact that the party signed the cheque without capacity or without knowledge that his signature made him a party to the cheque.

Example H. B asks A to sign a document as a witness. A, without negligence, signs what is in fact a cheque. B transfers the cheque to C, a protected holder. In an action on the cheque by C against A, A has a valid defence.

Limitation or exclusion of liability

7. The rights of a protected holder on a cheque are determined by what is apparent *ex facie* the cheque. Therefore if a party has limited or excluded by a stipulation on the cheque the rights of a subsequent party or subsequent parties against him, as where an endorser has endorsed "without recourse" or has endorsed for collection or where a guarantor has guaranteed payment of only part of the sum payable, the protected holder cannot overcome such stipulation. Similarly where a party has paid part of the sum payable by the cheque — the cheque is then dishonoured by non-payment as to the amount unpaid (article 62 (3)) — and such partial payment is stated on the cheque (article 62 (5)), the party who paid partially can successfully raise against a protected holder the fact that he is discharged of his liability on the cheque to the extent of the amount he paid.

Paragraph (2)

8. Whereas paragraph (1) dealt with defences against liability, paragraph (2) deals with a claim to the cheque.

The basic rule is that a protected holder is not subject to such claim (see example *B*). However, when a claim to the cheque arises in the circumstances in which a defence becomes available under paragraph (1) (*b*), the protected holder cannot overcome such claim. Thus, in example *G* above the payee has a claim to the cheque against A.

Article 29

(1) The transfer of a cheque by a protected holder vests in any subsequent holder the rights to and upon the cheque which the protected holder had, except where such subsequent holder participated in a transaction which gives rise to a claim to or a defence upon the cheque.

(2) If a party pays the cheque in accordance with article 59 and the cheque is transferred to him, such transfer does not vest in that party the rights to and upon the cheque which any previous protected holder had.

Relevant legislation

BEA – section 29 (3).
UCC – section 3-201.

Cross references

Transfer: article 14.
Holder: articles 6 (5) and 16.
Protected holder: article 6 (6).

Commentary

Paragraph (1)

1. According to article 29 a holder who is not a protected holder may nevertheless obtain the rights of a protected holder. The purpose of this so-called “shelter rule” is to enable the protected holder to receive the full benefit of his protected status by being able freely to transfer the cheque. However, this rule is not intended, and should not be used, to permit any person who “participated in a transaction which gives rise to a claim to, or defence upon, the cheque” to wash the cheque clean by passing it into the hands of a protected holder. Consequently, under this paragraph, such a person is denied the benefit of the “shelter rule”.

Example A. The payee by fraud induces the drawer to draw a cheque payable to the payee (P). P endorses it to A who is a protected holder. A transfers the cheque to B who knows that the cheque was dishonoured. B brings an action against the drawer. Under article 29, the drawer is liable to B; the drawer has no defence against A since A is a protected holder. In the above facts the rights of A were transferred to B; therefore the drawer has no defence against B.

Example B. P and B by fraud induce the drawer to draw a cheque payable to P. P endorses the cheque to A who is

a protected holder. A transfers the cheque to B. B brings an action against the drawer. The drawer has a good defence. Though generally B acquires the same rights as A and A as a protected holder has a valid right against the drawer, article 29 (1) provides that this rule does not apply when the transferee was himself a party to the fraud.

However, it should be noted that the exception in article 29 (1) only applies where a person participated in the specified transaction and that mere knowledge is not sufficient. Thus if, in example *B*, B had not participated in the fraud, but only known about it, he would have had the rights of a protected holder.

Example C. In the fact situation described in example *B*, B transfers the cheque to C who is not a protected holder in his own right because he knew about the participation of B in the fraud. Under article 29 (1) C acquires the same rights as A had and, thus, obtains the rights of a protected holder.

Paragraph (2)

2. The shelter rule applies irrespective of whether the subsequent holder to whom the cheque is transferred is a previous party to the cheque.

Example D. The payee P induces by fraud the drawer to draw a cheque to P, which P transfers to A who knows about the fraud. A transfers to B who is a protected holder. B transfers to C and C to A. A acquires the rights of a protected holder according to article 29 (1) although as a previous party he was a holder against whom the drawer could have raised the defence of fraud.

However, a previous party may benefit from the shelter rule only if he obtains the cheque by transfer but not if he receives it against payment.

Article 30

Every holder is presumed to be a protected holder, unless the contrary is proved.

Relevant legislation

BEA – section 30.
UCC – section 3-307 (3).
ULC – article 19.

Cross reference

Protected holder: article 6 (6).

Commentary

If a person is the holder of a cheque it is presumed that he is a protected holder. Therefore, if, in an action by the holder on the cheque against a party liable to him, such party brings a claim to the cheque or raises a defence against his liability, it is for the party bringing the claim or raising

the defence to prove that the holder is not a protected holder.

Section 2. The liability of the parties

A. GENERAL PROVISIONS

Article 31

(1) Subject to the provisions of articles 32 and 34, a person is not liable on a cheque unless he signs it.

(2) A person who signs a cheque in a name which is not his own is liable as if he had signed it in his own name.

Relevant legislation

BEA – section 23.

UCC – section 3-401.

Cross reference

Signature: article 6 (8).

Commentary

1. Article 31 embodies one of the basic principles of negotiable instruments law, namely that a person is liable on an instrument only if he signed it. Therefore, for example, the drawee is not liable on the cheque. Articles 32 to 34 set forth certain exceptions to this rule.

2. A person may have more than one name, e.g. a "private" name and a "business" or "trade" name. Paragraph (2) provides that the signature in any one of these names is sufficient to establish the signer's liability on the cheque. It is the fact of signing, not in which name is signed, that is the decisive factor. A person signing in a fictitious name is thus liable on the cheque he signed. It also follows from paragraph (2) that a person who forges the signature of another person is liable on the cheque as if he had signed in his own name.

Article 32

A forged signature on a cheque does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed the cheque himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own.

Relevant legislation

BEA – section 24.

UCC – sections 3-404 and 3-406.

Cross reference

Signature, forged signature: article 6 (8).

Commentary

1. In conformity with the generally prevailing rule that a person is not liable on a cheque unless he signs it (cf. article 31), article 32 provides that a forged signature (as defined in article 6 (8)) on an instrument does not impose liability on the person whose signature was forged, not even against a protected holder (cf. article 28 (1)(a)). However, article 32 sets forth two exceptions to this rule. Such person is liable if he accepts or adopts the forged signature as his own or if he represents, in writing or orally or by other conduct, that the forged signature is his own.

Example. The payee intends to endorse a cheque to A. Before A takes the cheque he asks the drawer whether the signature on the cheque is his. The drawer mistakenly answers in the affirmative. It turns out that the drawer's signature was forged. Under article 32, the drawer is liable on the cheque since he represented to A that the signature was his own.

2. For the purposes of this second exception, it is material whether the person to whom an affirmative representation is made knows of the forgery. If he does so, the person whose signature was forged is not liable since the rule on representation presupposes justified reliance on the representation.

3. It should be noted that the liability of persons other than the person whose signature was forged is not dealt with in article 32 but in other provisions (articles 25, 31).

Article 33

(1) If a cheque has been materially altered:

(a) Parties who have signed the cheque subsequent to the material alteration are liable thereon according to the terms of the altered text;

(b) Parties who have signed the cheque before the material alteration are liable thereon according to the terms of the original text. Nevertheless, a party who has himself made, authorized, or assented to, the material alteration is liable on the cheque according to the terms of the altered text.

(2) Failing proof to the contrary, a signature is deemed to have been placed on the cheque after the material alteration.

(3) Any alteration is material which modifies the written undertaking on the cheque of any party in any respect.

Relevant legislation

BEA – sections 55 (2) (c) and 64.

UCC – sections 3-406 and 3-407.

ULC – article 51.

Cross reference

Signature: article 6 (8).

Commentary

Paragraph (1)

1. Article 33 deals with the material alteration of a cheque and not with forgery of the signature of a party, which is dealt with in article 32. It is irrelevant whether the material alteration is made by a party or a stranger.

2. The alteration does not discharge parties to the cheque of their liability. However, as to the extent of their liability it is relevant whether they signed before or after the alteration. A party who signs after the alteration is liable according to the terms of the altered text (subparagraph (a)). A party who signed before the alteration is liable according to the terms of the original text. The only exception to this rule is that such party is liable according to the terms of the altered text if he himself made, authorized, or assented to the alteration (subparagraph (b)).

Example. A cheque states the sum payable as X. The payee then raises the sum to Y and endorses the cheque to A. A endorses the cheque to B. If the drawee dishonours the cheque the drawer is liable to B for X. Pursuant to paragraph (1) (a) the payee and A are liable to B for Y.

3. The application of the above rules based on the time of the signature does not depend on whether the person claiming payment is with or without knowledge of the alteration or whether or not he is a protected holder. Thus, a party signing before the alteration is liable according to the original terms even if the holder had no knowledge of the alteration and even if he was a protected holder (cf. article 28 (1) (a)). Conversely, a party signing after the alteration is liable according to the altered terms even if the holder had knowledge of the alteration.

4. The rule in paragraph (1) places the risk of a material alteration on the person making the alteration and on the party who takes the cheque from that person. The same policy of risk allocation is adopted in the case of a forged endorsement (cf. article 25). In certain circumstances, this risk allocation may lead to the liability of an innocent person. Such potential hardship is unavoidable and seems justified by the fundamental principle "know your endorser".

5. It should be noted that the rule on material alteration laid down in article 33 deals only with the liability on the cheque. It does not prevent a person who suffered loss because of the alteration to claim damages under national law, for example from a drawer who facilitated the alteration by leaving open a space which enabled the payee to alter the figure and wording of the sum without it being apparent.

Paragraph (2)

6. In determining the liability of parties in a case of material alteration, the decisive factor is whether a party signed before or after the alteration. Since the point of time at which the cheque was altered is in many cases difficult to determine, paragraph (2) establishes a rebuttable presumption that the alteration has been made before a signature was placed on the cheque. A party may rebut this presumption by proving that he signed before the alteration. Such proof may be extrinsic to the cheque.

Paragraph (3)

7. Paragraph (3) defines what constitutes material alteration. The test is whether there was any change in the "written undertaking on the cheque". For example, there is such a change and, consequently, a material alteration where the sum payable is changed (whether increased or decreased). There is no such change if, for example, the sum is given in figures only and the corresponding amount is added in words, or if on a cheque the words "on demand" are added.

8. A change in the "written undertaking on the cheque" is possible only where there was already a cheque. According to article 1 (2) a writing must comply with certain formal requisites in order to qualify as a cheque. Therefore, if one or more of the essential requisites are missing article 33 does not apply. If missing elements are added, this would be a case of completion of a cheque dealt with in article 13. However, if a writing is a cheque an alteration on it may pertain to an essential or to a non-essential requirement. The only question is whether it changes the "written undertaking on the cheque of any party".

9. There is one exception to this test: an alteration is not material if it is authorized by this Convention. For example, article 33 does not apply in the cases envisaged under article 17 (b) (conversion of blank endorsement into special endorsement) or article 23 (1) (striking out of previous endorsements) or article 68 (crossing of cheque).

Article 34

(1) A cheque may be signed by an agent.

(2) The signature of an agent placed by him on a cheque with the authority of his principal and showing on the cheque that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the cheque by an agent with his authority, imposes liability on the principal and not on the agent.

(3) A signature placed on a cheque by a person as agent but without authority to sign or exceeding his authority or by an agent with authority to sign but not showing on the cheque that he is signing in a representative capacity for a named person, or showing on the cheque that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person

signing and not on the person whom he purports to represent.

(4) The question whether a signature was placed on the cheque in a representative capacity may be determined only by reference to what appears on the cheque.

(5) A person who is liable pursuant to paragraph (3) and who pays the cheque has the same rights as the person for whom he purported to act would have had if that person had paid the cheque.

Relevant legislation

BEA – sections 25 and 26.

UCC – section 3-403.

ULC – article 11.

Cross reference

Signature: article 6 (8).

Commentary

Paragraph (1)

1. This provision makes it clear that a signature may be placed on a cheque by an agent for any party, i.e. for the drawer, an endorser or their guarantor.

Paragraph (2)

2. If a cheque has been signed by an agent the question arises who is liable on the cheque, the agent or the principal. If an agent signs without authority, the answer of both agency law and negotiable instruments law is generally that the principal is not liable. If the agent signs with authority, the principal would be liable under agency law. However, in negotiable instruments law the liability of the principal depends on whether the cheque shows that the agent signing acted in a representative capacity for that principal. If it does not show that, the agent, though signing with authority, is liable and not the principal. The rationale of this rule is the fundamental principle of negotiable instruments law according to which a holder must be able to see from what appears on the cheque who is liable on it.

3. In conformity with these rules, paragraph (2) sets forth the cases in which the principal and not the agent is liable. One case is where an agent places his signature on a cheque with the authority of the principal and the cheque shows that he is signing in a representative capacity for that named principal. For example, A signs his name and adds the words "as agent of P" or "on behalf of P", or A writes P's name and signs "by A, agent". The second case is where an agent places the signature of his principal on the cheque with his authority. For example, A places P's signature on the cheque without any indication that this signature was placed by him and not by P.

Paragraph (3)

4. Paragraph (3) sets forth the cases in which not the principal but the agent himself is liable on the cheque. One case is where an agent signs without, or exceeding his, authority irrespective of whether the cheque shows that he is acting in a representative capacity. If he would simply use his principal's signature without authority, this would be a case of forgery and he would be liable under article 31 (2). The second case is where an agent signs the cheque for a named person. Unlike in the first case, A signs with authority and he is liable only because he does not specify on the cheque that he signs on behalf of his principal as, for example, where A signs his own name. The third case is where an agent signs with authority indicating that he signs in a representative capacity but does not name the principal as, for example, where he simply signs "A, as agent".

Paragraph (4)

5. In the above cases where an agent signs with authority, it is important to determine whether or not he has acted in a representative capacity. Paragraph (4) emphasizes that such determination may be made only by what appears *ex facie* the cheque and not by any circumstances outside the cheque.

Example. A places his signature under a stamp of X Corporation which appears at the place where usually the signature of the drawer appears. The question whether A signed as an agent for X Corporation or as a co-drawer must be decided on the basis of what appears on the cheque (e.g. the distance between stamp and signature may be relevant) but not on the basis of evidence extrinsic to the cheque (e.g. the fact that A is director of X Corporation).

6. Since the only relevant factor is what appears *ex facie* the cheque, it is immaterial whether or not the holder had knowledge of the agent's authority or of his acting as agent. Furthermore, the above rules apply even if the holder is a protected holder (cf. article 28 (1) (a)).

Paragraph (5)

7. Under paragraph (3), a person may be liable although he purports to act for another person. If, accordingly, he pays the cheque, paragraph (5) accords him the same rights as the person for whom he purported to act would have obtained upon payment.

Article 35

The order to pay contained in a cheque does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee.

Relevant legislation

BEA – section 53.

UCC – section 3-409.

ULC — article 19 of annex II to the Geneva Convention of 1931.

Commentary

Article 35 provides that the drawing of a cheque does not of itself operate as an assignment to the payee of any funds made available for payment by the drawer with the drawee. Therefore the payee has no rights against the drawee. However, nothing in this article prevents a drawer from assigning such funds to the payee by agreement. The effect of such an agreement would be governed by national law.

Article 36

(1) Any statement written on a cheque indicating certification, confirmation, acceptance, visa or any other equivalent expression has only the effect to ascertain the existence of funds and prevents the withdrawal of such funds by the drawer, or the use of such funds by the drawee for purposes other than payment of the cheque bearing such a statement, before the expiration of the time-limit for presentment.

[(2) However, a Contracting State may provide that a drawee may accept a cheque and determine the legal effects thereof. Such acceptance must be effected by the signature of the drawee accompanied by the word "accepted".]

Relevant legislation

UCC — section 3-411.

ULC — article 4.

Cross reference

Time-limit for presentment: article 43.

Commentary

1. The main legal systems show different approaches to the question whether a cheque is capable of being accepted. Under the ULC "a cheque cannot be accepted" and "a statement of acceptance on a cheque shall be disregarded" (article 4). Under the UCC "certification of a check is acceptance" and certification may be procured by the drawer (which leaves him liable) or by a holder (which discharges the drawer and other prior parties) (section 3-411). Under the BEA the acceptance of a cheque is in principle possible but the practice of acceptance is not much resorted to.

2. The Convention, in article 36, adopts the approach of the ULC in that any statement written on a cheque indicating certification, confirmation, acceptance etc. is not an acceptance. Paragraph (1) states that where such statement is written on a cheque there is an irrebuttable presumption that the statement does no more than ascertain the existence of funds in the hands of the drawee-bank. Such a statement on the cheque blocks the funds of the drawer

with the drawee in the amount of the cheque: the drawer cannot withdraw these funds nor can the drawee use them otherwise than for payment of the cheque before the expiration of the time-limit for presentment, i.e. within 120 days of the date stated on the cheque.

3. In view of the widespread practice of confirming cheques under the UCC, paragraph (2), placed between brackets, permits a Contracting State to provide for the acceptance of an international cheque and to determine the legal effects thereof.

B. THE DRAWER

Article 37

(1) The drawer engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the cheque in accordance with article 59, the amount of the cheque, and any interest and expenses which may be recovered under article 59 or 60.

(2) The drawer may not exclude or limit his own liability by a stipulation on the cheque. Any such stipulation is without effect.

Relevant legislation

BEA — section 55 (1) (a).

UCC — sections 3-413 (2) and 3-502.

ULC — article 12.

Cross references

Dishonour by non-payment: article 46.

Necessary protest: article 48.

Commentary

Paragraph (1)

1. The liability of the drawer is contingent upon the refusal by the drawee to pay the cheque and any necessary protest of dishonour. In this respect, the drawer's liability is like that of the endorser. However, the liability of an endorser or his guarantor is further conditioned by due presentment and due protest and, therefore, an unexcused delay in making presentment or protest will result in absence of liability on the cheque of the endorser and his guarantor. In contrast, an unexcused delay in making presentment or protest does not absolve the drawer. He remains liable because of the dishonour by non-payment. However, the delay in making presentment or protest affects the extent of the drawer's liability on the cheque since the drawer is discharged of liability on the cheque to the extent of the loss he suffered because of the delay in making presentment or protest.

2. The engagement of the drawer is to pay the cheque, upon dishonour and any necessary protest, to the holder or to any party subsequent to the holder who pays the cheque in a recourse action. Thus, if the cheque is paid by an endorser to the holder and is transferred to such endorser (with or without endorsement, cf. article 23) by the holder, the liability of the drawer is to pay the cheque to such endorser.

3. It may be noted that the liability of the drawer is not subject to any notice of dishonour. This is in conformity with the policy of this Convention that notice of dishonour is not necessary in order to render a party liable on the cheque. Under article 57 failure to give due notice of dishonour renders a person who is required to give notice to the drawer liable to the drawer for any damage that he may suffer from such failure.

Paragraph (2)

4. Unlike an endorser or guarantor, the drawer may not exclude or limit his own liability by a stipulation on the cheque. Any such stipulation is without effect and does not affect the validity of the cheque.

C. THE ENDORSER

Article 38

(1) The endorser engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the cheque in accordance with article 59, the amount of the cheque, and any interest and expenses which may be recovered under article 59 or 60.

(2) The endorser may exclude or limit his own liability by an express stipulation on the cheque. Such stipulation has effect only with respect to that endorser.

Relevant legislation

BEA – section 55 (2) (a).
UCC – section 3-414 (1).
ULC – article 18.

Cross references

Dishonour by non-payment: article 46.
Necessary protest: article 48.

Commentary

1. The endorsement may be a necessary element in the transfer of a cheque (cf. article 14 (a)) and serves the function of rendering the endorser liable on the cheque. This latter function is dealt with in article 38.

2. The endorser is liable only if the cheque is dishonoured by the drawee and his liability is subject to any necessary presentment and protest upon such dishonour.

Paragraph (1)

3. According to paragraph (1), the engagement of the endorser is to pay the cheque, upon dishonour and any necessary protest, to the holder or to any subsequent party who pays the cheque in a recourse action. Thus, if a cheque endorsed by the payee to A and by A to B is paid by A to B, the payee's liability is to pay A.

Paragraph (2)

4. The endorser – unlike the drawer (article 37 (2)) – may exclude or limit his own liability by an express stipulation on the cheque. It should be noted that in the case of an endorsement for collection the exclusion of liability follows from the rule laid down in article 22 (2).

5. The words "his own liability" make it clear that only the endorser himself benefits from such an exclusion or limitation and not any other party from whom payment is claimed. The exclusion or limitation being *ex facie* the cheque may be invoked by the endorser even against a remote protected holder.

6. Paragraph (2) deals only with a stipulation made expressly on the cheque. It does not prevent an endorser from excluding or limiting his liability by an agreement outside the cheque; in such a case he may invoke the exclusion or limitation as a defence against a holder in accordance with article 27 (1) unless that holder is a protected holder (cf. article 28 (1) (a)).

7. Paragraph (2) does not specify the wording that must be used to exclude or limit the liability. While the expression commonly used is "without recourse", the endorser may use other words for that purpose.

Article 39

(1) Any person who transfers a cheque by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer:

- (a) A signature on the cheque was forged or unauthorized; or
- (b) The cheque was materially altered; or
- (c) A party has a valid claim or defence against him; or
- (d) The cheque was dishonoured by non-payment.

(2) The damages recoverable under paragraph (1) may not exceed the amount referred to in article 59 or 60.

(3) Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the cheque without knowledge of such defect.

Relevant legislation

BEA – section 58.
 UCC – section 3-417 (2).

Cross references

Transfer: article 14.
 Forged signature: articles 6 (8) and 32.
 Unauthorized signature: article 34 (3).
 Material alteration: article 33.
 Dishonour by non-payment: article 46.
 Knowledge: article 7.

*Commentary***Paragraph (1)**

1. A person who transfers a cheque by mere delivery (cf. article 14 (b)) is not liable on it since he has not signed it. However, such person may incur liability under article 39. Under this article, he is liable for any damage that a subsequent holder may suffer as a consequence of any of the circumstances referred to in subparagraphs (a) to (d) of paragraph (1).

2. The fact that the transferor did not know of any such circumstance, whether negligently or not, does not affect his liability under the article. Such liability benefits any subsequent holder who, when taking the cheque, has no knowledge of the deficiency. The liability under article 39 is off the cheque and, thus, presentment and protest are not conditions precedent to such liability. It materializes the moment the cheque is transferred.

Example A. The drawer issues a cheque to the payee (P) for the sum of 1,000 Swiss francs. P endorses the cheque in blank and delivers it to C who alters the sum payable to 11,000 Swiss francs. C delivers the cheque to D who does not know about the alteration, and D delivers it to E who does not know about the alteration. E may claim from the drawer and from P 1,000 Swiss francs under article 33 (1) (b). E has no right on the cheque against C or D since they have not endorsed it. However, E may recover from C or D, under article 39, 10,000 Swiss francs as compensation for the damages suffered by him.

3. A person who transfers a cheque by mere delivery and who has no knowledge of any circumstances giving rise to liability under article 39 may exclude or limit his liability by agreement off the cheque or by an express stipulation on the cheque. Although this faculty is not stated in article 39, it follows from the fact that it is liability off the cheque and for damages.

4. Under article 39 the holder may recover only those damages which he has suffered "on account of" any factor enumerated in paragraph (1). Consequently, insolvency of the drawer would not confer a right of action under article

39 on the transferee by mere delivery, since the transferor is not deemed, under the article, to have warranted the solvency of a secondary obligor.

5. The holder may recover only if, on account of the factors enumerated, he has in fact suffered damages. This is not the case where he has been paid the amount due, for example, by a person whose signature had been forged but who accepted it or represented it to be his own (cf. article 32). Another example is where a cheque which was dishonoured by non-payment was nevertheless paid.

Subparagraph (a)

6. According to article 32 a person whose signature has been forged is not liable on the cheque. A holder who takes the cheque without knowledge of the forgery may therefore suffer loss by relying on the liability of that person. Subparagraph (a) is intended to protect him against such risk. The same is true with regard to an unauthorized signature.

Example B. The drawer issues a cheque which shows on it that he signs as agent, though he had no authority to sign. The payee endorses the cheque in blank to B who transfers it by delivery to C. Upon dishonour by non-payment, C has an action against B under article 39 (1) (a).

Subparagraph (b)

7. According to article 33 (1) (b) parties who have signed the cheque before a material alteration are liable according to the terms of the original text. This may cause loss to a holder who receives a cheque without knowledge of the alteration (cf. above example A, paragraph 2). Subparagraph (b) is intended to protect him.

Subparagraph (c)

8. The transferee may be subject to a valid claim against him and as a consequence may suffer loss.

Example C. The drawer issues a cheque payable to bearer to A. The cheque is stolen and the thief transfers it to B who transfers it to C who is not a protected holder. C is subject to a valid claim to the cheque by A but may recover any ensuing damages from B under article 39 (1) (c).

9. The same rule applies with regard to a valid defence which a party prior to the transferor may raise against the transferee.

Example D. The payee by fraud induces the drawer to issue a cheque to him, the payee (P). P endorses the cheque in blank and transfers it to A who is not a protected holder. A transfers it to B who is not a protected holder. In an action by B against the drawer, the drawer may raise the defence of fraud. B has an action for damages against A.

Subparagraph (d)

10. This subparagraph protects the transferee against the risk that the cheque was dishonoured by non-payment. The words "was dishonoured" make it clear that damages lie only if the cheque was dishonoured before the transfer. Thus transfer by mere delivery, unlike transfer by endorsement, does not provide a warranty of payment.

Paragraph (2)

11. Paragraph (2) limits the amount of damages to the amount of the cheque. Other questions concerning the extent of liability, such as mitigation of damages, limitation of action, are left to the applicable national law.

Paragraph (3)

12. Following the rationale of the liability rule in paragraph (1), i.e. to protect the innocent transferee, paragraph (3) specifies that only those transferees may recover who are without knowledge of the defect which causes the loss (as to the definition of "knowledge", see article 7).

D. THE GUARANTOR

Article 40

(1) Payment of a cheque may be guaranteed, as to the whole or part of its amount, for the account of a party by any person who may or may not have become a party.

(2) A guarantee must be written on the cheque or on a slip affixed thereto (*allonge*).

(3) A guarantee is expressed by the words: "guaranteed", "aval", "good as *aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires,

(a) A signature alone on the front of the cheque, other than that of the drawer, is a guarantee;

(b) A signature alone on the back of the cheque is an endorsement. A special endorsement of a cheque made payable to bearer does not convert the cheque into an order instrument.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the drawer.

Relevant legislation

BEA — no relevant provision and see section 56.

UCC — no relevant provision and see sections 3-402, 3-415 and 3-416.

ULC — articles 25 and 26.

Cross reference

Party: article 6 (7).

Commentary

1. In addition to the liability incurred by the drawer and endorser of a cheque the Convention recognizes the special liability of a person who signs a cheque as a "guarantor". The liability is a guarantee of payment of the whole or part of the amount of the cheque for the account of a party. Such a guarantee may be given by a stranger or by someone who is already a party. The guarantee is "transferable" in nature in that it runs with the cheque.

2. The provisions of the Convention in respect of this liability of a guarantor follow in substance the provisions of the ULC in respect of the giver of an *aval*.

3. The guarantee is given on the cheque itself, or on a *allonge* or slip affixed to the cheque, by a signature accompanied by the words "guaranteed", "payment guaranteed", "aval", "good as *aval*" or by words of similar import. However, if the guarantee is given on the face of the cheque a signature alone is sufficient to express the guarantee provided the signature is not that of the drawer. A signature alone on the back of the cheque is an endorsement.

4. The person signing as guarantor may, but need not, indicate on the cheque for whose account he effects the guarantee. In the absence of such indication the guarantee is given for the drawer.

5. It is to be noted that in the case of a cheque payable to bearer a special endorsement does not transform such cheque into an order cheque payable to the special endorsee or to his order. Of course, the endorsement establishes the liability on the cheque of the endorser.

Article 41

A guarantor is liable on the cheque to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the cheque.

Relevant legislation

ULC — article 27.

Commentary

1. The liability of a guarantor is of an accessory nature: he is liable to the same extent as the party for whom he has become guarantor. Thus, if upon dishonour of a cheque by non-payment there is an unexcused delay in making protest, the guarantor of the endorser is not liable but the guarantor of the drawer is liable except to the extent of the loss suffered by the delay (see article 52).

2. A further corollary of the rule stated in article 41 is that the guarantor may base defences against his liability on

the cheque on the defences which the party for whom he became guarantor may invoke. In addition the guarantor may set up defences which are personal to himself. On the other hand the guarantor is not entitled to the benefit of excussion: the holder or a party who has taken up and paid the cheque is not obliged to demand payment first from the person in favour of whom the guarantee was given. Therefore, the liability of the guarantor is not dependent on the refusal to pay by the person for whom he became guarantor. However the guarantor cannot be sued under the guarantee until the liability of the person for whom he became guarantor has materialized.

3. Under the article the guarantor may "stipulate otherwise", i.e. the liability under a guarantee may be extended or restricted by the giver thereof. Such stipulation may relate to any possible element of the guarantor's liability in any possible way, including different time or place of payment and reduction or increase of the amount. For example, the guarantor may stipulate that the guarantee is given for part of the sum due or that the guarantee is given for a limited time.

Article 42

The guarantor who pays the cheque has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

Relevant legislation

ULC — article 27.

Cross reference

Party: article 6 (7).

Commentary

The guarantor upon payment of the cheque by him acquires rights on it against the party for whom he became guarantor and against those parties who are liable to that party. It may be noted that the guarantor has rights on the cheque against parties who are liable on it to the party for whom he became guarantor even if he is not a holder (as where the cheque was not transferred to him under article 14). A guarantor who is not a holder may not transfer the cheque.

CHAPTER FIVE. PRESENTMENT, DISHONOUR BY NON-PAYMENT, AND RECOURSE

Section 1. Presentment for payment and dishonour by non-payment

Article 43

A cheque is duly presented for payment if it is presented in accordance with the following rules:

(a) The holder must present the cheque to the drawee on a business day at a reasonable hour;

(b) A cheque must be presented for payment within 120 days of its stated date;

(c) A cheque must be presented for payment:

(i) At the place of payment specified on the cheque; or

(ii) If no place of payment is specified, at the address of the drawee indicated on the cheque; or

(iii) If no place of payment is specified and the address of the drawee is not indicated, at the principal place of business of the drawee;

(d) A cheque may be presented for payment at a clearing-house.

Relevant legislation

BEA — section 74.

UCC — sections 3-503 and 3-504.

ULC — articles 2, 29, 30 and 55.

Cross references

Holder: articles 6 (5) and 16.

Commentary

1. In order to establish the liability of parties because of dishonour by non-payment, presentment for payment must be due presentment. Article 43 specifies what constitutes due presentment for payment.

Paragraph (a)

2. As elsewhere in this Convention, the word "holder" or "drawee" includes an authorized agent.

3. The requirement that presentment must be made "on a business day at a reasonable hour" refers to the business day and reasonable hour at the place of the drawee.

Paragraph (b)

4. This paragraph sets forth a rule as to the time within which presentment for payment must be made. Presentment for payment after this period of time deprives the holder of the right of recourse against the endorsers and their guarantors. Yet, if there is delay in presentment the drawer remains liable except to the extent of the loss suffered because of the delay. However, failure to present the cheque for payment, unless dispensed with, results in absence of liability of the drawer on the cheque.

Paragraph (c)

5. This paragraph sets forth rules regarding the proper place of presentment for payment.

Paragraph (d)

6. In the collection process a collecting bank will often use a clearing-house of which it itself and the drawee-bank are members to present the cheque for payment (to "collect" the cheque). Paragraph (d) makes clear that this is due presentment for payment and consequently the holder of such a cheque may, upon due protest, exercise his rights of recourse against prior parties.

Article 44

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:

- (i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;
- (iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.

(b) If the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment.

Relevant legislation

BEA – section 46.
UCC – section 3-511.
ULC – article 38.

Commentary

1. Article 44 provides for the excuse of delay in making presentment of a cheque for payment and states the grounds on which such presentment is dispensed with.

Paragraph (1)

2. When delay is excused the liability of parties prior to the holder is not affected on the ground that there was no due presentment for payment. Under paragraph (1) delay is excused when the holder is prevented from presenting the cheque for payment by circumstances beyond his control which he could neither avoid nor overcome. When the cause of delay ceases to operate presentment must be made with reasonable diligence. However, if such cause continues to operate beyond 30 days after the time period within

which a cheque must be presented for payment (cf. article 43 (b)) presentment is altogether dispensed with and a right of recourse may be exercised against the drawer, the endorsers, and the guarantors of the drawer and the endorsers. It should be noted that under article 45 an unexcused delay, though it results in absence of liability of the endorsers and their guarantors, does not discharge the drawer of liability except to the extent of the loss suffered by the delay.

Paragraph (2)

3. Paragraph (2) states the cases where presentment for payment is dispensed with. Under article 46 (1) (b) such cases constitute constructive dishonour and under article 46 (2) the holder may then, subject to any necessary protest, exercise a right of recourse.

4. A waiver of presentment for payment may be stipulated expressly on the cheque or expressly or impliedly off the cheque. If waiver is on the cheque the dispensation is operative only as regards the party waiving presentment except if waiver is made by the drawer in which case the dispensation runs with the cheque and is operative as regards any party subsequent to the drawer. A waiver of presentment on the cheque benefits any holder. If waiver is off the cheque, whether impliedly (as where payment is made after the time period within which the cheque must be presented for payment) or expressly, the dispensation is operative only as regards the party waiving presentment and benefits only a holder in whose favour there has been a waiver.

Article 45

If a cheque is not duly presented for payment, the drawer, the endorser and their guarantors are not liable thereon. However, if a cheque is not duly presented because of delay in making presentment, the drawer is not discharged of liability except to the extent of the loss suffered because of the delay.

Relevant legislation

BEA – section 74.
UCC – sections 3-501 and 3-502.

Cross reference

Due presentment for payment: article 43.

Commentary

Presentment for payment of a cheque is one of the conditions precedent to the liability of parties prior to the holder. Therefore, non-presentment deprives the holder of his right of recourse against prior parties. However, delay in presentment does not discharge the drawer of liability except to the extent of loss suffered because of that delay. Thus, the liability of the drawer of a cheque is not purely of a secondary nature.

Article 46

(1) A cheque is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment, or when the holder cannot obtain the payment to which he is entitled under this Convention, or as regards the drawer only, if presentment of the cheque, otherwise duly made, is delayed and payment is refused;

(b) If presentment for payment is dispensed with pursuant to article 44 (2) and the cheque is unpaid.

(2) If a cheque is dishonoured by non-payment, the holder may, subject to the provisions of article 48, exercise a right of recourse against the drawer, the endorsers and their guarantors.

Relevant legislation

BEA – section 47.

UCC – section 3-507.

ULC – article 40.

Cross references

Due presentment for payment: article 43.

Dispensation of presentment for payment: article 44 (2).

Payment to which the holder is entitled: articles 62, 63 and 64.

*Commentary**Paragraph (1)*

1. Article 46 states when a cheque is dishonoured by non-payment. Paragraph (1) (a) deals with actual dishonour by non-payment: when payment is refused or the holder cannot obtain the payment to which he is entitled. Paragraph (1) (b) deals with constructive dishonour by non-payment: when presentment for payment is dispensed with under article 44.

Payment to which the holder is entitled

2. Pursuant to articles 62 and 63 the holder may refuse to take partial payment and refuse to take payment in a place other than the place where the cheque was presented for payment in accordance with article 43. Therefore, the refusal by the holder to take such payment results in dishonour by non-payment.

3. Pursuant to article 64 the refusal of the holder to take payment of a cheque, denominated in foreign currency or to be paid in a specified currency, in local currency results in dishonour by non-payment.

Paragraph (2)

4. The effect of dishonour by non-payment is that the holder is, subject to any necessary protest (cf. article 48),

entitled to exercise a right of recourse against the drawer, the endorsers and their guarantors.

Article 47

If a cheque is presented before its stated date, refusal by the drawee to pay does not constitute dishonour by non-payment under article 46.

Relevant legislation

UCC – section 3-114 (2).

ULC – article 28.

Cross references

Stated date: article 1 (2) (d).

Dishonour by non-payment: article 46.

Commentary

If a cheque is post-dated, i.e. the drawer places on the cheque a date ("stated date") which is later than the date on which he issues it, the question arises whether a refusal by the drawee to pay before the stated date constitutes or not a dishonour by non-payment. Article 47 adopts the approach that a post-dated cheque is not due before its stated date. Consequently, refusal by the drawee to pay the cheque upon its presentment before the stated date does not constitute dishonour by non-payment. In the result, the holder cannot effectuate protest and no liability arises of parties to the cheque upon the drawee's refusal to pay in these circumstances.

*Section 2. Recourse**A. PROTEST**Article 48*

If a cheque has been dishonoured by non-payment, the holder may exercise a right of recourse only after the cheque has been duly protested for dishonour in accordance with the provisions of articles 49 to 51.

Relevant legislation

BEA – sections 48 and 51 (2).

UCC – section 3-501 (2) and (3).

ULC – article 40.

Cross references

Dishonour by non-payment: article 46.

Holder: articles 6 (5) and 16.

Protest for dishonour: articles 49 to 51.

Commentary

1. The effect of dishonour by non-payment is that it entitles the holder to a right of recourse against the drawer, endorsers and guarantors. The making of a protest is necessary in order for the holder to be entitled to exercise that right. Protest where protest is necessary is a condition precedent to the liability of the drawer, endorsers and guarantors.

Protest and notice of dishonour

2. Under article 40 of the ULC, non-payment must be evidenced by either a formal instrument (protest) or a declaration dated and written by the drawee on the cheque and specifying the date of presentment or by a dated declaration made by a clearing-house stating that the cheque has been delivered in due time and has not been paid. Under article 20 of annex II to the Geneva Convention of 1931, High Contracting Parties may reserve the right to make or not to make protest or an equivalent declaration a condition for the exercise of the right of recourse (upon dishonour by non-payment) against the drawer.

3. Under the UCC (section 3-501 (2)), notice of dishonour is necessary to charge any endorser but failure to give such notice discharges the drawer only to the extent stated in section 3-502 (1) (b). This section expressly limits the rule that the drawer is discharged where he has sustained loss through the delay to loss sustained through insolvency of the drawee. Under the BEA, the exercise of the right of recourse consequent upon dishonour requires, as a general rule, notice of dishonour. If notice of dishonour is not given the drawer and endorsers are discharged (section 48). Under both the UCC (section 3-501 (3)) and the BEA (section 51 (1), (2)), protest is required only in the case of foreign cheques.

4. Under this Convention the exercise of a right of recourse is conditional upon effectuating protest and failure to protest results in the discharge of the drawer, an endorser and their guarantors. See, however, article 52 (2) regarding the effect of delay in protesting a cheque for non-payment on the liability of the drawer or his guarantor. Notice of dishonour is, under this Convention, not a condition precedent to liability of parties to the cheque but may give rise to an action for damages suffered by a party because of not having received notice (cf. article 57).

Article 49

(1) A protest is a statement of dishonour drawn up at the place where the cheque has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

- (a) The person at whose request the cheque is protested;
- (b) The place of protest; and

(c) The demand made and the answer given, if any, or the fact that the drawee could not be found.

(2) A protest may be made:

(a) On the cheque itself or on a slip affixed thereto (*allonge*); or

(b) As a separate document, in which case it must clearly identify the cheque that has been dishonoured.

(3) Unless the cheque stipulates that protest must be made, a protest may be replaced by a declaration written on the cheque and signed and dated by the drawee; the declaration must be to the effect that payment is refused.

(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purposes of this Convention.

Relevant legislation

BEA — section 51 (7).

UCC — section 3-509.

ULC — article 40; article 21 of annex II to the Geneva Convention of 1931.

Cross references

Protest as a condition precedent to the liability of parties: articles 48 and 52.

Dishonour by non-payment: article 46.

Commentary

1. Under article 49 protest may be made (a) in the form of a written statement, on the cheque itself or in a separate document, signed by a person authorized by the law of the place of dishonour to certify dishonour or (b) in the form of a written declaration on the cheque, signed by the drawee, to the effect that payment is refused. Paragraphs (1) and (2) deal with the protest mentioned under (a) above and paragraphs (3) and (4) with the declaration written on the cheque mentioned under (b) above.

2. The object of protest is to provide proof that the cheque was duly presented for payment and of dishonour by the drawee consequent upon such presentment. However, if presentment for payment is dispensed with under article 44 (2), protest for dishonour by non-payment is also dispensed with (cf. article 51 (2) (d)).

3. Pursuant to article 59 the holder in a recourse action may recover from any party liable any expenses of protest.

4. If the holder of a cheque takes partial payment (cf. article 62 (3)) he must protest the cheque as to the balance of its amount.

Article 50

Protest for dishonour of a cheque by non-payment must be made on the day on which the cheque is dishonoured or on one of the two business days which follow.

Relevant legislation

BEA — sections 51 (4) and 93.
 UCC — section 3-509 (4) and (5).
 ULC — article 41.

Cross references

Form of protest: article 49.
 Dishonour by non-payment: article 46.

Commentary

Article 50 lays down the time-limits within which a cheque must be protested for dishonour. Failure to observe these time-limits deprives the holder of his right of recourse against the endorsers and their guarantors but delay in protesting the dishonour does not discharge the drawer except to the extent of the loss suffered by the delay (cf. article 52 (2)).

Article 51

(1) Delay in protesting a cheque for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

- (i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;
- (iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made;
- (b) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;
- (c) As regards the drawer of a cheque, if the drawer and the drawee are the same person;
- (d) If presentment for payment is dispensed with in accordance with article 44 (2).

Relevant legislation

BEA — section 51 (9).
 UCC — section 3-511.
 ULC — article 48.

Cross reference

Time-limit within which protest must be made: article 50.

*Commentary**Paragraph (1)*

1. When delay in protesting a cheque for dishonour is excused the liability of parties is not affected on the ground that there was no protest. Delay is excused when the holder is prevented from effecting protest by circumstances beyond his control which he could neither avoid nor overcome. When the cause of delay ceases to operate protest must be made with reasonable diligence. However, if such cause continues to operate beyond 30 days from the date of dishonour, protest is altogether dispensed with and a right of recourse may be exercised against the drawer, the endorsers, and the guarantors of the drawer and the endorsers.

Paragraph (2)

2. Paragraph (2) states the cases where protest is dispensed with. The effects of waiver of protest by the drawer, his endorser or guarantor on or off the cheque are, as regards the person or party waiving protest and the holder whom the waiver benefits, identical to the effects of a waiver of presentment for payment (see paragraph 4 of the commentary to article 44).

3. Where the drawer and the drawee are the same person protest is dispensed with as regards the drawer by reason of the fact that the drawer having dishonoured the cheque in the capacity as drawee cannot require proof of the dishonour.

Article 52

(1) If a cheque which must be protested for non-payment is not duly protested the drawer, the endorsers and their guarantors are not liable thereon.

(2) Delay in protesting a cheque for non-payment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered by the delay.

Relevant legislation

BEA — section 51 (2).
 UCC — sections 3-501 (3) and (4), and 3-502.
 ULC — article 40; article 20 of annex II to Geneva Convention of 1931.

Cross references

Due protest: articles 49 and 50.

Commentary

1. Failure on the part of the holder to make due protest under articles 49 and 50, unless dispensed with under article 51, results in the absence of liability of parties liable on the cheque.

2. Delay in protesting a cheque for non-payment, other than a delay giving rise to dispensation under article 51 (2)

(b), results in the absence of liability of the endorsers and their guarantors, but not of the drawer or his guarantor, except to the extent of the loss suffered by the delay. This provision emphasizes the special nature of the drawer's liability on the cheque which is not purely a secondary liability since the drawer is liable even where there was an unexcused delay in presenting or protesting.

B. NOTICE OF DISHONOUR

Article 53

(1) The holder, upon dishonour of a cheque by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.

(2) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the cheque.

(3) Notice of dishonour operates for the benefit of any party who has a right of recourse on the cheque against the party notified.

Relevant legislation

BEA — section 49.
UCC — sections 3-501 and 3-508
ULC — article 42.

Cross reference

Dishonour by non-payment: article 46.

Commentary

1. As noted in the commentary to article 48 (paragraphs 2-4), the Convention follows the approach of the ULC in considering protest as one of the conditions precedent to the liability of parties secondarily liable. In line with the ULC, the duty of the holder to give due notice of dishonour is not a condition precedent to the liability of the parties entitled to notice but the holder is liable for damages which such parties may have suffered as a consequence of his failure to give due notice. Article 53 should, therefore, be read in conjunction with article 57 which states the consequences of failure to give due notice of dishonour.

2. According to article 53 notice of dishonour must be given by the holder to any prior party and by any party, who has himself received notice, to the party immediately preceding him and liable on the cheque. However, the notice operates for the benefit of any party who has a right of recourse against the party who received notice of dishonour.

Example. The payee endorses the cheque to A. A endorses it to B, B to C and C to D. Upon dishonour of the cheque by the drawee, D must, under article 53, give notice of dishonour to the drawer, the payee, A, B and C and failure to do so will render D liable for damages to the party paying

the cheque. When C receives notice of dishonour from D, C, in turn, must give notice of dishonour to B. Notice sent by D to the drawer ensures for the benefit of the payee, A, B and C.

3. The rule stated in paragraph (2) specifies that notice must be given to an immediately preceding party who is liable on the cheque. Therefore, in the example given above (paragraph 2), if B had endorsed the cheque without recourse, C, having received notice from D, must now give notice to A.

Article 54

(1) Notice of dishonour may be given in any form whatever and in any terms which identify the cheque and state that it has been dishonoured. The return of the dishonoured cheque is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.

(2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.

(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

Relevant legislation

BEA — section 49 (5), (6), (7) and (15).
UCC — section 3-508 (3) and (4).
ULC — article 42.

Cross references

Notice of dishonour: articles 53 to 57.
Dishonour by non-payment: article 46.

Commentary

1. This article retains the substance of the relevant provisions of the BEA, UCC and ULC. It is not necessary that the notice be given in any particular form. It may be given in writing or orally provided that the communication identifies the cheque and conveys the fact that it has been dishonoured by non-payment. The return of the dishonoured cheque with an indication on or off the cheque that it was dishonoured constitutes sufficient notice.

2. Written notice is duly given when it is sent even though it is not received by the addressee. However, the burden of proof that due notice has been given falls on the person who, under article 53, is obliged to give notice.

Article 55

Notice of dishonour must be given within the two business days which follow:

(a) The day of protest, or, if protest is dispensed with, the day of dishonour; or

(b) The receipt of notice given by another party.

Relevant legislation

BEA — section 49 (12).

UCC — section 3-508 (2).

ULC — article 42.

Cross references

Time-limit for protest: article 50.

Protest dispensed with: article 51 (2).

Commentary

1. Article 55 sets forth the period of time within which notice of dishonour can duly be given. It is commercially desirable that parties liable on the cheque as a consequence of dishonour be advised without delay that they have become liable. Inquiries amongst banking and trade circles have led to the conclusion that a period of three days (i.e. the day of protest or, where protest is dispensed with, the day of dishonour, *and* the two business days that follow) is an adequate and practicable period in which to give notice; it will, in most cases, enable the holder's agent in a foreign country where the cheque was payable to inform his principal of the dishonour and will enable the holder to give notice to prior parties. According to article 50 protest must be made on the day on which the cheque is dishonoured (say, Tuesday) or on one of the two business days which follow (Wednesday or Thursday). Pursuant to article 55 notice of dishonour may duly be given on the day of protest (latest possible day: Thursday) or within the two business days which follow (i.e. either Friday or Monday of the following week at the latest).

2. When a party has received notice he in turn may duly give notice on the day on which he received notice or on one of the two business days which follow the day of receipt of notice.

Article 56

(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(2) Notice of dishonour is dispensed with:

(a) If after the exercise of reasonable diligence notice cannot be given;

(b) If the drawer, an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:

(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.

(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person.

Relevant legislation

BEA — section 50.

UCC — section 3-511.

Cross reference

Time-limit for giving notice: article 55.

Commentary

1. Paragraph (1) sets forth the ground justifying delay in giving notice of dishonour. The provision is similar to paragraph (1) of article 44 in respect of delay in making presentment for payment and paragraph (1) of article 51 in respect of delay in protesting a cheque. When delay is excused the liability of the person who is obliged to give notice (i.e. for damages, cf. article 57) is not affected on the ground that there was no due notice.

2. Paragraph (2) states the cases in which notice of dishonour is dispensed with. In such cases the person obliged to give notice is not liable for damages under article 57.

3. As to the legal effects of waiver on or off the cheque see the commentary to article 44 (paragraph 4).

Article 57

Failure to give notice of dishonour renders a person who is required to give such notice under article 53 to a party who is entitled to receive such notice liable for any damages which that party may suffer from such failure, provided that such damages do not exceed the amount referred to in article 59 or 60.

Relevant legislation

BEA — section 48.

UCC — section 3-501 (2).

ULC — article 42.

Cross references

By whom and to whom notice of dishonour must be given: article 53.

Form of notice: article 54.

When to give notice: article 55.

Delay in giving notice: article 56 (1).

Notice dispensed with: article 56 (2).

Commentary

1. The consequences of failure to give notice differ sharply between the Anglo-American law and the Geneva Uniform Law. Under the BEA and the UCC, the giving of notice of dishonour is necessary to charge parties and is thus a condition precedent to their liability on the cheque to the holder or to any other party who has acquired a right of recourse against them. Under the ULC, failure to give notice does not discharge a party's liability on the cheque, but merely makes the party who failed to give notice liable for the damages resulting from such failure. Under the ULC, therefore, a holder or any other party who acquires a right of recourse, but failed to give notice, may exercise such right of recourse upon due protest.

2. Article 57 follows the ULC approach. Due notice of dishonour is not a condition precedent to liability of parties on the cheque but renders the person who failed to give notice liable for damages resulting from such failure. The amount of damages is limited to the amount of the cheque and may include the interest and expenses due under article 59 or 60.

Section 3. Amount payable

Article 58

The holder may exercise his rights on the cheque against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

Relevant legislation

ULC – article 44.

Cross references

Parties liable on the cheque: Section 2 of Chapter Four.

Liability of the drawer: article 37.

Liability of the endorser: article 38.

Liability of the guarantor: article 41.

Commentary

The liability of the parties to a cheque and the conditions in which they become liable are stated in Section 2 of Chapter Four of this Convention. Article 58 is intended to make clear that the holder in exercising his rights on the cheque may proceed against all parties together or against all parties individually or against any individual party without being required to observe the order in which they have become liable. The right of recourse against the endorsers and their guarantors is conditional upon the holder's having

duly presented the cheque and protested the dishonour, except in those cases where presentment and protest is dispensed with. However, the right of recourse against the drawer and his guarantor is conditional upon the holder's having presented the cheque and protested the dishonour, except in those cases where presentment and protest is dispensed with.

Article 59

(1) The holder may recover from any party liable the amount of the cheque.

(2) When payment is made after the cheque has been dishonoured, the holder may recover from any party liable the amount of the cheque with interest at the rate specified in paragraph (3) calculated from the date of presentment to the date of payment and any expenses of protest and of the notices given by him.

(3) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the cheque is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the cheque is payable. In the absence of any such rates, the rate of interest shall be [] per cent per annum.

Relevant legislation

BEA – section 57.

UCC – no equivalent provision, but see section 3-122.

ULC – article 45.

Cross references

Holder: articles 6 (5) and 16.

Commentary

1. Article 59 lays down what sums of money are owed to the holder upon due presentment for payment and what sums of money he may recover, in a recourse action upon dishonour by non-payment, from a party liable to him. Upon presentment the holder is entitled to be paid the amount of the cheque. According to article 62 the holder is not obliged to take partial payment. Upon the dishonour of a cheque by non-payment the holder may recover from any party liable on the cheque (cf. article 46 (2)). Paragraph (2) lays down what the holder may recover in these cases. When the cheque is paid after it was dishonoured, the holder may recover the amount of the cheque; and delay interest at the rate specified in paragraph (3) calculated from the date of presentment on the amount of the cheque; and any expenses consequent upon the making of protest and the giving of any notice of dishonour.

2. The expenses referred to in paragraph (2) do not include bank charges, costs of collection and lawyers' fees but only any legitimate and necessary expenses actually incurred with the making of protest or the giving of notice of dishonour.

3. Paragraph (3) specifies the rate at which interest is to be calculated when the holder recovers in a recourse action upon dishonour by non-payment. The actual percentage points are placed between brackets for further consideration at a future conference of plenipotentiaries which may be called to conclude a convention on the basis of the UNCITRAL draft Convention.

Article 60

A party who pays a cheque in accordance with article 59 may recover from the parties liable to him:

(a) The entire sum which he was obliged to pay in accordance with article 59 and has paid;

(b) Interest on that sum at the rate specified in article 59, paragraph (3), from the date on which he made payment;

(c) Any expenses of the notices given by him.

Relevant legislation

BEA — section 57.

UCC — no equivalent provision, but see section 3-122.

ULC — article 46.

Commentary

1. Article 60 lays down what sums of money a party who has paid a cheque may recover from the drawer, prior endorsers, and the guarantors of the endorsers. Thus, if the payee has taken up and paid the cheque he may recover from the drawer the sum the drawer was compelled to pay pursuant to article 59 and interest on that sum from the date on which the payee made payment.

2. For the purposes of this article it is not necessary that when the party paid the cheque it was endorsed to him or endorsed in blank (cf. article 23).

CHAPTER SIX. DISCHARGE

Section I. Discharge by payment

Article 61

(1) A party is discharged of liability on the cheque when he pays the holder, or a party subsequent to himself who has paid the cheque and is in possession thereof, the amount due pursuant to article 59 or 60.

(2) A party is not discharged of liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the cheque or that the holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(3) (a) A person receiving payment of a cheque must, unless agreed otherwise, deliver:

(i) To the drawee making such payment, the cheque;

(ii) To any other person making such payment, the cheque, a receipted account and any protest.

(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the cheque to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 46.

(c) If payment is made but the person paying, other than the drawee, fails to obtain the cheque, such person is discharged but the discharge cannot be set up as a defence against a protected holder.

Relevant legislation

BEA — sections 59 and 60.

UCC — section 3-603.

Cross references

Knowledge: article 7.

Claim by third person: article 27 (2, 3).

Commentary

1. A person who signs a cheque assumes the obligation to pay the cheque if certain conditions are met (see Chapter Four, Section 2). If a party pays the cheque in accordance with his undertaking, he is discharged of his liability. Article 61 lays down when payment constitutes a discharge of liability.

Paragraph (1)

"Discharged of liability on the cheque"

2. "Discharge" is a technical term used in the Convention for the termination of an undertaking on the cheque. Thus, discharge presupposes liability of the person paying. There is therefore no discharge if the drawee pays since he is not liable on the cheque. Also, there is no discharge if a party whose liability has not crystallized for lack of presentment and protest pays the cheque.

3. The fact that a party is discharged of liability runs with the cheque and has effect against any person subsequent to him; however, the discharge cannot be invoked against a protected holder (cf. article 28 (1) (a)).

4. Payment discharges not only the payer of his liability but also, according to article 67 (1), all parties who have a right of recourse against him. A further effect is that any guarantor of the payer or of another party to whom the payer is liable is discharged to the same extent (cf. article 41 (1)).

5. Payment of a cheque is often intended to discharge an obligation underlying the cheque. Article 61 does not deal with the effect of payment of the cheque on the underlying transaction, nor does it deal with the effect of dishonour by non-payment on the underlying transaction. Article 61 only deals with the consequences of payment on the liability of parties on the cheque itself.

"Pays the holder"

6. Discharge under article 61 is consequent upon payment, i.e. by the payment of money as defined in article 6 (9). Thus, it would not suffice to pay in kind or to give another negotiable instrument.

7. Payment is to be made to the person who is the holder as defined in article 16. Thus, for example, payment to the payee in possession of the cheque is payment to the holder. The same is true in respect of payment to a person in possession of a cheque on which the last endorsement is in blank and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged. On the other hand, if a cheque on which the last endorsement is a special endorsement is delivered to a person other than the person to whom it is endorsed, payment to that person is not payment to the holder and, therefore, does not discharge the payer under article 61.

8. There is one special set of circumstances where payment to a "non-holder" constitutes discharge of liability: if a holder has lost the cheque, he may nevertheless claim payment under certain conditions (see article 73), and payment to such ex-holder discharges the party paying (article 78). In this context, reference should be made to article 73 (2) (d), according to which, under certain conditions, payment may be effected by way of deposit with a court or other competent body.

"A party subsequent to himself who has paid the cheque and is in possession thereof"

9. The person receiving payment is usually the holder. If a cheque is dishonoured by the drawee, the holder has a right of recourse against the drawer, the endorsers and their guarantors. When the drawer of a cheque, or any guarantor, pays, the cheque must be delivered to the payer. In the absence of an endorsement to the payer — and such endorsement is not necessary — the payer, though in possession of the cheque, is not a holder. However, such payer, if in possession of the cheque, has a right to payment against prior parties. Article 61 provides that payment by such

parties to him discharges the party paying of his liability on the cheque.

Paragraph (2)

10. Paragraph (2) deals with the question whether discharge may be affected or prevented by a claim of a third party to the cheque. If the party paying had no knowledge of such claim, payment by such party constitutes discharge, provided that the other requirements of article 61 are met. Among other things the party must pay to the holder and not, for example, to a person in possession of a cheque on which there appears an interrupted series of endorsements. Even if the payer did not know that one of the endorsements was forged, he is not discharged since he did not pay to the holder. Thus, for there to be discharge, a party must examine the regularity of the endorsements but is not required to examine their genuineness.

11. If, on the other hand, the party paying had knowledge of a claim of a third party, the decisive factor is whether or not he was under an obligation to pay. Thus, he is discharged if he paid a protected holder under circumstances in which he, the payer, could not have raised the defence of *ius tertii* in an action on the cheque by the protected holder (cf. article 28 (2)).

12. In respect of payment of a cheque to which there is a claim by a third party, payment to the holder who is not a protected holder discharges the payer only if he cannot raise the defence of *ius tertii* under article 27 (3) against such holder. This is so because in such a case the payer is obliged to pay and payment by him should therefore discharge him of liability.

Example A. A cheque made payable to bearer is stolen from A. The thief is therefore a holder. Payment by the drawer to the thief with knowledge of the theft does not discharge the drawer.

Example B. A induces the payee to endorse the cheque to A. A demands payment from the drawer who knows about the fraud. The payee has not asserted a claim to the cheque. Payment by the drawer to A discharges the drawer of liability.

Paragraph (3) (a)

13. A holder who receives payment from a party or the drawee must deliver the cheque to the payer. The payer's right to possession is justified by the fact that, if the cheque remained in the hands of the person receiving payment and that person transferred the cheque to a protected holder, the payer, if a party, would be obliged to pay the cheque a second time upon presentment by the protected holder (cf. articles 28, 61 (3) (c)).

14. If the payer is a party, the person receiving payment must deliver, in addition to the cheque, a receipted account and any protest (subparagraph (ii)). These docu-

ments are necessary to enable the payer to exercise rights on the cheque against parties liable to him (cf. article 60).

Paragraph (3) (b)

15. The person from whom payment is demanded is not required to pay if the cheque is not delivered to him. Withholding payment in these circumstances does not constitute dishonour by non-payment. Consequently, in such a case the person who refuses to deliver the cheque would not be entitled to exercise a right of recourse against parties liable to him. However, if the cheque is not delivered because it has been lost, the special rules on lost cheques apply (articles 73-78).

Paragraph (3) (c)

16. If the person from whom payment is demanded pays the cheque although it is not delivered to him, such payment constitutes a discharge of liability on the cheque but such discharge may not be raised as a defence against a protected holder (cf. article 28).

Example C. The drawer issues a cheque to the payee. The payee endorses the cheque to A who endorses it to B. B presents the cheque for payment to the drawee who refuses payment. Upon protest, B asks payment from the payee. The payee pays but B retains the cheque. Subsequently, B requests payment from A. A may raise as a defence against B that the cheque was paid by the payee, and that he therefore is discharged of liability on the cheque (cf. article 67).

Example D. The drawer issues a cheque to the payee. The payee endorses it to A who endorses it to B. B presents the cheque for payment to the drawee. The drawee pays but B retains possession of the cheque. B endorses the cheque to C who is not a protected holder. C presents the cheque for payment to the drawee. The drawee refuses to pay. C brings an action against the drawer. Because C is not a protected holder, the drawer may raise the defence that the cheque was already paid and that such payment discharged him. If, on the other hand, C is a protected holder, then payment by the drawee cannot be raised as a defence, neither by the drawer nor by parties prior to C.

Article 62

- (1) The holder is not obliged to take partial payment.
- (2) If the holder who is offered partial payment does not take it, the cheque is dishonoured by non-payment.
- (3) If the holder takes partial payment from the drawee, the cheque is to be considered as dishonoured by non-payment as to the amount unpaid.
- (4) If the holder takes partial payment from a party to the cheque

(a) The party making payment is discharged of his liability on the cheque to the extent of the amount paid; and

(b) The holder must give such party a certified copy of the cheque and of any authenticated protest.

(5) The drawee or a party making partial payment may require that mention of such payment be made on the cheque and that a receipt therefor be given to him.

(6) If the balance is paid, the person who receives it and who is in possession of the cheque must deliver to the payer the receipted cheque and any authenticated protest.

Relevant legislation

BEA – section 47.
UCC – section 3-507.
ULC – article 34.

Cross references

Discharge by payment: article 61.
Dishonour by non-payment: article 46.
Authenticated protest: article 49 (3).

Commentary

1. A party's undertaking is to pay the cheque in full as provided in articles 59 and 60. Accordingly, a holder is entitled to receive the full amount; he is not obliged to take partial payment which would impose on him the burden of having to claim the remaining part of the sum from another party.

2. Consequently, if he does not accept partial payment, the cheque is dishonoured by non-payment and the holder has rights against parties liable to him for the full amount. If, however, he elects to take partial payment, any party liable is discharged *pro tanto* (paragraph (4) (a) and article 67) and the cheque is dishonoured to the extent of the amount unpaid (paragraph (3)).

3. If partial payment is made the payer is not entitled to receive the cheque since the holder needs it in order to obtain payment of the amount unpaid. In order to give the payer the protection which he would have by receiving the cheque (article 61 (3)), he may require that his partial payment be stated on the cheque and that he be given a receipt for it. As regards payment of the remaining part of the cheque, the payer of it is entitled to receive the receipted cheque.

4. If partial payment is made by a person other than the drawee or the drawer, that person has, as a party secondarily liable, a right of recourse. Since he does not receive the cheque (see above, paragraph 3), he needs some other document to exercise his right of recourse as to the amount paid by him. Therefore, the holder must give such party a

certified copy of the cheque and of any protest, if protest was made as a separate document (paragraph (4) (b)).

Article 63

(1) The holder may refuse to take payment in a place other than the place where the cheque was presented for payment in accordance with article 43.

(2) If in such case payment is not made in the place where the cheque was presented for payment in accordance with article 43, the cheque is considered as dishonoured by non-payment.

Relevant legislation

BEA – section 45 (4).

UCC – section 3-504.

ULC – article 9 of annex II to Geneva Convention of 1931.

Cross references

Presentment for payment: article 43.

Dishonour by non-payment: article 46.

Commentary

Article 43 specifies the proper place for due presentment for payment (see paragraphs (c) and (d)). Since it is commercially reasonable to require that payment be made at such place, article 63 provides that an offer to pay the cheque in some other place may be rejected by the holder, who may then treat the cheque as dishonoured by non-payment. However, if the holder accepts payment at another place, the payer is discharged of liability on the cheque according to article 61.

Article 64

(1) A cheque must be paid in the currency in which the amount of the cheque is expressed.

(2) The drawer may indicate on the cheque that it must be paid in a specified currency other than the currency in which the amount of the cheque is expressed. In that case:

(a) The cheque must be paid in the currency so specified;

(b) The amount payable is to be calculated according to the rate of exchange indicated on the cheque. Failing such an indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment:

(i) Ruling at the place where the cheque must be presented for payment in accordance with article 43 (c), if the specified currency is that of that place (local currency); or

(ii) If the specified currency is not that of that place, according to the usages of the place where the cheque must be presented for payment in accordance with article 43 (c);

(c) If such a cheque is dishonoured by non-payment, the amount payable is to be calculated:

(i) If the rate of exchange is indicated on the cheque, according to that rate;

(ii) If no rate of exchange is indicated on the cheque, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment at the place where the cheque must be presented for payment in accordance with article 43 (c) or at the place of actual payment.

(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-payment.

Relevant legislation

BEA – section 72 (4).

UCC – section 3-107 (2).

ULC – article 36.

Cross references

Currency: article 6 (9).

Rate of exchange indicated on the cheque: article 8 (a).

Dishonour by non-payment: article 46.

Commentary

1. This article lays down rules in respect of payment of a cheque denominated in a currency which is not that of the place of payment. In respect of such cheque the following questions arise:

(a) May a person liable on the cheque discharge that liability by paying in the currency of the place of payment or must he pay in the currency in which the amount of the cheque is expressed?

(b) If payment is made upon presentment in local currency, what should be the rate of exchange between the currency in which the amount of the cheque is expressed and the currency of the place of payment?

(c) If the cheque is dishonoured by non-payment and a change in the rate of the specified currency *vis-à-vis* the currency of the place of payment takes place after the date of dishonour, what are then the obligations of the parties liable on the cheque?

Paragraph (1)

2. When a cheque is drawn payable in a currency which is not that of the place of payment, in which currency

("foreign" or "local") should payment be made upon presentment in order to discharge parties of their liability on the cheque? In theory, one can envisage the following answers:

(a) The party liable must pay in the specified foreign currency. The rationale behind this approach is that when a cheque is drawn payable in a foreign currency, the parties manifest thereby their intention that the cheque be paid in that currency;

(b) The party liable must pay in local currency. The rationale behind this approach is that the mere specification of a foreign currency on a cheque does not necessarily manifest an intention that the cheque should be paid in such currency. Such intention should be manifested by an express provision requiring payment in the specified foreign currency. According to this view, the specification of the amount of the cheque in a foreign currency serves only the purpose of providing a criterion according to which the value of the local currency is to be measured;

(c) The party liable has an option to pay in either local or foreign currency. The rationale behind this approach is that the fact that a cheque was drawn payable in a foreign currency should permit the person liable to pay either in that currency or in the currency of the place of payment;

(d) The holder has an option to demand payment in either local or foreign currency. The rationale is that the absence of a strong and clear indication of the obligation to pay in foreign currency should operate in favour of the holder.

3. Paragraph (1) states the basic rule that a cheque drawn payable in a currency other than that of the place of payment is, in the absence of an express stipulation to the contrary, to be paid in that currency. Enquiries made amongst banking circles revealed that under current commercial and banking practices instruments are frequently paid in the currency in which the amount of an instrument is expressed even though it is not stipulated on the instrument that payment be made in such currency. The rule, it is submitted, is a most suitable one at a time of frequent fluctuations between currencies.

4. It follows from the rule stated in paragraph (1) that if the drawee offers to pay the cheque, denominated in a specified currency, in the currency of the place of payment, the holder may consider the cheque to be dishonoured by non-payment.

5. The rule is subject to exchange control regulations imposing restrictions on payment in a currency other than that of the place of payment (cf. article 65).

Paragraph (2) (a) and (b)

6. The drawer of a cheque may stipulate on it that it is to be paid in a specified currency other than the currency in which the amount of the cheque is expressed. In such a

case the cheque is to be paid in the specified currency. Thus if a cheque is denominated in Swiss francs and contains a stipulation that it is to be paid in rubles, the cheque must be paid in rubles. Under article 8 (b) the sum so payable is deemed to be a definite sum for the purposes of article 1. In such a case the question arises as to what rate of exchange should be applicable. If a rate of exchange is indicated on the cheque the amount payable is to be calculated according to that rate. Under article 8 (a) the sum so payable is deemed to be a definite sum for the purposes of article 1. If no rate of exchange is indicated on the cheque the amount payable is to be calculated according to the rate of exchange for sight drafts (or, in the absence of such rate, according to the appropriate established rate of exchange) on the date of presentment. The rate of exchange is the rate ruling at the place where the cheque must be presented for payment in accordance with article 43 (c) (see paragraph (2) (b) (i) and (ii)).

Paragraph 2 (c)

7. Where a cheque is dishonoured by non-payment the holder has, upon due protest (cf. article 48), a right of recourse against prior parties (cf. article 46 (2)). The question then arises as to what rate of exchange should prevail when payment is made: the rate specified on the cheque (if so specified), the rate ruling on the date of presentment or on the date of actual payment. The further question arises whether provision should be made for one or several possible rates of exchange or whether the holder or the payer should be entitled to exercise an option between two or more of these rates and, if so, under what circumstances. Yet another question is whether the rules applicable to the rate of exchange should be the same for all parties liable on the cheque or whether a distinction should be made between the drawer and parties secondarily liable. Lastly, the question arises whether the rate of exchange should be that prevailing at the place where the cheque should have been paid upon due presentment for payment or that prevailing at the place where payment is actually made.

8. Subparagraph (c) (i) provides that, in the case of dishonour by non-payment, if a rate of exchange is indicated on the cheque that rate prevails. If the rate of exchange is not indicated on the cheque, subparagraph (c) (ii) provides that the holder has the option of demanding that payment be made at either the rate of exchange ruling on the date of presentment or on the date of actual payment. The holder is given the option of choosing between two rates of exchange in order to protect him against any loss he may suffer because of speculation by the party liable. Subparagraph (c) (ii) further sets forth a rule as to the place which determines the rate of exchange if the amount payable is to be calculated according to a rate prevailing at a given date. Upon dishonour the holder has the option of choosing between the rate of exchange ruling at the place where the cheque must be

presented for payment under article 43 (c) and that ruling at the place of actual payment.

Paragraph (3)

9. Under certain legal systems a holder may be awarded damages compensating him for loss suffered because of fluctuations in rates of exchange if such loss is caused by dishonour by non-payment. Paragraph (3) preserves such right to damages which a holder may have under the applicable law. It must be noted, however, that paragraph (3) does not create a statutory right entitling a holder to damages in the event of his suffering loss because of fluctuations in rates of exchange.

Article 65

(1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party.

(2) (a) If, by virtue of the application of paragraph (1) of this article, a cheque drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment ruling at the place where the cheque must be presented for payment in accordance with article 43 (c).

(b) If such a cheque is dishonoured by non-payment:

- (i) The amount is to be calculated, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment;
- (ii) Paragraph (3) of article 64 is applicable where appropriate.

Cross references

Currency: article 6 (9).

Dishonour by non-payment: article 46.

Commentary

Paragraph (1)

1. As noted in the commentary to article 64 (paragraph 5), the provisions regarding payment in a currency that is not the currency of the place of payment are subject to exchange control regulations imposing restrictions on payment in such currency. Therefore, article 65 sets forth a general provision to this effect. The regulatory provisions referred to in this article are not only those of the Contracting State itself but include those which the Contracting State is bound

to enforce by virtue of international agreements to which it is a party. An example of the latter type of regulatory provisions is Article VIII, section 2 (b), of the Articles of Agreement of the International Monetary Fund according to which "exchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with [the Fund] Agreement shall be unenforceable in the territories of any member".

Paragraph (2)

2. This paragraph envisages situations where in accordance with article 64 a cheque is to be paid in a currency which is not the currency of the place of payment but where by virtue of the application of paragraph (1) of article 65 it is to be paid in local currency. For these situations paragraph (2) sets forth rules regarding the rate of exchange to be applied and on which date that are similar to the rules set forth in article 64 (2) and (3).

Article 66

If the drawer countermands the order to the drawee to pay a cheque drawn on him, the drawee is under a duty not to pay.

Relevant legislation

BEA — section 75.

UCC — section 4-403.

ULC — article 32.

Commentary

1. The BEA, UCC and ULC all contain rules as to the legal effect of an order by the drawer to the drawee-bank to stop payment of a cheque payable for his account. The systems differ as to the duty of the drawee-bank when it receives such an order.

2. Under the UCC (section 4-403) a customer has the right to stop payment of a cheque, and the drawee-bank has a corresponding duty to comply with such order, provided the order is received by the bank at such time and in such manner as to afford it a reasonable opportunity to act. There is no right to stop payment after the cheque has been "certified", i.e. accepted. Payment of a cheque by the drawee-bank in violation of the stop payment order is improper payment. In such a case the drawee-bank must recredit the drawer's account but is entitled to subrogation to prevent unjust enrichment (section 4-407).

3. Similar rights obtain under the BEA to the extent that the drawee-bank is obliged to comply with its customer's order countermanding payment.

4. According to the ULC the countermand of a cheque is without effect until the expiration of the time-limit for

presentment. The holder of a cheque is thus protected against a stop payment order by the drawer until that time-limit has expired. There are within the various countries following the Geneva Uniform Law different interpretations in respect of the duty of the drawee-bank to comply with the countermand.

5. Article 66 follows the approach of the common law jurisdictions that the drawee-bank must comply with the countermand of the drawer. If the bank disregards the countermand and pays the cheque it may not debit the account of the drawer. It should be noted that a countermand once notified to the drawee remains effective until revoked by the drawer.

Section 2. Discharge of a prior party

Article 67

(1) When a party is discharged wholly or partly of his liability on the cheque, any party who has a right of recourse against him is discharged to the same extent.

(2) Payment by the drawee of the whole or a part of the amount of the cheque to the holder, or to any party who has paid the cheque in accordance with article 59, discharges all parties of their liability to the same extent.

Relevant legislation

BEA — section 37.

UCC — section 3-208.

ULC — article 47.

Cross reference

Discharge: article 61.

Commentary

1. The discharge of a party of his liability on the cheque affects also the rights of parties subsequent to him. When a party signed the cheque he was entitled to assume that, if he paid the cheque, he would have a right of recourse against prior parties. The discharge of a prior party impairs this right of recourse. It is reasonable therefore that in such a case parties subsequent to the party discharged are also discharged.

Example. The payee endorses a cheque to A who endorses it to B. Payment by the drawer to B operates as a discharge of the payee and A.

2. Similarly, payment by the drawee discharges all parties of their liability (paragraph (2)).

3. Where payment is made only in part, the discharge of the subsequent parties is to the extent of that partial payment.

CHAPTER SEVEN. CROSSED CHEQUES AND CHEQUES PAYABLE IN ACCOUNT

Section 1. Crossed cheques

Article 68

(1) A cheque is crossed if it bears across its face two parallel transverse lines.

(2) A crossing is general if it consists of the two lines only or if between the two lines the word "banker" or an equivalent term or the words "and Company" or any abbreviation thereof is inserted; it is special if the name of a banker is so inserted.

(3) A cheque may be crossed generally or specially by the drawer or the holder.

(4) The holder may convert a general crossing into a special crossing.

(5) A special crossing may not be converted into a general crossing.

(6) The banker to whom a cheque is crossed specially may again cross it specially to another banker for collection.

Relevant legislation

BEA — sections 76 to 81.

ULC — articles 37 and 38.

Commentary

1. The practice of crossing cheques is known and has received statutory recognition in both civil law and common law countries though the legal effects of crossing may be different. One function of crossing a cheque is common to all legal systems which know the practice: to lessen the risk that the drawee-bank pays a cheque to a person who is not the true owner of it in that the drawee-bank is obliged to make payment either to a bank or to its own customer. Consequently if the drawee-bank pays not in accordance with the crossing and the person to whom it pays the crossed cheque is not the true owner of it, the drawee-bank does not make due payment and, therefore, may not debit the drawer's account. The difference between civil law and common law systems lies in the fact that, in common law systems, if the drawee-bank pays a cheque in accordance with the crossing in good faith and without negligence it may raise that fact as a defence if so paying it did not make payment to the true owner. The same defence is available to a collecting bank. The need for such a defence does not arise in the systems based on the Geneva Uniform Law because of the general rules set forth in articles 19 and 35 of the ULC (see commentary to article 25, paragraphs 8-10).

2. This Convention provides for the possibility of crossing a cheque in order to achieve the purpose of cross-

ings common to all systems: to lessen the risk that cheques are paid to the wrong person. The Convention therefore makes provision for the manner in which an international cheque may be crossed and sets forth the basic rule that payment by a drawee-bank not in accordance with the crossing imposes liability on the drawee-bank. Liability is also imposed on a collecting bank which collects a cheque not in accordance with the crossing. Because of the provisions of the Convention relating to the legal effects of a forged endorsement, the Convention need not, and does not, retain the defence available in common law systems to a drawee-bank or collecting bank that it paid or collected a cheque in good faith and without negligence in accordance with the crossing. However, under article 25 (2) the liability of the drawee-bank which pays the person who forged an endorsement and of the collecting bank which collects as an agent of such forger is not regulated by this Convention. Therefore, such a drawee-bank or collecting bank may, under some applicable national laws, be liable to the true owner and may then be in a position to raise the defence of payment in accordance with the crossing in good faith and without negligence.

3. Paragraph (1) states the manner in which a crossing of a cheque is effected, in accordance with general practice: the crossing consists of two parallel transverse lines drawn across the face of the cheque. Transverse lines include vertical but not horizontal lines.

4. A crossing may be either general or special. It is general if it consists of two parallel transverse lines only or with the word "banker" or an equivalent term or the words "and Company" or any abbreviation thereof inserted between those lines. It is special if the name of a banker is inserted between the two parallel transverse lines.

5. A general crossing may be converted into a special crossing but not vice versa. The banker to whom a cheque is crossed specially may in turn cross it specially to another banker for collection.

6. Only the drawer and a holder may cross a cheque either generally or specially. However, only a holder may convert a general crossing into a special crossing. Thus the drawee or a guarantor, if he is not a holder, may not cross a cheque or convert the crossing from general into special. If he does so the rules on material alteration apply (cf. article 33).

Article 69

If a cheque shows on its face the obliteration either of a crossing or of the name of the banker to whom it is crossed, the obliteration is considered as not having taken place.

Relevant legislation

BEA — section 78.
ULC — article 37.

Commentary

Once a cheque has been crossed the crossing, in that it produces legal effects, becomes an integral part of the cheque. Therefore the holder may not obliterate the crossing or convert a special crossing into a general crossing by striking out the name of the banker. Any such obliteration or striking out is deemed not to have taken place.

Article 70

(1) (a) A cheque which is crossed generally is payable only to a banker or to a customer of the drawee.

(b) A cheque which is crossed specially is payable only to the banker to whom it is crossed or, if such banker is the drawee, to his customer.

(c) A banker may not take a crossed cheque except from his customer or from another banker and may not collect such a cheque except for such a person.

(2) The drawee who pays, or the banker who takes or collects, a crossed cheque in violation of the provisions of paragraph (1) of this article incurs liability for any damages which a person may have suffered as a result of such violation, provided that such damages do not exceed the amount of the cheque.

Relevant legislation

BEA — section 79.
ULC — article 38.

Commentary

1. This article sets forth the legal effects of a general or special crossing of a cheque and the consequences of inobservance of such crossing.

2. The effect of crossing a cheque is that the drawee-bank is directed to pay the cheque only to a holder who is a banker or to its customer and, if the cheque is crossed specially, to the banker named in the crossing or to the customer of the named banker if that banker is the drawee. The purpose of this rule is to protect the true owner to the extent that if payment is made to someone not entitled to it he, the true owner, may more easily trace the person to whom payment was made and recover from him.

3. If the drawee-bank pays, or a collecting bank collects, a crossed cheque not in accordance with the crossing it will be liable for damages which the true owner may have suffered because of the inobservance. Such damages may not exceed the amount of the cheque.

Article 71

If the crossing on a cheque contains the words "not negotiable" the transferee becomes a holder but cannot become a protected holder. However, such transferee may acquire the rights of a protected holder under article 29.

Relevant legislation

BEA — section 81.

Commentary

The addition of the words "not negotiable" to a crossed cheque has the following effect:

(a) The holder may transfer the cheque notwithstanding the provision of article 18; and

(b) The transferee cannot become a protected holder in his own right.

*Section 2. Cheques payable in account**Article 72*

(1)(a) The drawer or the holder of a cheque may prohibit its payment in cash by writing transversally across the face of the cheque the words "payable in account" or words of similar import.

(b) In such case the cheque may only be paid by the drawee by means of a book-entry.

(2) The drawee who pays such a cheque otherwise than by means of a book-entry incurs liability for any damages which a person may have suffered as a result thereof, provided that such damages do not exceed the amount of the cheque.

(3) If a cheque shows on its face the obliteration of the words "payable in account", the obliteration is considered as not having taken place.

Relevant legislation

ULC — article 39.

Commentary

1. This article provides an exception to the rule that the payee is entitled to payment of the cheque in cash. The drawer or the holder may, by writing transversally across the face of the cheque the words "payable in account" (or words of similar import), direct the drawee-bank to pay the cheque only by means of a book-entry. If the drawee-bank fails to observe the direction so given, it will be liable for damages to the true owner of the cheque. Such damages may not exceed the amount of the cheque.

2. Obliteration of the words directing the drawee-bank to pay the cheque only by means of a book-entry is deemed not to have taken place.

CHAPTER EIGHT. LOST CHEQUES

Article 73

(1) When a cheque is lost, whether by destruction, theft or otherwise, the person who lost the cheque has,

subject to the provisions of paragraph (2) and (3) of this article, the same right to payment which he would have had if he had been in possession of the cheque. The party from whom payment is claimed cannot set up as a defence against liability on the cheque the fact that the person claiming payment is not in possession thereof.

(2)(a) The person claiming payment of a lost cheque must state in writing to the party from whom he claims payment:

(i) The elements of the lost cheque pertaining to the requirements set forth in article 1 (2); for this purpose the person claiming payment of the lost cheque may present to that party a copy of that cheque;

(ii) The facts showing that, if he had been in possession of the cheque, he would have had a right to payment from the party from whom payment is claimed;

(iii) The facts which prevent production of the cheque.

(b) The party from whom payment of a lost cheque is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost cheque.

(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms.

(d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost cheque, and any interest and expenses which may be claimed under article 59 or 60, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

(3) The person claiming payment of a lost cheque in accordance with the provisions of this article need not give security to the drawer who has inserted in the cheque, or to an endorser who has inserted in his endorsement, such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import.

Relevant legislation

BEA — section 70.

UCC — section 3-804.

ULC — articles 7 and 16 of annex II to Geneva Convention of 1931.

Cross references

Defences against liability: articles 27 and 28.

Discharge by payment: article 61.

Commentary

1. Under the Convention the rights on a cheque are vested in the holder, i.e. the payee or endorsee who is in possession of the cheque or the possessor of a bearer cheque (cf. articles 6 (5) and 16). Thus a holder when losing possession of the cheque is no longer a holder. The question, then, is what are the rights of such an "ex-holder"?

2. Legal systems generally recognize that the loss of a cheque does not entail loss of the rights thereon. However, they differ as to the procedures and conditions under which the ex-holder may exercise his rights. Most legal systems of civil law tradition provide for a special cancellation procedure: upon request by the ex-holder, accompanied by a statement setting forth the essential elements of the lost cheque and the circumstances of its loss, the court may issue a cancellation order which terminates the validity and effect of the lost cheque and serves the ex-holder as a substitute for the lost cheque. On the other hand, under the BEA and the UCC, no such cancellation procedure is required. The ex-holder may maintain an action on the lost cheque but may be required to give security to the payer so as to cover the risk of the payer of having to pay twice, i.e. to the ex-holder and to a holder in due course of the lost cheque.

3. The latter approach has been adopted in the Convention which requires the giving of security and of a written statement by the ex-holder (article 73 (2)). The institution of cancellation, as embodied in national laws of civil law tradition, seemed less appropriate in the context of an international negotiable instrument because cancellation takes place by a judicial decision which would not necessarily be known in countries other than the country in which it was rendered.

Paragraph (1)

4. Article 73, paragraph (1), expresses the idea, common to all systems, that the loss of a cheque does not result in loss of the rights on it. Loss of the cheque is to be understood in a wide sense. It includes, in addition to normal loss, any loss by destruction, theft or any other dispossession against the possessor's will.

5. Under paragraph (1), the ex-holder has, subject to the provisions of paragraph (2), the same right to payment as he would have had if he had been in possession of the cheque. Retention of his legal position means not only that he retains his rights on the cheque but also that he retains any burden, i.e. to make presentment (cf. article 45), to make protest (cf. article 48), to give notice of dishonour (cf. article 53 (1)), and continues to be subject to the same claims and defences as before.

Example A. The drawer draws a cheque payable to payee (P), P endorses it to A who loses it. Under article 73, paragraph (1), A has the right to claim payment from the drawer and P; but, before he may claim payment he must make presentment for payment and any necessary protest if payment is refused (article 76). In an action brought against the drawer and P, each party may raise any defence which he could raise if A would be in possession of the cheque. On the other hand, if the drawer or P pays, such payment constitutes a discharge and is a defence available against any holder who is not a protected holder.

6. The provisions on lost cheques are applicable only to situations where an ex-holder claims payment from a party, but not to cases where payment is sought from the drawee. This is clear from the use of the word "party" instead of "person". The underlying reason is that, since a drawee is not liable on the cheque, payment by him would be at his own risk.

Paragraph (2)

7. According to paragraph (1), the ex-holder's exercise of his rights is subject to the provisions of paragraph (2) which lays down two requirements. The ex-holder must give security to the person from whom he claims payment as regulated in subparagraphs (b) and (c). An alternative method of security is envisaged in subparagraph (d). He must also supply that person with a written statement the contents of which are set forth in subparagraph (a). Such statement is intended to substitute for the lost cheque.

Subparagraph (a)

8. Under subparagraph (a), the ex-holder must state in writing certain elements of the lost cheque (i) and certain facts (ii, iii). If he does not do so, he may not exercise his rights under article 73. This would, for example, include the case where he does not remember the sum of the cheque or the date of the cheque.

9. The procedure under the provisions on lost cheques may only be used if the cheque at the time it was lost was a complete cheque, i.e. complied with the formal requisites set forth in article 1 (2). Therefore a cheque cannot be completed by the use of the written statement.

10. Subparagraph (ii) requires that the ex-holder show that he was a holder of the cheque. For example, he must show that, at the time of the loss of an order cheque, he held it through an uninterrupted series of endorsements (cf. article 16 (1) (c)). Finally, subparagraph (iii) requires from the ex-holder to state that he lost the cheque and how.

Subparagraphs (b), (c) and (d)

11. In addition to the above written statement the ex-holder must give security to the person from whom he

claims payment. This requirement arises from the fact that under the Convention a party must pay the ex-holder. However, the lost cheque may get into the hands of a protected holder against whom such party could not raise the first payment as a defence (cf. article 28 (1) (a)). The security is intended to provide for such contingency and to cover the risk of his being obliged to pay a second time.

Example B. In the situation described in example A (above, paragraph 5), the lost cheque is found by B who forges A's signature and endorses it to C. C endorses it to D. If D is a protected holder, he has a right to claim payment.

12. According to subparagraph (c), it is for the parties to settle the matters relating to the security, i.e. whether it is needed and, if so, its nature and terms. However, if the parties cannot agree, a court may make a determination. For example, it may decide, if security is needed, that a bank guarantee in a specified amount be given.

13. Subparagraph (d) provides an alternative way of covering the risk of double payment in those cases where security cannot be given. A court may order that the party from whom payment is claimed deposit the amount of the lost cheque and any interest and expenses recoverable under article 59 or 60 with the court or with another authority or institution which is competent under national law to receive and hold such deposit. According to subparagraph (d), the deposit is then to be considered as payment to the claimant. Such payment has the same legal effects under the Convention as any ordinary payment.

Paragraph (3)

14. A cheque in which the drawer or an endorser has inserted the words "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import may not be transferred except for purposes of collection, and the transferee does not become a holder except for such purposes (cf. article 18). It follows that such holder for collection may not qualify as a protected holder in his own right (cf. article 22 (1) (c)). Thus, if the lost cheque is presented for payment by such holder the party from whom payment is demanded may refuse to pay. Therefore, a person claiming payment of a lost cheque containing the above words need not give security.

Article 74

(1) A party who has paid a lost cheque and to whom the cheque is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

(2) Such notification must be given on the day the cheque is presented for payment or on one of the two business days which follow and must state the name of the person presenting the cheque and the date and place of presentment.

(3) Failure to notify renders the party who has paid the lost cheque liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 59 or 60.

(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost cheque and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

Commentary

Paragraph (1)

1. Article 74 imposes upon the party who has paid the cheque to the ex-holder the obligation to notify him of a subsequent presentment of the cheque for payment. The purpose of that notification is to enable the ex-holder to assert a claim to the cheque, to prevent a party from paying the cheque to a holder (cf. article 27 (3)) or to claim damages under article 25.

Paragraph (2)

2. Paragraph (2) sets forth the required particulars and the time-limit for the notification. Speedy notification is imperative in such situations where someone appears with the lost cheque since the surrounding circumstances normally make this a matter of urgency.

Paragraph (3)

3. If the party who paid the lost cheque fails to give the notification he is liable for damages which the ex-holder might suffer because of that failure. Damages may result, for example, from circumstances such as these: The payee (P) loses the cheque and receives payment from the drawer under article 73; the thief forges P's signature and endorses the cheque to A; A endorses the cheque to B who presents it for payment to the drawee. The drawee dishonours the cheque and payment is demanded from the drawer. Under paragraph (1) it is the duty of the drawer to notify P that B has presented the cheque to him. Such notification may, for example, enable P to claim damages from A who, at the time of notification, is solvent. If the drawer fails to notify and A becomes insolvent, P may claim damages from the drawer to compensate him for not having been able to recover damages from A when he was still solvent.

4. Such action for damages based on failure to notify is an action off the cheque like, for example, the actions provided for under articles 25, 39 and 57.

Paragraphs (4) and (5)

5. Paragraphs (4) and (5) set forth the circumstances under which delay in giving notice is excused or under which notice is dispensed with, similar to the provisions of article 44.

Article 75

(1) A party who has paid a lost cheque in accordance with the provisions of article 73 and who is subsequently required to, and does, pay the cheque, or who, by reason of the loss of the cheque, then loses his right to recover from any party liable to him, has the right:

(a) If security was given, to realize the security; or

(b) If the amount was deposited with the court or other competent authority or institution, to reclaim the amount so deposited.

(2) The person who has given security in accordance with the provisions of paragraph (2) (b) of article 73 is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the cheque is lost.

Commentary

Paragraph (1)

1. This provision sets forth the circumstances under which a party who paid a lost cheque in accordance with article 73 may realize the security given to him or claim the amount deposited under article 73, paragraph (2) (d). The first of these situations is where a party had to pay a second time. The other situation is where a party who received security loses his right of recourse by reason of payment by a prior party. For example, a cheque endorsed by the payee to A and by A to B is lost by B. B asks payment from A under article 73 and is paid upon giving security to A. C acquires the lost cheque under circumstances which make him a protected holder. C demands payment from the drawer and is paid by him. Payment by the drawer discharges the payee. Therefore, because A loses his right of recourse against the payee and the drawer, A may realize the security.

Paragraph (2)

2. This provision deals with the circumstances under which an ex-holder who gave security and received payment is entitled to obtain release of the security. He may do so when the party who paid and received the security is no longer at risk to be obliged to pay a second time. This is the case, for example, where the time periods provided in article 79 have expired or where proof is brought that the lost cheque was in fact destroyed.

Article 76

A person claiming payment of a lost cheque duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 73, paragraph (2) (a).

Cross reference

Protest: article 49.

Commentary

1. The fact that the cheque is lost does not dispense the ex-holder of the obligation to protest the cheque in the event of dishonour by non-payment. Article 76 lays down rules as to how protest is to be effected in this case: it is to be effected by use of the same item as is used for presentment, i.e. the written statement which satisfies the requirements of article 73, paragraph (2) (a), and, as provided therein, may be a copy of the lost cheque.

2. In the lost cheque situation, in general, the ordinary rules apply except for the replacement of the lost cheque by the written statement. Thus, e.g., a declaration made in accordance with article 49, paragraph (3), is deemed to be a protest for the purpose of the Convention (cf. article 49 (4)) also in the case of a lost cheque.

Article 77

A person receiving payment of a lost cheque in accordance with article 73 must deliver to the party paying the written statement required under article 73, paragraph (2) (a), receipted by him and any protest and a receipted account.

Cross reference

Payment: article 61.

Commentary

Under article 61, paragraph (3), the person receiving payment must deliver the cheque (and any protest and a receipted account) to the payer; if he does not do so, the person from whom payment is demanded may withhold payment. Article 77 makes it clear that the person obliged to pay may not withhold payment on the mere ground that the person claiming payment is unable to deliver the (lost) cheque; therefore, such withholding would constitute dishonour. However he must deliver the written statement which substitutes for the lost cheque.

Article 78

(1) A party who has paid a lost cheque in accordance with article 73 has the same rights which he would have had if he had been in possession of the cheque.

(2) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 77.

Cross reference

Right of recourse: article 60.

Commentary

This provision establishes in respect of parties who took up and paid a lost cheque rights similar to those of the ex-holder under article 73. Thus, where an endorser, upon dishonour by the drawee, pays the ex-holder, the endorser has in turn, against prior parties, those rights on the lost cheque which he would have had if he had acquired, upon payment, possession of the cheque.

CHAPTER NINE. LIMITATION (PRESCRIPTION)

Article 79

(1) A right of action arising on a cheque can no longer be exercised after four years have elapsed:

(a) Against the drawer or his guarantor, from the date of the cheque;

(b) Against an endorser or his guarantor, from the date of protest for dishonour or, where protest is dispensed with, the date of dishonour.

(2) If a party has paid the cheque in accordance with article 59 or 60 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year from the date on which he paid the cheque.

Relevant legislation

UCC — section 3-122.

ULC — articles 52, 53 and 56; article 26 of annex II to Geneva Convention of 1931.

Cross references

Protest for dishonour by non-payment: article 50.

Dispensation of protest: article 51 (2).

Exercise of right of recourse: article 48.

Commentary

1. This article lays down special rules in respect of the period of time within which an action arising on the cheque

must be brought and the point of time from which such period starts to run. The article does not deal with actions off the cheque (e.g. those arising by virtue of article 25, 39, 57 or 74 (3)) nor does the article deal with other aspects of limitation or prescription such as the causes of an interruption or suspension of the limitation period.

2. The general period of limitation is four years for actions against any party liable on the cheque. This period is, however, extended in those cases where an action may be brought by a party who paid the cheque against a party liable to him.

Example A. A cheque is issued by the drawer to the payee. The payee transfers the cheque to A who transfers it to B. Upon presentment for payment the cheque is dishonoured by the drawee. B, upon protesting the dishonour, exercises his right of recourse against A who pays the cheque. Under article 79 B may exercise his right of recourse on the cheque within four years against (a) the drawer or his guarantor from the date of cheque; (b) an endorser or his guarantor from the date of protest for dishonour or, where protest is dispensed with, the date of dishonour. If B exercises his right of recourse against A within a period of three years, A in turn may exercise his right of recourse within the remaining period of time of four years. However, if B exercises his right of recourse against A after a period of three years has elapsed, A may exercise his right of recourse within a period of one year from the date on which he paid the cheque to B.

Example B. In example A, B exercises his right of recourse against A after three and a half years from the date of protest for dishonour by non-payment. A who pays B may now exercise his right of recourse against the payee within one year from the date he paid the cheque. If A should exercise his right of recourse against the payee after, say, nine months from the date he, A, paid the cheque and the payee should pay, then the payee in turn would have one year from the date he paid the cheque within which he may bring an action on the cheque against the drawer.

3. Article 79 sets forth rules regarding the point of time at which an action on the cheque accrues. The basic rule in this respect is that this point of time is the date on which a party became liable on the cheque. Thus an action

(a) Against the drawer of a cheque accrues on the date of the cheque;

(b) Against parties secondarily liable accrues on the date of protest for dishonour by non-payment or, if protest is dispensed with, the date of dishonour.

7. NOTE BY THE SECRETARIAT: POSSIBLE COURSES OF ACTION CONCERNING THE DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES AND THE DRAFT CONVENTION ON INTERNATIONAL CHEQUES (A/CN.9/223)*

Introduction

1. The United Nations Commission on International Trade Law, at its fourteenth session, requested the Working Group on International Negotiable Instruments to complete expeditiously its work on the preparation of a draft Convention on International Bills of Exchange and International Promissory Notes and on a draft Convention on International Cheques.¹ The Commission further requested the Secretary-General, after the completion of the texts by the Working Group, to circulate them, together with a commentary, to all Governments and interested international organizations for their comments.²

2. The Working Group, at its eleventh session, completed its work and adopted the two draft Conventions, after a Drafting Group had reviewed both drafts and established corresponding language versions (in Chinese, English, French, Russian and Spanish).³ The text of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211)** and the text of the draft Convention on International Cheques (A/CN.9/212)*** were published and distributed in March 1982.

3. The commentary on the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/213),**** which has now been translated, will be circulated at the end of June and the commentary on the draft Convention on International Cheques (A/CN.9/214)***** soon thereafter. In the covering note verbale, Governments and interested international organizations are invited to transmit their comments on the draft Conventions before 16 February 1983.

Discussion at fourteenth session on future course of action

4. The question which exact procedure should be followed after receiving these comments was considered

* 18 June 1982.

** Reproduced in this volume, part two, II, A, 3.

*** Reproduced in this volume, part two, II, A, 5.

**** Reproduced in this volume, part two, II, A, 4.

***** Reproduced in this volume, part two, II, A, 6.

¹ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth session, Supplement No. 17* (A/36/17), para. 22 (2) (Yearbook . . . 1981, part one, A).

² *Ibid.*, para. 22 (5).

³ A/CN.9/210: Report of the Working Group on International Negotiable Instruments on the work of its eleventh session (New York, 3-14 August 1981), paras. 234-241 (reproduced in this volume, part two, II, A, 1).

by the Commission at its fourteenth session; the Commission agreed to defer its decision on this question and to revert to it at its fifteenth session.⁴ In order to facilitate the deliberations and decision at this session, the discussion during the fourteenth session shall be recalled here,⁵ followed by some additional points which the Commission may wish to take into account.

5. During the discussion at the fourteenth session "[d]ifferent views were expressed as to the proper procedure to be followed after the comments were received. Under one view, the comments should be referred for consideration to the Working Group, which should revise the texts, if appropriate, in the light of the comments. Thereafter the revised texts, with a report by the Working Group on the action taken by it, should be submitted to the Commission, and the Commission could thereafter devote some time during a session to examine and approve the texts. In this context, a view was expressed that if the comments were made available to members of the Commission that were not members of the Working Group, before the Working Group commenced the review, it would assist those non-members of the Working Group in assessing the need to send observers to the Working Group session.

6. Under another view, the comments should be referred to the Commission, which should examine the texts in detail in the light of the comments, and revise them as appropriate.

7. In support of the former view it was noted that a revision of the draft texts in the light of the comments received could more expeditiously be undertaken by the Working Group than by the Commission. Furthermore, the prior revision of the texts by the Working Group would considerably expedite the work when the Commission came to consider the texts. It was suggested that a detailed examination of the two texts without such a prior review might result in the Commission having to devote an inordinate length of time to this work because of the highly complex and technical nature of the subjects. Accordingly, thought should be given at least to the advisability of adopting appropriate procedures which would, whilst not affecting the quality of the work, reduce the period of time needed for the conclusion of such a convention or conventions. It was noted that all States were free to attend sessions of the Working Group as observers, and that several States did so attend, and as a result the approval

⁴ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 21 (Yearbook . . . 1981, part one, A).

⁵ *Ibid.*, paras. 17-20.

of the texts by the Working Groups was one whose scope extended beyond the membership of the Working Group. Another suggestion in this context was for an enlargement of the membership of the Working Group for the purposes of revising the texts after the comments had been received.

8. In support of the latter view, it was noted that texts submitted by the Commission to the General Assembly, and later to a Diplomatic Conference, should carry the full approval of the Commission. Such approval could only be secured by a careful examination of the texts by the Commission itself. Furthermore, time would not be saved by a prior revision of the texts by the Working Group in the light of the comments received, as it would be difficult to prevent questions settled by the Working Group from being re-opened during the deliberations of the Commission. It was also observed that, although States not members of the Working Group could attend sessions of the Working Group as observers, many States, particularly the developing States, were unable due to budgetary constraints to send representatives as observers. Moreover, the apprehension that a careful examination of the texts by the Commission might take an inordinate length of time was unjustified."⁶

Further considerations

9. As indicated in the above discussion, one important factor is the amount of time needed for considering in detail the draft Conventions in the light of the comments if

⁶ *Idem*.

that were done by the Commission itself without prior review by the Working Group. In order to determine whether this traditional approach would be feasible, the Commission may wish to consider how much time it would probably have to devote to this work. While an accurate forecast is impossible, it is submitted that at least five weeks will be needed for the consideration of both draft Conventions together.

10. Whether this work could be undertaken during the sixteenth session of the Commission, would in large measure depend on how much time will be needed for all the other items on the agenda of that session, assuming that these items would be considered before or after the review of the draft Conventions but not concurrently. Inclusion of the work on negotiable instruments would appear to be feasible if, as is not unlikely, only one week or at the most two weeks are needed for the other items. Of course, this depends on the decisions which the Commission will take at its fifteenth session in respect of a number of topics.

11. To mention another possibility, the Commission might devote three to four weeks of its sixteenth session to the review of the draft Convention on International Bills of Exchange and International Promissory Notes and then about two weeks of its seventeenth session to the review of the draft Convention on International Cheques. Should this approach be taken, it would seem desirable, in view of the similarity of large parts of both Conventions, to reach an understanding that questions settled at the sixteenth session would not be re-opened at the seventeenth session.

B. Unit of account*

1. REPORT OF THE WORKING GROUP ON INTERNATIONAL NEGOTIABLE INSTRUMENTS ON THE WORK OF ITS TWELFTH SESSION (VIENNA, 4-12 JANUARY 1982) (A/CN.9/215)**

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* For consideration by the Commission see Report, chapter III, B (part one, A, above).
 ** 19 January 1982.

Introduction

1. At its eleventh session the United Nations Commission on International Trade Law adopted the proposal of the delegation of France that the Commission "should study ways of establishing a system for determining a universal unit of constant value which would serve as a point of reference in international [transport and liability] conventions for expressing amounts in monetary terms."¹

2. The proposal was examined by the UNCITRAL Study Group on International Payments at its meetings in 1978, 1979 and 1980. The Study Group was of the view that the most desirable approach was to combine the use of the Special Drawing Right (SDR) with a suitable index which would preserve over time the purchasing power of the monetary values set forth in the international conventions in question.

3. At its fourteenth session the Commission considered a report of the Secretary-General on the subject, (A/CN.9/200)* which reflected the views of the Study Group. The report contained an annex prepared by the staff of the International Monetary Fund at the request of the UNCITRAL Secretariat which discussed issues relating to the choice of an appropriate index to be used in connection with the SDR. It was there suggested that for most purposes a consumer price index would be suitable, but that other indexes could be used if desired. After discussion, the Commission decided to refer the matter to the Working Group on International Negotiable Instruments.²

4. The Working Group was requested to consider various possibilities in regard to the formulation of a unit of account of constant value and to prepare a text, if possible.³

5. The Working Group is currently composed of the following eight States members of the Commission: Chile, Egypt, France, India, Nigeria, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America.

6. The Working Group held its twelfth session at Vienna from 4 to 12 January 1982. All members of the Working Group were represented except Nigeria.

7. The session was attended by observers from the following States members of the Commission: Australia, Austria, Cuba, Czechoslovakia, Germany, Federal Republic of, Japan, Kenya and Spain.

8. The session was also attended by observers from the following States not members of the Commission: Argentina, Bolivia, Brazil, China, Ecuador, Greece, Holy See, Luxembourg, Netherlands, Portugal, Republic of Korea, Romania, Switzerland, Thailand, Tunisia, Turkey, Uruguay and Venezuela.

9. The session was also attended by observers from the following international organizations:

- (a) *Specialized agency*
International Monetary Fund
- (b) *Inter-governmental organizations*
Bank for International Settlements
Office Central des Transports Internationaux par Chemins de Fer
- (c) *Non-governmental organizations*
International Law Association
Union Internationale des Chemins de Fer
Union Internationale des Transports Routiers

10. The Working Group elected the following officers:

Chairman: M. Joë Galby (France)
Rapporteur: Mrs. Malena Saavedra (Chile)

11. The following documents were placed before the Working Group:

- (a) Provisional agenda (A/CN.9/WG.IV/WP.26)
- (b) Report of the Secretary-General entitled "Universal Unit of Account for International Conventions" (A/CN.9/200)*
- (c) Report of the Secretary-General entitled "Unit of Account of Constant Value" (A/CN.9/WG.IV/WP.27). **

12. The Working Group adopted the following agenda:

- (a) Election of officers
- (b) Adoption of the agenda
- (c) Universal unit of account of constant value for use in international conventions
- (d) Other business
- (e) Adoption of the report.

Deliberations and decisions

GENERAL DISCUSSION

13. The Working Group was in agreement that the problems caused by the effects of inflation on the limits of liability in transport and liability conventions were serious. It was noted that a limit of liability which remained fixed over a long period of time often became seriously eroded. The most striking example of the problem was the limit of liability for loss of life in the Warsaw Convention, but the problem was a general one which applied in greater or lesser degree to all such provisions.

14. It was noted that as a result of the erosion of the real value of the maximum compensation which could be recovered under the various limit of liability provisions, the courts in some countries had sought means of avoiding these

* Yearbook ... 1981, part two, II, C.

¹ A/CN.9/156 (Yearbook ... 1978, part two, IV, C); Report of the United Nations Commission on International Trade Law on the Work of its eleventh session, *Official Records of the General Assembly, Thirty-third session, Supplement No. 17* (A/33/17), para. 67 (Yearbook ... 1978, part one, II, A).

² Report of the United Nations Commission on International Trade Law on the Work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth session, Supplement No. 17* (A/36/17), para. 32 (Yearbook ... 1981, part one, A).

³ *Ibid.*

* Yearbook ... 1981, part two, II, C.

** Reproduced in this volume, part two, II, B, 2.

provisions so that larger damages could be awarded. The result was that the uniformity of application of the conventions was compromised. Moreover, the uncertainty as to the maximum amount of damages which the courts might award had led insurance companies to charge premiums commensurate with the increased risk, thereby effectively nullifying one of the main purposes of the provisions.

15. It was also noted that there was the danger that some States might choose not to be a party to a convention rather than be bound by a limit of liability which had become too low through the effect of inflation. The problem existed both for conventions which were in force, but which some States might denounce, as well as for conventions which had not yet come in force. It was noted that the problems might be particularly serious in respect of those conventions not yet in force. As the passage of time made the limit of liability provision increasingly inadequate, the likelihood of the convention receiving sufficient ratifications to come into force was reduced. It was also noted that the revision procedure in a convention did not come into force until the convention itself came into force thereby making it particularly difficult to adjust the limit of liability to the new situation.

16. The Working Group considered the possibility of creating a new unit of account which would be determined and would evolve by reference to the value of a number of goods and services characteristic of international trade. It was suggested that such a unit of account would have a constant value as to those goods and services, thereby reducing or eliminating the consequences of inflation on the limit of liability. Under another view it was thought that there would be difficulties in determining the content of the basket of goods and services and the relative weights to be given the various items which could make the adoption of such a new unit of account undesirable.

17. There was general agreement in the Working Group that in the current monetary environment the universal character of the unit of account might better be attained by using the SDR rather than other units of account in all conventions containing limitation of liability provisions.⁴

18. The Working Group considered possible approaches to deal with the effects of inflation on limits of liability expressed in SDRs.

19. Under one view the best means of increasing a limit of liability which has been eroded by inflation is by a revision conference. Under this view the need to revise the limit of liability is influenced by several factors, of which the general rate of inflation is only one. In addition, it would be necessary to consider the change in value of the particular goods or services for which claims would be made under the convention in question. Furthermore, changes in the

types of merchandise carried by various forms of transportation influenced the amount of the claims, and therefore of the appropriate limits of liability. Under this view only a revision conference could take all of these factors into consideration.

20. Under another view, which agreed in principle with the considerations expressed, such a more comprehensive approach was outside the framework of the agenda but was within the competence of the conventions themselves.

21. It was suggested that the Working Group consider means of facilitating the commencement of the revision process and of the entry into force of the new limit of liability. Under one view a new limit of liability adopted by a qualified majority of two-thirds, three-fourths, or even higher should come into force automatically for all Contracting States after a certain period of time without the need for ratification or further acceptance by the individual Contracting States. Only by this means could there be assurance that the new limit of liability would come into force before it in turn had been eroded by inflation. Furthermore, it was important that only one limit of liability be in force for any one convention at a given time. Under this view those States which could not accept the new limit of liability could denounce the convention.

22. It was noted that the new Convention Relative aux Transports Internationaux Ferroviaires (COTIF), adopted in Berne on 9 May 1980, had a procedure similar to that suggested.

23. Under another view any revision conference, no matter how much it might be facilitated, would necessarily be expensive and problematical as to result. Under this view some form of automatic revision process based on indexation should be sought.

24. The question arose as to whether there should exist only one index to be applied in liability conventions generally, or whether different indexes should be tailored to the different risks and types of damage in particular conventions. According to one view, there should exist only one index, since it would be impractical to have separate indexes for different conventions. A contrary view maintained that separate indexes should be created for limits of liability in conventions dealing with different risks. In this connection the liability limits in conventions dealing with maritime pollution were specifically mentioned.

25. One opinion suggested that a consumer price index be appropriate for use in connection with liability limits in transportation conventions. It was stated to be technically possible to base an index upon the consumer price indexes in the five countries whose currencies comprise the SDR "basket" of currencies. The view was expressed that consumer price indexes had the advantage of being subject to constant scrutiny by the governments which issued them, that they were regularly up-dated, and that published index figures were not later changed.

⁴ For further discussion and the recommendation of the Working Group, see paras. 91 to 97, below.

26. A question arose as to whether an index to be linked with a unit of account could be based upon a basket of primary commodities. It was pointed out that due to the recent wide fluctuations in the prices of primary commodities such an index would be quite unstable. However, it was possible that for a particular convention dealing with particular primary commodities, an index could be based upon a basket of those commodities.

27. It was pointed out that the purpose of a limit of liability provision was to cut down on extreme damage awards; its purpose was not to reduce such awards generally. Limits were supposed to be high enough to compensate for damages incurred by most claimants. The problem was that with inflation, these limits had been reduced in value, effectively denying many claimants full compensation. Adjusting liability limits according to an index would not increase damage awards generally; it would only adjust the upper limits of such awards. Nor would the use of an index change the way in which damages were calculated.

28. Moreover, it was suggested that the absolute amount of the increase in liability limits was not of critical importance. It was more important for those limits to be stable and certain so that carriers could know the upper limit of their liability against which they must insure. Indexation, therefore, should not produce rapidly fluctuating liability limits; the amounts of the limits should be fixed for a certain period of time. It was suggested that if the limits were unstable or ambiguous, shippers would have to over-insure, and the cost of their higher insurance premiums would ultimately be borne by their customers.

29. Various periods of time during which liability limits should be stable were mentioned, the shortest being one year.

30. It was also suggested that a possible method to provide stability in liability limits over a period of time would be for the limit to be adjusted at fixed intervals, but that the adjustment would be made only if a minimum percentage change in the relevant index had occurred. It was noted that this approach was embodied in the sample price index clause in document A/CN.9/WG.IV/WP.27, annex III.*

31. It was pointed out to the Working Group that the use of any indexing system would require an institution to prepare and maintain the index. If required, such an index could be calculated by the IMF as well as by other competent international organizations. It was suggested that, if requested, the IMF might in principle be prepared to calculate such an index.

32. It was noted that any solution to the problems under consideration which might be proposed by the Working Group would, if adopted by the Commission, serve only as a recommendation available for use by organizations drafting or revising conventions containing limitation of liability provisions. These organizations would not be bound to

apply such a recommendation. However, the recommendation could be expected to be influential in the drafting or revision of a convention by other organizations, since it would have emanated from the core legal body of the United Nations in the field of international trade law.

33. It was generally agreed that the Working Group should explore all realistic solutions to the problems under consideration, including indexing, revision processes, and some combination of these approaches, such as using an index to "trigger" a review process.

34. It was suggested that the Working Group might recommend two alternative solutions, since these alternatives could be considered for use by organizations and applied as required by the particular circumstances of the conventions being drafted or revised.

REVISION BY USE OF AN INDEX

35. The Working Group decided to consider the sample price index clause contained in A/CN.9/WG.IV/WP.27, annex III* as a basis for its discussion of revision of liability limits by use of an index. That sample clause is as follows:

"1. The amounts set forth in article [] shall be adjusted effective on the first day of July of each year, commencing on the first day of July [19], by an amount corresponding to the increase or decrease in the [Consumer Price Index in Special Drawing Rights as published by the International Monetary Fund] for the month ending on the last day of the previous December over the same period one year earlier.

"2. The provision in paragraph 1, however, shall not be invoked if the ratio of increase or decrease in the [Consumer Price Index in Special Drawing Rights] over the preceding year does not exceed [15] per cent. Where no adjustment was made in the previous year because the ratio was less than [15] per cent the comparison shall be made with [19] or with the last year on the basis of which an adjustment was made, whichever is later.

"3. By the first day of April of each year the [depository] shall notify each Contracting Party and each State which has signed this [Protocol-Convention] of the amounts to be in force as of the first day of July following, rounded to the nearest number of Special Drawing Rights and monetary units and, after the entry into force of this [Protocol-Convention], the [depository] shall at the same time transmit to the Secretariat of the United Nations a notice of the amounts to be in force as from the first day of July following for registration and publication under Article 102 of the Charter of the United Nations.*

*"It would also be necessary to provide in the final clauses that when the Convention enters into force and the depositary transmits a certified copy of the Convention to the Secretariat of the United Nations for registration and publication under Article 102 of the Charter, he also indicates the amounts then in force under the various articles." (Footnote in original.)

* Reproduced in this volume, part two, II, B, 2.

36. One view considered that the sample provision was in the nature of an automatic adjustment mechanism, and was therefore not a good basis for discussion. According to this view, it should be left for determination in each convention as to the method of dealing with a given increase in inflation, whether these methods involved automatic adjustment, a review conference or some other method.

37. Other views considered that the sample provision presented a reasonable approach for an indexation mechanism were to be proposed by the Working Group. It was pointed out that the sample provision avoided a freely fluctuating index, and therefore provided a measure of stability.

38. With respect to the words "Consumer Price Index in Special Drawing Rights" contained within brackets in paragraphs 1 and 2 of the sample provision, it was stated that consumer price indexes are usually expressed in percentages or points, rather than in monetary units. It was explained that the idea intended to be conveyed by this language was that the index would measure the loss of purchasing power of the SDR. It would be based on the consumer price indexes of the five countries whose currencies comprise the SDR "basket" of currencies, these national indexes being weighted in accordance with the weights given their respective currencies in the SDR basket.

39. It was suggested that the point of reference for the index should be the time when the limits of liability were negotiated, and not when the convention entered into force. In this way the index could take account of the effects of inflation which occurred during the period before the convention came into force, a period which was often from five to ten years.

40. The question was raised as to how the index provision could be in effect prior to the time the entire protocol or convention came into effect. It was suggested that this might be primarily a question of drafting.

41. One view recommended that the minimum increase in inflation which should occur before liability limits could be adjusted should be left for determination in each convention. The 15 per cent suggested in the sample provision should therefore be deleted.

42. It was suggested that in any case this percentage was too low, since some States had inflation rates of more than 15 per cent. According to this opinion, from the point of view of private law, an adjustment of liability limits every year, or even every two years, was too frequent. It was suggested that, in fixing the limit of liability in a convention, a certain degree of inflation should be anticipated. If this were done, it would be possible to require a greater amount of inflation before the limit of liability would be adjusted. It would also be possible to lengthen the interval mentioned in paragraph 2 of the sample provision to two or three years.

43. The suggestion was also made that the time of the first adjustment should be left for determination in each

convention, and should not be generalized as it was in paragraph 1 of the sample provision.

44. The suggestion was made that automatic adjustment of the limit of liability by an index should take place only up to a certain amount. If the increase were higher, the adjustment should be made by a revision conference.

45. According to another view, if an unusually high rate of inflation existed, the index provision would correctly increase the limits of liability by a large amount.

46. It was also suggested that a State which had become a party to a convention containing an index provision would have accepted the principle of indexation and its consequences. If it could not accept the adjustment effected by such a provision, its only alternative should be to denounce the convention.

47. A proposal was made that the limit of liability should be raised only if the rate of inflation as shown by the Index persisted over a period of time. It was suggested that this might be accomplished by requiring that the requisite increase of the index have persisted for each of the last four months of the year over the last four months of the previous relevant year. It was suggested however that it would be better if the figures to be compared were the index for the entire year compared to the index for the previous relevant year.

48. It was suggested that it may be important for some States in deciding whether to ratify a convention or protocol containing such a provision to know what limits of liability would be in effect when the instrument came into force. Therefore, the depositary should perhaps be required to inform States, upon request, what the adjusted amounts would then be. On the other hand it was suggested that the depositary would probably be prepared to do this on an informal basis.

49. The Working Group was of the view that it was preferable to delete any reference to a particular price index and to insert in the brackets in paragraphs 1 and 2 of the sample provision the words "a specific price index which might be considered appropriate for a particular convention".

50. Under one view the word "shall" in the first sentence of paragraph 2 should be replaced by "may". Under this view it should be possible to increase the limits even if the requisite percentage was not met, especially if it was evident that the rate of inflation was increasing.

51. Under another view such a proposal raised questions as to who would exercise the discretion envisaged.

52. It was noted that the reference to rounding the calculation to the nearest whole number did not belong in paragraph 3 but in paragraph 1. It was suggested that after the words "shall be adjusted by an amount" in the first and second sentences of paragraph 1 could be added the words

"rounded to the nearest whole number". This change had the added advantage of deleting any reference to Special Drawing Rights and monetary units from the text. This was particularly useful in the light of the decision of the Working Group to recommend to the Commission that in the future all limit of liability provisions be expressed only in units of account equal to the Special Drawing Right and not in monetary units, as is the current practice.⁵

53. The Working Group requested that a revised version of the sample price index provision be prepared in the light of the discussion. The revised provision is as follows:

"Sample price index Provision"

"1. The amounts set forth in article [] shall be linked to [a specific price index which might be considered appropriate for a particular convention]. On coming into force of this [Protocol-Convention], the amounts set forth in article [] shall be adjusted by an amount, rounded to the nearest whole number, corresponding in percentage to the increase or decrease in the index for the year ending on the last day of December prior to which this [Protocol-Convention] came into force over its level for the year ending on the last day of December [of the year in which the Protocol or Convention was opened for signature]. Thereafter, they shall be adjusted on the first day of July of each year by an amount, rounded to the nearest whole number, corresponding in percentage to the increase or decrease in the level in the index for the year ending on the last day of the previous December over its level for the prior year.

"2. The amounts set forth in article [] shall not, however, be increased or decreased if the ratio of increase or decrease in the index does not exceed [] per cent. Where no adjustment was made in the previous year because the ratio was less than [] per cent, the comparison shall be made with the level for the last year on the basis of which an adjustment was made.

"3. By the first day of April of each year the Depositary shall notify each Contracting Party and each State which has signed this [Protocol-Convention], of the amounts to be in force as of the first day of July following and, after the entry into force of this [Protocol-Convention], the Depositary shall at the same time transmit to the Secretariat of the United Nations a notice of the amounts to be in force as from the first day of July following for registration and publication under Article 102 of the Charter of the United Nations.*

* It would also be necessary to provide in the final clauses that when the Convention enters into force and the Depositary transmits a certified copy of the Convention to the Secretariat of the United Nations for registration and publication under Article 102 of the Charter, he also indicates the amounts then in force under the various articles." (Footnote in original.)

⁵ See paras. 91 to 97, below.

54. The Working Group decided to adopt this text and to recommend it to the Commission as one alternative means of revising limits of liability in conventions.

REVISION BY A COMMITTEE

55. The Working Group considered an expedited revision process as a second alternative method of adjusting limits of liability for inflation or deflation.

56. Several different procedures to initiate the revision process were suggested. A meeting of the Contracting States could be convened if there had been a change in a specified price index of a certain percentage. A second possibility was that the meeting could be convened at regular intervals. A third possibility was that the meeting could be convened upon the request of a stipulated number or percentage of the States parties to the convention.

57. One view suggested that these possibilities could be combined. After the lapse of a certain period of time, or upon the request of one-fourth of the States parties to the convention, the depositary could be required to inquire of all States parties as to whether they deemed it necessary to revise the limits of liability. If the depositary received an affirmative response from more than one-half of the States parties, he would be required to convene a revision conference. It was suggested that inquiry of States parties as to whether they desired a revision conference would avoid the convening of a conference which was unnecessary.

58. Another view suggested that in some instances a revision committee might be preferable to a revision conference. The revision committee could be a representative body made up of a certain number of States parties to the convention which would be able to act more expeditiously and with less formality than a full revision conference composed of all States parties to the convention. It was noted that particularly with respect to conventions to which a large number of States were parties, the convening of a full revision conference would be a substantial undertaking. It was thought not to be feasible to convene such a conference every time liability limits were to be reviewed. Moreover, although the purpose of such a conference would be to revise the limits of liability, it would be difficult to restrict the conference to that issue and to avoid attempts to revise other aspects of the convention.

59. According to yet another view, under a committee procedure every Contracting State should have the opportunity to participate in the meeting in view of the future binding effect of an amendment on all Contracting States.

60. According to one view, the effects of inflation upon liability limits should be dealt with uniformly among all conventions with limitation of liability provisions, and that this uniformity would be difficult to promote if different conventions employed different revision processes. However, a contrary view suggested that it was not neces-

sary for all conventions to react in the same way to a given increase in inflation. Each convention was subject to its own specific circumstances, and it should be able to respond to an increase in inflation in accordance with these circumstances.

61. The Working Group was of the view that any revision should be implemented rapidly, otherwise the new limits could be overtaken by inflation or deflation by the time they entered into force. In this context the Working Group discussed whether revisions adopted by a revision conference or a revision committee should be made binding on all States parties without requiring ratification by them. In this regard, it was pointed out that ratification procedures typically took 5 to 10 years to complete, which made it important to avoid the necessity of ratification.

62. There was general agreement on the principle that States parties to a convention not wishing to accept revised liability limits adopted by a revision conference or a revision committee should be compelled either to accept the new limit or to withdraw from the convention. They should not be permitted to retain the old limits. It was suggested that this rigid approach was necessary to avoid multiple limits of liability within the same convention regime. It was suggested that if a particular revision were adopted by the required majority of States parties, it would be unwise to compromise the principle of uniformity by permitting several liability limits to exist simply for the sake of keeping within the convention regime the small percentage of States parties which chose not to accept the revision.

63. It was suggested that making a revision binding upon all States parties which had not denounced the convention had the additional advantage of easing the role of domestic courts, which would not have to determine whether a particular State party had accepted the revised limits of liability.

64. As one possible approach to these issues, it was suggested that a revision of liability limits accepted by a stipulated majority of States parties could be made binding upon all States parties to the convention after the lapse of a certain period of time, which might be one year. Within a given amount of time prior to the expiration of this period, States parties which could not accept the revised limits could denounce the convention.

65. The Working Group recognized that a procedure whereby an increase or decrease in the limits of liability adopted by a revision conference or revision committee that would come into force for all States at the same time could cause difficulties of a procedural nature for some States. Those States for which treaties are not self-executing might have to implement the increase or decrease in the limit of liability by legislation. If that were the case, a certain period of time would be required. It was also recognized that unexpected events could delay the implementation procedure beyond the normal period of time. It was

stated that the envisaged procedure should not, if possible, lead a State to be in breach of its international obligations.

66. The Working Group requested the Secretariat to prepare a draft text in the light of the discussions, in consultation with interested delegations. The draft text submitted in response to this request is as follows:

"Sample amendment procedure for limit of liability"

"1. The Depositary shall convene a meeting of a Committee composed of a representative from each Contracting State within the first year after the present [Protocol-Convention] comes into force to consider amending the amounts in article []. Thereafter, the Depositary shall convene the Committee

"(a) When a request has been made by at least [] Contracting States, or

"(b) When there has been a change in the [Consumer Price Index published by the International Monetary Fund] of at least [] per cent, provided that at least five years have passed since the Committee last met.

"2. Amendments shall be adopted by the Committee by a [] majority of its members present and voting."

"3. Any amendment adopted in accordance with paragraph 2 of this article shall be notified by the Depositary to all Contracting States. The amendment shall be deemed to have been accepted at the end of a period of [] months after it has been notified, unless within that period not less than [one-third] of the Contracting States have communicated to the Depositary that they were unable to accept the amendment. An amendment deemed to have been accepted in accordance with this paragraph shall enter into force for all Contracting States [] months after its acceptance.

"4. A contracting State which has not accepted an amendment shall nevertheless be bound by it, unless such State denounces the present Convention in accordance with article [] before the amendment has entered into force.

"* The Conference of Plenipotentiaries may wish to insert a list of criteria to be taken into account by the Committee." (Footnote in original.)

67. A question arose concerning the number of States whose objection to an amendment could prevent it from coming into force. According to one view, a minority of States should not be permitted to prevent it from coming into force. It was suggested that the interest of States were sufficiently safeguarded by their being able to present their views at the meeting of the committee to revise the liability limits. If they are unable to accept the revised liability limits they should withdraw from the convention.

68. Under one view a quorum requirement should be established for the meeting of the revision committee to

ensure that a small number of States at such a meeting would not produce a revision of the liability limits which would bind other States parties.

69. Under another view a quorum requirement was not advisable, especially for those conventions to which a large number of States were parties. Many States which did not hold strong views on the question to be submitted to the meeting might not attend, even though they would not be opposed to an increase in the limit of liability.

70. It was suggested that providing a minority of States the means to prevent an amendment from coming into force served as a safeguard for the convention. If a significant minority could block the amendment, they would not be compelled to withdraw from the convention.

71. A question was raised as to whether States voting in favour of an amendment at a meeting of a revision committee should later be able to object to its coming into force. Concern was expressed that States might have become accustomed to traditional procedures, according to which their votes in favour of an instrument were not necessarily binding.

72. According to one view, States voting in favour of an amendment should not be able to object to its coming into force. Another view suggested, however, that particularly if a decision adopting an amendment were taken by a qualified majority, States parties, including those voting in favour, should be able to reflect upon this decision. It was pointed out that the delegate of a State might vote in favour of an amendment as a result of a misunderstanding, perhaps produced by communication difficulties with his home Government.

73. There was general agreement in the Working Group that States voting in favour of an amendment should be able to object to its coming into force.

74. The Working Group agreed to delete from subparagraph (b) of paragraph 1 of the sample procedure the requirement that a meeting be convened upon a given change in the consumer price index. The meeting should be convened on the request of a given number of Contracting States or when a specific time had passed since the committee last met.

75. According to one view, five-year intervals between meetings of the committee were too long. During these intervals the purchasing power of liability limits could erode by as much as 50 per cent. According to another view, five years was adequate, since if States desired a meeting to amend limits sooner, they could request it pursuant to subparagraph (a).

76. It was generally agreed that five-year intervals were sufficient.

77. In connection with paragraph 4 of the sample procedure, it was pointed out that the amended liability limits would not be effective as to States which denounced the

convention. A denunciation might not become effective until after the amended liability limits had come into force; in such a case the denouncing State would remain subject to the old limits until the denunciation took effect.

78. According to one view, because it was undesirable for two limits of liability to exist under a convention, the denunciation of a State party should take effect upon the coming into force of the amendment.

79. According to another view, the existence of two limits in the same convention for a short period of time was not an insurmountable problem. The unamended limits of liability should apply to a State until its denunciation becomes effective.

80. It was pointed out that if a denunciation became effective at the time the amended limits came into force, in many cases the normal denunciation period would be shortened. This could create problems in conventions in which the parties needed time to adjust to the new situation which would exist as a result of the withdrawal of the denouncing party.

81. One solution was to delay the coming into effect of the amended limits until the denunciation of a withdrawing party had become effective. This solution was not generally accepted.

82. Another possible way to deal with this problem and to avoid two limits of liability in the same convention, was to extend the time period for the amended limits to come into effect, and to have a denunciation become effective upon the coming into effect of the amended limits.

83. The Working Group requested that a new draft text be prepared in the light of the discussions. The new draft text is as follows:

"Sample amendment procedure for limit of liability"

"1. The Depositary shall convene a meeting of a Committee composed of a representative from each Contracting State to consider amending the amounts in article []

"(a) Upon the request of at least [] Contracting States, or

"(b) When five years have passed since the Committee last met.

"2. If the present [Protocol-Convention] comes into force more than five years after it was opened for signature, the Depositary shall convene a meeting of the Committee within the first year after it comes into force.

"3. Amendments shall be adopted by the Committee by a [] majority of its members present and voting.*

*"The Conference of Plenipotentiaries may wish to insert a list of criteria to be taken into account by the Committee." (Footnote in original.)

"4. Any amendment adopted in accordance with paragraph 3 of this article shall be notified by the Depositary to all Contracting States. The amendment shall be deemed to have been accepted at the end of a period of [6] months after it has been notified, unless within that period not less than [one-third] of the Contracting States have communicated to the Depositary that they were unable to accept the amendment. An amendment deemed to have been accepted in accordance with this paragraph shall enter into force for all Contracting States [12] months after its acceptance.

"5. A Contracting State which has not accepted an amendment shall nevertheless be bound by it, unless such State denounces the present Convention at least one month before the amendment has entered into force. Such denunciation shall take effect when the amendment enters into force.

"6. A State acceding to this Convention shall be bound by any amendment which has been accepted in accordance with paragraph 4. When an amendment has been adopted by the Committee but the [6] month period for its acceptance has not yet expired, a State acceding to this Convention shall be deemed to have accepted such amendment unless that State declares upon deposit of its instrument of accession with the Depositary that it does not accept it.

84. The opinion was expressed that since the object of this sample procedure was the same as that contained in the Sample Price Index Provision, namely, to adjust liability limits, the sample procedure should refer to "adjustments" rather than to "amendments". This would make it clear that the purpose of the revision was merely to adjust the convention to its original intention. It was suggested that this might eliminate any necessity of submitting a revision of the limits to national parliaments for approval.

85. Another view suggested that the use of the word "adjustment" could wrongly imply that the revision of the limits was based only on a price index. It should be possible to base a revision upon other criteria in addition to an increase in inflation.

86. It was suggested that if the words "increasing or decreasing" were used in paragraph 1, it would make it clear that the purpose of the revision procedure was only to change the limits of liability. In that case the word "amendments" could remain elsewhere in the sample provision, since it would be clear that the amendments referred to were the increases or decreases of the liability limits. This approach was agreed to by the Working Group.

87. With reference to paragraphs 1 (b) and 2, it was pointed out that these provisions did not provide for the first meeting of the Committee if the convention or protocol came into force less than five years after it had been opened for signature. It was therefore agreed to add, in paragraph 1 (b), that a meeting shall be convened five years

after the convention or protocol has been opened for signature.

88. With reference to paragraph 6, it was generally agreed that if a revision had entered into force before a State acceded to the convention, the State should be bound by the revised limits. Moreover, a State which acceded after the revised limits had been accepted but before they had entered into force should also be bound by them when they did enter into force.

89. A question arose as to the position of a State which acceded before the expiration of the six-month period following the adopting of the revised limits by the revision committee, but who lodged an objection to the revised limits during the six-month period. The question was whether such a State should be counted toward the one-third of States parties whose objections would prevent the revised limits from coming into force. It was generally agreed that such a State should not be counted for this purpose. In order to give effect to this understanding it was agreed that the Contracting States which could express their objection under paragraph 4 should only be States which were parties at the time of adoption of the amendment by the committee.

90. The Working Group decided to adopt the following text and to recommend it to the Commission as the other alternative means of revising limit of liability provisions in conventions:

"Sample amendment procedure for limit of liability"

"1. The Depositary shall convene a meeting of a Committee composed of a representative from each Contracting State to consider increasing or decreasing the amounts in article []

"(a) Upon the request of at least [] Contracting States, or

"(b) When five years have passed since the [Protocol-Convention] was opened for signature or since the Committee last met.

"2. If the present [Protocol-Convention] comes into force more than five years after it was opened for signature, the Depositary shall convene a meeting of the Committee within the first year after it comes into force.

"3. Amendments shall be adopted by the Committee by a [] majority of its members present and voting.*

"4. Any amendment adopted in accordance with paragraph 3 of this article shall be notified by the Depositary to all Contracting States. The amendment shall be deemed to have been accepted at the end of a period of [6] months after it has been notified, unless within that period not less than [one-third] of the States that were

* The Conference of Plenipotentiaries may wish to insert a list of criteria to be taken into account by the Committee." (Footnote in original.)

Contracting States at the time of the adoption of the amendment by the Committee have communicated to the Depositary that they do not accept the amendment. An amendment deemed to have been accepted in accordance with this paragraph shall enter into force for all Contracting States [12] months after its acceptance.

"5. A Contracting State which has not accepted an amendment shall nevertheless be bound by it, unless such State denounces the present Convention at least one month before the amendment has entered into force. Such denunciation shall take effect when the amendment enters into force.

"6. When an amendment has been adopted by the Committee but the [6] month period for its acceptance has not yet expired, a State becoming a Party to this Convention during that period shall be bound by the amendment if it comes into force. A State becoming a Party to this Convention after that period shall be bound by any amendment which has been accepted in accordance with paragraph 4.

A UNIVERSAL UNIT OF ACCOUNT FOR LIABILITY CONVENTIONS

91. During its detailed consideration of the draft texts before it, the Working Group returned to the consideration of the use of the SDR as the unit of account in international transport and liability conventions.

92. The delegate of the Soviet Union stated that although the Soviet Union was not a member of the International Monetary Fund and under its law the Special Drawing Right could not be used as a means of payment, the Soviet Union was prepared to agree to the use as a unit of account in international transport and liability conventions of the SDR as calculated by the IMF. It did not insist that these conventions include a separate means of calculating the limit of liability in "monetary units" equivalent to specified quantities of gold, as had previously been the case. In this matter it could not, of course, speak for other States which were also not members of the International Monetary Fund which might wish to continue to calculate the limit of liability in "monetary units".⁶

93. The Working Group welcomed this statement of the delegate from the Soviet Union. It expressed its hope that other States which were not members of the International Monetary Fund would also be able to rely upon the SDR as the unit of account in limit of liability provisions in international conventions.

94. The Working Group noted that under a provision such as article 26, paragraph 1, of the Hamburg Rules,* "The value of a national currency in terms of the Special

Drawing Right of a Contracting State which is not a member of the International Monetary Fund is to be calculated in a manner determined by that State." The Working Group took note of the statement of the observer from Switzerland that Switzerland, which is also not a member of the International Monetary Fund, establishes the value of the Swiss franc in terms of the SDR through a cross-rate with the United States dollar.

95. It was suggested that in future conventions or in revisions of conventions which use a unit of account article in the form of article 26, paragraph 1 of the Hamburg Rules,* the third and fourth sentences might read as follows:

"The value of a national currency, in terms of the Special Drawing Right, of a Contracting State which is a member of the International Monetary Fund is to be calculated in accordance with the method of valuation applied by the International Monetary Fund in effect at the date in question for its operations and transactions. The value of the Special Drawing Right in terms of the national currency of a Contracting State which is not a member of the International Monetary Fund is to be calculated in a manner determined by that State."

It was noted by the delegation that made this suggestion that this change in text, which presented the relationship between the SDR and the national currency in a more logical order for the States not members of the IMF, was not meant to introduce changes in substance but was better suited to the currency regulations of some States which are not members of the IMF.

96. Another formulation of article 26, paragraph 1 which was suggested for consideration was as follows:

"The unit of account referred to in article [] of this Convention is the Special Drawing Right as defined by the International Monetary Fund. The amounts mentioned in article [] are to be expressed in the national currency of a State according to the value of such currency at the date of judgment or the date agreed upon by the parties. The [relationship] [equivalence] between the national currency of a Contracting State which is a member of the International Monetary Fund and the Special Drawing Right is to be calculated in accordance with the method of valuation applied by the International Monetary Fund in effect at the date in question for its operations and transactions. The [relationship] [equivalence] between the national currency of a Contracting State which is not a member of the International Monetary Fund and the Special Drawing Right is to be calculated in a manner determined by that State."

97. The Working Group decided to recommend to the Commission that it recommend that in the preparation of future international conventions containing limitation of liability provisions or in the revision of existing conven-

* Yearbook . . . 1978, part three, I, B.

⁶ Also see the written statement submitted by the delegation of the Soviet Union in the Annex to this report.

* Yearbook . . . 1978, part three, I, B.

tions the unit of account article be substantially in the form of article 26, paragraph 1 of the Hamburg Rules and of paragraph 4 as modified to the extent necessary by the deletions of paragraphs 2 and 3.

CONCLUSION

98. The Working Group thus concluded its deliberations in response to the mandate entrusted to it by the Commission. The conclusions reached by the Working Group are contained in paragraphs 54, 90 and 97. All decisions were taken by consensus.

ANNEX

Statement of the delegation of the Soviet Union*

Guided by the task which the Commission entrusted to this Working Group — namely, "establishing a system for determining a universal unit of constant value which would serve as a point of reference in international [transport and liability] conventions for expressing amounts in monetary terms" — the Soviet Union is prepared to agree to the use for these purposes of the SDR as a unit of account calculated by the International Monetary Fund on the basis of a "basket" of the principal currencies of the capi-

* Original: Russian.

talist countries. The Soviet Union assumes, in this connection, that the limits of liability fixed in these units will, for practical purposes, be converted into the national currencies of the countries participating in the conventions, on the basis of their published currency exchange rates.

In taking this step, the Soviet Union hopes that it will help to eliminate the dualism in the methods of calculating liability under international conventions, a dualism which has persisted until recently since the time when the major capitalist currencies were backed by gold. This step does not imply any change in the Soviet Union's positions *vis-à-vis* IMF, but is an indication of its desire to find constructive approaches to the solution of existing international problems in keeping with the traditions of co-operation which have been established in the climate of international détente. In the view of the Soviet Union, the use of the SDR unit of account to express the limit of liability in international conventions must not encroach on the basic provisions in the currency legislation of those countries which are not members of IMF and which, consequently, do not recognize the SDR as a medium of international payments.

Inasmuch as amounts expressed in SDRs are subject to depreciation under the effect of inflation, the task of maintaining their constant value can, in a more or less satisfactory manner, be solved by indexing these amounts to the current prices of the goods and services characteristic of the kinds of liability in question. The participants in the conventions must themselves determine the representative composition of these "baskets", and the Commission must subsequently ensure that their value is periodically calculated by competent international organizations (e.g. UNCTAD). The indexes obtained in this way may be used under the conventions for the periodic adjustment of the initial amounts of liability.

2. WORKING PAPER SUBMITTED TO THE WORKING GROUP ON INTERNATIONAL NEGOTIABLE INSTRUMENTS AT ITS TWELFTH SESSION (VIENNA, 4-12 JANUARY 1982): REPORT OF THE SECRETARY-GENERAL: UNIT OF ACCOUNT OF CONSTANT VALUE (A/CN.9/WG.IV/WP.27)*

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Introduction

1. At its eleventh session the Commission adopted the proposal of the delegation of France that the Commission "should study ways of establishing a system for determining a universal unit of constant value which would serve as a point of reference in international [transport and liability] conventions for expressing amounts in monetary terms".¹

2. The proposal was examined by the UNCITRAL Study Group on International Payments at its meetings in 1978, 1979 and 1980. The Study Group was of the view that the most desirable approach was to combine the use of the Special Drawing Right (SDR) with a suitable index which would preserve over time the purchasing power of the monetary values set forth in the international conventions in question.

3. At its fourteenth session the Commission had before it a report of the Secretary-General (A/CN.9/200)* which reflected the view of the Study Group. The report contained an annex prepared by the Staff of the International Monetary Fund at the request of the Commission's secretariat which discussed issues relating to the choice of an appropriate index to be used in connection with the SDR. It was there suggested that for most purposes a consumer price index would be suitable, but that other indexes could be used if desired.

4. The Commission at its fourteenth session referred the matter to the Working Group on International Negotiable Instruments.² The Working Group was requested to consider various possibilities in regard to the formulation of a unit of account of constant value and to prepare a text, if possible. The Secretary-General was requested to conduct such studies as seemed desirable in the light of the discussion in the Commission and to submit those studies to the Working Group. This report is submitted in response to that request.

I. SDR as a unit of account

5. The limits of liability in most transport and liability conventions adopted prior to 1975 were expressed in units of account measured in gold. Although a few earlier conventions had mentioned specific national currencies,³ most later conventions defined the unit of account as either 10/31

of a gram of gold of millesimal fineness nine hundred, otherwise known as the germinal franc, or 65.5 milligrams of gold of millesimal fineness nine hundred, otherwise known as the Poincaré franc. In 1975 three protocols were adopted to the Warsaw Convention for the Unification of Certain Rules relating to International Carriage by Air by which the Poincaré franc was replaced as the unit of account by the Special Drawing Right (SDR).⁴ The formula first adopted in Montreal has been modified in several later conventions. The currently standard formulation was first used in the Hamburg Rules.⁵

6. The SDR has been chosen as the unit of account in these conventions primarily because of the stability of its exchange rate. A second important reason has been that the value of the SDR is calculated and published daily by the International Monetary Fund for 43 currencies. The value of any other currency measured in SDR can easily be calculated so long as it has an exchange rate with any one of those 43.

7. However, since the national law of some non-member States of the International Monetary Fund does not permit their use of the SDR, the Hamburg formula also provides a separate rule of calculation for those States. The limit of liability is expressed in "monetary units", which are equivalent to the gold content either of the germinal franc or of the Poincaré franc depending on the convention. Since the original value of the SDR was equal to 0.888 671 grams of fine gold, an amount almost exactly equal to the gold content of three germinal francs or to fifteen Poincaré francs, the limits of liability in the various conventions as expressed in "monetary units" are three or fifteen times those limits as expressed in "units of account", subject to rounding.

8. This coupling of a "monetary unit" expressed in gold

tuted for the pound sterling. By a further Protocol of 21 December 1979 the SDR was substituted for the Poincaré franc.

The limits of liability in the Convention for the Unification of Certain Rules Relating to International Carriage by Air (Warsaw, 12 October 1929) were "deemed to refer to the French franc consisting of 65.5 milligrams of gold of millesimal fineness 900" (art. 22, para. 4). The reference to the "French" franc was removed by a Protocol of 28 September 1955. By Protocols of 25 September 1975 the SDR was substituted for the franc in the Convention, and the Convention as amended.

A more recent liability convention which refers specifically to a national currency in the limit of liability provision is the Vienna Convention on Civil Liability for Nuclear Damage (21 May 1963) which uses the United States dollar. "The United States dollar referred to in this Convention is a unit of account equivalent to the value of the United States dollar in terms of gold on 29 April 1963; that is to say US\$35 per one troy ounce of fine gold." (Art. V, para. 3).

⁴ The three protocols of 25 September 1975 amend the original Convention signed at Warsaw on 12 October 1929, the Convention as amended by the Protocol Done at The Hague on 25 September 1955, and the Convention as amended by the Protocols Done at The Hague on 28 September 1955 and at Guatemala City on 8 March 1971. A fourth protocol adopted on the same date made substantive amendments to the Convention and, at the same time, substituted the SDR for the Poincaré franc.

⁵ United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg, 31 March 1978), art. 26 (Yearbook . . . 1978, part three, I, B). The text of the article is reproduced in annex II to this report.

* Yearbook . . . 1981, part two, II, C.

¹ Official Records of the General Assembly, Thirty-third session, Supplement No. 17 (A/33/17), para. 67 (Yearbook . . . 1978, part one, II, A). The French proposal as contained in A/CN.9/156/Annex is set forth in Annex I to this report.

² Official Records of the General Assembly, Thirty-sixth session, Supplement No. 17 (A/36/17), para. 32 (Yearbook . . . 1981, part one, A).

³ The limits of liability in the International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading (Brussels, 24 August 1924) were expressed in pounds sterling. According to article 9 the monetary unit was "to be taken to be gold value". By a Protocol of 23 February 1968 the Poincaré franc was substi-

with a "unit of account" expressed in SDR has seemed to raise no fundamental objections on the part of the non-member States of the International Monetary Fund. It is, however, a less than completely desirable solution that the limit of liability in the same convention should be expressed in two different units for different States. More important, however, is the fact that the member States of the International Monetary Fund are required to calculate the limit of liability in their national currencies in accordance with the method of valuation of their currencies in terms of the SDR applied by the International Monetary Fund in effect at the date in question. On the other hand, those States for which the limits of liability are expressed in monetary units are required to calculate the limit of liability in their national currency according to the law of the State concerned. In order to achieve a uniform result, the conversion from monetary units is to be made in such a manner as to express in the national currency of the State as far as possible the same real value of the limits of liability as are expressed in units of account measured in SDR. There is no experience as yet whether this admonition will achieve the desired result.

9. The Hamburg formula does not provide a solution for the problem of inflation (or deflation), which has the same type of effect on a basket of currencies such as the SDR as it does on a national currency. The major effort in the diplomatic conferences which have adopted the conventions and protocols using the SDR as the unit of account has been to devise means of expeditiously revising the limit of liability by a revision conference or by other institutional means. These efforts are discussed further below.⁶

II. Possible solutions for the maintenance of real value

A. BASKET OF GOODS AND SERVICES CHARACTERISTIC OF INTERNATIONAL TRADE

10. It is in this context that the delegation of France suggested at the eleventh session of the Commission that UNCITRAL might "explore the possibility of creating a unit which would be determined and would evolve by reference to the value of a number of goods and services characteristic of international trade".⁷ In discussing the proposal this report is limited to a consideration of some of the institutional consequences of creating such a unit of account for transport and liability conventions. It does not attempt to suggest what might be the content of the basket itself.

11. The use of an appropriate basket of goods and services as the unit of account in international transport and

liability conventions would overcome the two objections raised to the use of the SDR. In a period of inflation the limit of liability, as measured by the national currencies in which payment for damages would eventually be made, would automatically increase and there would be no political, though there might be economic, reasons for any State not to apply the unit of account.

12. The composition of the basket to be used as the unit of account should be such that an increase in loss in monetary terms suffered by a claimant due to inflation would be matched by an increase in the limit of liability. Ideally, the basket should match the characteristics of the type of damage for which compensation would be claimed. Ultimately, this would call for a separate basket of goods and services for each convention since there are important differences in the nature of the losses which are suffered under them. These losses include death or bodily injury to individuals, loss or damage to their luggage, loss or destruction of goods carried as freight by sea, air, rail, road and inland waterways, and damage to shore lines, fisheries and the like from oil pollution.⁸ No single basket of goods and services could be fully appropriate for all these purposes.

13. This degree of precision, however, may not be necessary. A limit of liability in a convention is chosen in the first instance through a process which does not admit of fine calculations. The purpose of a unit of account of constant value would be to ensure that the real value of the limit of liability remained approximately the same as originally agreed. Therefore, it would be reasonable to expect that one, or no more than two or three, baskets of goods and services would adequately serve the purposes for all the conventions in question.

14. Nevertheless, the choice of the goods and services to be included and the weights to be given to each would lead to significant differences in the result over an extended period of time. Moreover, the changing character of international trade would suggest that a mechanism would be necessary to substitute from time to time different goods or services for those in the basket as originally calculated or to change their weights. Therefore, the services of a technically qualified international statistical or economic organization would be necessary to suggest the content of the original basket or baskets, to suggest revisions of the content as needed, and to calculate the value of the basket or baskets at the periodic intervals called for in the unit of account provision.

15. It would be possible that the organization so charged would be given the authority to construct, calculate and revise the basket under criteria set forth in the unit of account provision. More likely, however, that organiza-

⁶ See paras. 27 to 40.

⁷ See annex I.

⁸ A list of transport and liability conventions in which the SDR has been adopted as the unit of account is contained in annex VI.

tion would report to some other political or legal entity which would make the final decision.

16. The value of the basket as calculated would have to be available to its ultimate users throughout the world. This suggests that arrangements would have to be made for its prompt publication in a suitable manner by an appropriate international body.

17. The value of the basket of goods and services would ultimately have to be calculated in some monetary unit or unit of account for monetary purposes. That monetary unit or unit of account could be a national currency widely used in international trade. However, that would leave the unit of account in question subject to the exchange fluctuations of the currency chosen. Therefore, it would be preferable that a basket of currencies such as the SDR be used as the basis for calculation. If the value of the basket of goods and services were published as a ratio of the current value to that of some fixed earlier date, it would serve as an index which could be applied directly to the limits of liability.

B. SDR WITH PERIODIC ADJUSTMENTS TO THE LIMIT OF LIABILITY

1. Use of index clause

18. The report submitted by the Secretary-General to the fourteenth session of the Commission suggested that the best available method for creating a unit of account of constant value was to combine the use of the SDR with a suitable price index linked to the SDR.⁹ The report contained an annex prepared by the staff of the International Monetary Fund in which it was stated that:

"If the SDR in conjunction with a suitable SDR price index were chosen as a unit of account for use in international conventions, the data needed for calculating monthly values of the index, as well as monthly exchange rates between the SDR and the currencies of IMF member countries (and of some non-member countries) would be available in the monthly IMF publication *International Financial Statistics*. Moreover, there would in principle appear to be no obstacle to calculation of the monthly price index by the IMF staff, with a delay of no more than three months."¹⁰

19. In the annex were discussed a number of the factors to be considered in the creation of such an index. It was suggested that for most purposes a consumer price index would be suitable. It was recognized, however, that it would be possible to specify any of a number of other price indexes — producer prices, export prices, GNP deflators etc. — if that were found to be preferable. As to the country composition of the index, the annex stated that it would be best to combine the national price indexes of the

countries whose currencies were contained in the SDR currency basket with weights corresponding to the currency composition of the basket.

20. This proposal would combine the relative stability of the SDR, a mechanism for adjusting the limit of liability in order to maintain its real value, the agreement of a technically qualified organization to undertake the necessary calculations, and a means of publishing the results.

21. To this proposal the objection was raised in the Commission that indexing contributed to inflation.¹¹ If indexing were generalized throughout the economy, a rise in prices would automatically increase various monetary obligations, such as wages, rents and pensions, bringing about added costs and further inflation.

22. The objection to indexing as stated in the Commission was not an objection to an increase in the limit of liability. Indeed, it was recognized that the limits of liability must be increased periodically in a period of inflation.¹² The objection to indexing lies in the direct link between the increase in prices which has already occurred and the consequent increase in costs which occurs as a result of the use of the index. It is feared that once the inflationary process begins, there is no possibility of breaking the circle.

23. It would appear that the use of an index in connection with a limit of liability provision in a transport or liability convention would not have the same degree of inflationary effect. The monetary obligation that arises out of these conventions exists only to the extent that damage has occurred of the nature described in the convention. If the limit of liability is at an appropriate level, some of the claims to be paid would be of a lesser sum. Therefore, an increase in the limit of liability of a certain percentage could be expected to lead to an increase in the total amount of claims paid, and of the insurance premium, of a smaller percentage.

24. Nevertheless, if the objections to the automatic adjustment of the limit of liability through the use of an SDR price index are thought to outweigh its advantages, a less automatic formula could also be considered.

25. For example, the depositary of a convention could periodically notify all Contracting States of the new limit of liability by use of the index. This new limit of liability might go into effect six months later in the absence of veto by one third of the Contracting States.¹³

26. A variation of the above procedure would be that the limit of liability might be increased only if the index

¹¹ *Official Records of the General Assembly, Thirty-sixth session, Supplement No. 17 (A/36/17)*, para. 28 (Yearbook . . . 1981, part one, A).

¹² *Ibid.*, para. 27.

¹³ See paras. 36-40, below, for similar rules in respect of an amendment proposed by a revision conference. Of particular importance is the effect on a Contracting State of an increase which has entered into force even though that State has objected to the increase.

⁹ A/CN.9/200 (Yearbook . . . 1981, part two, II, C).

¹⁰ *Ibid.*, annex I, p. 6.

increased by a certain percentage. This would adjust the frequency of revision to the rate of inflation. Combining these two variations, the adjustment in the limit of liability would be made periodically, but only if the index had increased by the requisite percentage.¹⁴

2. Revision conference

(a) General remarks

27. The view was expressed at the fourteenth session of the Commission that it was preferable to adjust the limits of liability through a revision conference. In addition to the arguments advanced against the use of an index, it was stated that "the erosion of currencies was not the only reason for changing the limit of liability. Technical changes, such as a change in the nature of the cargo carried, might also justify a change in the limit of liability. These factors could only be taken into account by a revision conference".¹⁵

28. On the other hand, the view was expressed that "recent experience had shown such rapid generalized inflation that a revision conference would need to be held at least every five years for each convention in question if the limits of liability were not to deteriorate excessively".¹⁶

29. Experience has shown that the traditional procedures used to amend a convention, which include a diplomatic conference and the acceptance of the protocol of amendment by a high percentage of the Contracting States, at which time it enters into force only for those States, is usually time-consuming, costly and problematical as to its results. As conventions have become more technical in their concerns and as the need for complete uniformity of text among the Contracting States has become of greater importance, a number of special procedures have been developed to facilitate the process of amending a convention and to apply the amendment to all Contracting States.

30. These special procedures have concentrated on two aspects, the actions necessary for the revision process to commence and the actions necessary for the proposed amendments to go into force.

(b) Convening of the conference

31. A number of conventions which anticipate future amendments to various provisions have provided that a revision conference should be convened on the request of not less than one-third of all Contracting States.¹⁷ The Ham-

burg Rules provide, however, that the request of only one-fourth of the Contracting States is necessary to convene a conference to revise the limit of liability or the unit of account.¹⁸

32. A variant of this procedure is to be found in the CVN, the CLN, the CMR, the CVR and in the four protocols to these conventions by which the SDR was substituted as the unit of account in place of the germinal franc.¹⁹ After the convention or protocol has been in force for three years any Contracting State may request the depositary to convene a revision conference. The conference will be convened if, within four months after the depositary has notified the other Contracting States of the request, not less than one-fourth of them notify the depositary of their concurrence with the request. By this rule the action of only one Contracting State is necessary to cause the procedure to commence officially and the four month deadline undoubtedly causes some pressure on the other Contracting States to react to the proposal.

33. A procedure which is available in the case of some conventions is illustrated by the Convention Relative aux Transports Internationaux Ferroviaires (COTIF) (Berne, 9 May 1980). According to this Convention, which is the most recent one governing international rail traffic in Europe and the Middle East, a Revision Commission was created to decide on proposals for amending the majority of the substantive rules for the international carriage by rail of passengers and their luggage (CIV) (annex A to the Convention) and for the international carriage by rail of goods (CIM) (annex B to the Convention), including an increase in the limits of liability.²⁰ The Revision Commission can be convened by the Office Centrale des Transports Ferroviaires on its own initiative or at the request of five States.* To the extent that the Revision Commission can propose amendments to the substantive rules contained in the annexes to the Convention, which are then submitted directly to the Contracting States for approval, the Commission serves the same role as would a diplomatic conference.

34. Even though the procedure in COTIF relies upon the existence of a permanent Revision Commission in the framework of an international organization, a similar pro-

* This sentence has been corrected from the original report.

¹⁴ Art. 33 reproduced in annex IV of this report.

¹⁵ See annex III.

¹⁶ *Official Records of the General Assembly, Thirty-sixth session, Supplement No. 17 (A/36/17)*, para. 28 (Yearbook . . . 1981, part one, A).

¹⁷ *Ibid.*, para. 30.

¹⁸ Hamburg Rules, art. 32 (Yearbook . . . 1978, part three, I, B); United Nations Convention on International Multimodal Transport 1980, art. 39 (Final Act of the United Nations Conference on a Convention on International Multimodal Transport and Convention on International Multimodal Transport of Goods, TD/MT/CONF/17, 1981).

¹⁹ Convention on the Contract for the International Carriage of Passengers and Luggage by Inland Waterway (CVN) (Geneva, 6 February 1976) and the Protocol of 5 July 1978; Convention Relating to the Limitation of the Liability of Owners of Inland Navigation Vessels (CLN) (Geneva, 1 March 1973) and the Protocol of 5 July 1978; Convention on the Contract for the International Carriage of Goods by Road (CMR) (Geneva, 19 May 1956) and the Protocol of 5 July 1978; Convention on the Contract for International Carriage of Passengers and Luggage by Road (CVR) (Geneva, 1 March 1973) and the Protocol of 5 July 1978.

²⁰ The Revision Commission is created by art. 8. Its competence to review proposed amendments to the annexes is set forth in art. 19, para. 3. The procedure to be followed is set forth in art. 21. See para. 40, below.

vision could be envisaged for any convention. For example, in the Convention on Civil Liability for Oil Pollution Damage Resulting from Exploration for and Exploitation of Seabed Mineral Resources (London, 1 May 1977), a Committee composed of a representative of each Contracting State was established to consider the limits of liability and extent of required insurance as set forth in that convention and to make recommendations to the Contracting States as to any amendments in those amounts.²¹ As in COTIF only one Contracting State need request that the Committee be convened to consider amendments to these amounts. It is to be expected that a Contracting State would feel less hesitant to convene a meeting of a committee to consider such an amendment than it would to convene a diplomatic conference to do so, even if the membership of the committee was identical to the expected participation in the conference.

35. In addition to these procedures which have already been adopted in various conventions, it would be possible to use an index to cause the revision process to commence. For example, if an appropriate SDR price index increased by a certain percentage, a revision conference might be convened by the depositary. Alternatively, if a given index rose above a certain percentage, a revision conference might be convened on the request of one Contracting State, or of some other similarly small number. For this purpose, the nature of the index chosen may not be of vital importance since it would serve only as a device to authorize a State to request that the revision conference be convened. One suggestion would be that if the cost of living index of three of the five States whose currencies enter into the SDR basket were to rise by more than 25 per cent, a revision conference could be convened on the request of one State. Other possibilities could also be envisaged.

(c) *Entering into force*

36. The most difficult procedural problem to be faced in amending a convention is to decide on the actions necessary for an amendment to enter into force after it has been adopted by a revision conference or by a revision commission, and to decide on its applicability to those Contracting States to the original convention which have not accepted the amendment. The traditional rule that the amendment enters into force only on its positive acceptance by a certain number of States and only as to those States which have so accepted it can lead to the situation faced in the Warsaw Convention where three separate limits of liability are in force between different pairs of States.

37. The minimal change from traditional practice is that the original convention provides for the number of acceptances necessary for an amendment to enter into force. The Hamburg Rules provide, for example, that an

amendment of the limit of liability or of the unit of account enters into force one year following its acceptance by two-thirds of the Contracting States.²² In a departure from traditional practice, after the amendment has entered into force, a Contracting State which has accepted the amendment is entitled to apply the Convention as amended in its relations with all Contracting States which have not within six months after the adoption of the amendment notified the depositary that they are not bound by the amendment. This procedure, however, still leaves the possibility that two different limits of liability might be in force under the convention.

38. The Convention on Civil Liability for Oil Pollution Damage Resulting from Exploration for and Exploitation of Seabed Mineral Resources (London, 1 May 1977) goes beyond the Hamburg Rules. If three-fourths of the representatives of the Contracting States in the Committee formed for the purpose of considering proposals to amend the limit of liability vote in favour of an amendment, it enters into force seven months after it has been notified to the Contracting States without the need for any positive act of acceptance.²³ However, the old limit of liability remains in force for any Contracting State which within six months notifies the depositary Government that it is unable to accept the recommended amount.

39. This Convention is also interesting because it is the only one to indicate factors which should be taken into account by the Committee in making its recommendation on a new limit of liability. Those factors are:

“(a) Any information concerning events causing or likely to cause pollution damage having a bearing on the objects of this Convention;

“(b) Any information on increases and decreases occurring after the entry into force of this Convention in the costs of goods and services of the kinds involved in the treatment and remedying of marine oil spillages;

“(c) The availability of reliable insurance cover against the risk of liability for pollution damage.”²⁴

40. The most far-reaching provision of all is to be found in COTIF. An amendment decided upon by the Revision Commission enters into force for all Contracting States on the first day of the twelfth month after it was sent to them unless one-third of the Contracting States have objected within the first four months after the amendment was sent.²⁵ However, if a State objects within the four months period and also denounces the Convention at least two months before the amendment is to enter into force, the amendment enters into force only at the time the denunciation of the Convention by that State takes effect.

²² Article 33 (Yearbook . . . 1978, part three, I, B).

²³ Article 9, paras. 3 and 4.

²⁴ Art. 9, para. 2.

²⁵ Art. 21, See para. 33, above.

²¹ Article 9, reproduced in annex V of this report.

3. Relationship between unit of account and monetary unit

41. The Hamburg formula accepts the necessity, for those non-member States of the International Monetary Fund whose national law does not permit the use of the SDR, of calculating the limit of liability in a monetary unit in the ratio of one unit of account measured in SDR to three monetary units measured in germinal francs (10/31 of a gram of gold of millesimal fineness nine hundred) or to fifteen monetary units measured in Poincaré francs (sixty-five and one half milligrams of gold of millesimal fineness nine hundred). Therefore, whatever the procedure chosen for an increase in the limit of liability, it should be such as to preserve that ratio.

42. To this end, *inter alia*, the Contracting States which avail themselves of the possibility of applying the limit of liability in monetary units should be required to communicate to the depositary the manner of calculation of the conversion from monetary units to the national currency of that State, but they should not be required to communicate the result of that calculation.²⁶ With this change an increase in the limit of liability in units of account and in monetary units would automatically increase the limit of liability in the national currency of all Contracting States by a uniform percentage.

Conclusion

43. The erosion of the purchasing value of the maximum compensation recoverable under conversions which specify a limit of liability is a serious problem and means should be found at least to assure periodic increases in the liability as necessary.

44. At the present time there appears to be no preferable alternative to the use of the SDR as the unit of account for expressing the limit of liability in international conventions. The creation of a new unit of account would entail serious institutional difficulties.

45. Technically, the best method available for the purpose of maintaining the real value as regards the limit of liability is to combine the use of the SDR with a suitable price index linked to the SDR. However, if the objections to the automatic adjustment of the limit of liability through the use of an SDR price index are thought to outweigh its advantages, less automatic procedures can be envisaged

²⁶ For example, when Czechoslovakia signed the Hamburg Rules on 6 March 1979, it declared, in conformity with article 26, that the conversion of the amounts of the limit of liability into the Czechoslovak koruna (Kčs) to one monetary unit, and that "the limits of liability provided for in this Convention to be applied in the territory of the Czechoslovak Socialist Republic are fixed as follows:

6,000. - Kčs per package or other shipping unit, or
18. - Kčs per kilogram of gross weight of the goods."

An increase of the limit of liability as expressed in units of account or monetary units would not, therefore, automatically increase the limit of liability in Czechoslovak koruna as it would in currencies of member States of the International Monetary Fund.

whereby a certain increase in the index or passage of a certain period of time would cause the procedure for increasing the limit of liability to commence.

46. If it is considered that on balance it is preferable for the limit of liability to be increased through a revision conference, or through a revision committee, various steps can be taken to facilitate the convening of the conference or commission and to bring into force the amendments adopted by it.

47. The Working Group might wish to consider these suggestions and decide whether any of them should be recommended to the Commission. The Working Group might also wish to consider whether the suggestions to be recommended to the Commission should be in the form of a draft text and, if so, whether it would wish to commence the preparation of such a text at this session of the Working Group.

ANNEX I

Proposal by France for the Programme of Work of the Commission made at its Eleventh Session (1978)

(A/CN.9/156, annex)*

At the recent United Nations Conference on the Carriage of Goods by Sea, the question of determining a unit of account which would enable the amounts fixed by the Convention on the Carriage of Goods by Sea to be expressed in national currencies was raised once again.

The abandonment of the reference to gold in transactions between monetary authorities in 1968 and the discontinuance of the convertibility of the dollar into gold in 1971 spelled the end of the system of reference to gold which had been used for decades in international conventions on carriage and liability, whether in the form of the so-called germinal franc (10/31 milligrams of gold of millesimal fineness nine hundred), used principally in conventions on carriage by rail, road and inland waterway, the Poincaré franc (65.5 milligrams of gold of millesimal fineness nine hundred), used mainly in conventions on carriage by air or sea, or the E.M.A. unit (0.88867088 milligrams of fine gold) of the European Monetary Agreement and the Paris Convention on Civil Liability in the field of Nuclear Energy.

The most recent conventions have used the International Monetary Fund unit known as "special drawing rights" (SDR). This is only a temporary solution, however, for SDRs, which are made up essentially of a "basket" of currencies, do not guarantee a constant real value. Above all, they pose very serious problems for countries which are not members of IMF, for whom a different system must be established. This difficulty now arises each time a unit of value has to be expressed in an international convention, and none of the solutions proposed so far, however ingenious, has been completely acceptable to everyone.**

The French Government suggests that, as part of its long-term programme of work, UNCITRAL should study ways of establishing a system for determining a universal unit of constant value which would serve as a point of reference in international conventions for

* As a document of the eleventh session of the Commission it was also reproduced in Yearbook . . . 1978, part two, IV, C.

** On this point, see document A/CONF.89/C.1/L.109 of the United Nations Conference on the Carriage of Goods by Sea. (Footnote in original.) (Official Records, A/CONF.89/14, part one, E, ANNEX.)

expressing amounts in monetary terms. UNCITRAL could, for instance, explore the possibility of creating a unit which would be determined and would evolve by reference to the value of a number of goods and services characteristic of international trade.

ANNEX II

Hamburg Rules*

Unit of account

Article 26.—1. The unit of account referred to in article 6 of this Convention is the Special Drawing Right as defined by the International Monetary Fund. The amounts mentioned in article 6 are to be converted into the national currency of a State according to the value of such currency at the date of judgement or the date agreed upon by the parties. The value of a national currency, in terms of the Special Drawing Right, of a Contracting State which is a member of the International Monetary Fund is to be calculated in accordance with the method of valuation applied by the International Monetary Fund in effect at the date in question for its operations and transactions. The value of a national currency in terms of the Special Drawing Right of a Contracting State which is not a member of the International Monetary Fund is to be calculated in a manner determined by that State.

2. Nevertheless, those States which are not members of the International Monetary Fund and whose law does not permit the application of the provisions of paragraph 1 of this article may, at the time of signature, or at the time of ratification, acceptance, approval or accession or at any time thereafter, declare that the limits of liability provided for in this Convention to be applied in their territories shall be fixed as:

- 12,500 monetary units per package or other shipping unit or
- 37.5 monetary units per kilogram of gross weight of the goods.

3. The monetary unit referred to in paragraph 2 of this article corresponds to sixty-five and a half milligrams of gold of millesimal fineness nine hundred. The conversion of the amounts referred to in paragraph 2 into the national currency is to be made according to the law of the State concerned.

4. The calculation mentioned in the last sentence of paragraph 1 and the conversion mentioned in paragraph 3 of this article is to be made in such a manner as to express in the national currency of the Contracting State as far as possible the same real value for the amounts in article 6 as is expressed there in units of account. Contracting States must communicate to the depositary the manner of calculation pursuant to paragraph 1 of this article, or the result of the conversion mentioned in paragraph 3 of this article, as the case may be, at the time of signature or when depositing their instruments of ratification, acceptance, approval or accession, or when availing themselves of the option provided for in paragraph 2 of this article and whenever there is a change in the manner of such calculation or in the result of such conversion.

ANNEX III

Sample SDR price index provision

1. The amounts set forth in article [] shall be adjusted effective on the first day of July of each year, commencing on the first day of July [19], by an amount corresponding to the increase or decrease in the [Consumer Price Index in Special Drawing Rights as published by the International Monetary Fund] for the month ending on the last day of the previous December over the same period one year earlier.

2. The provision in paragraph 1, however, shall not be invoked if the ratio of increase or decrease in the [Consumer Price Index in Special Drawing Rights] over the preceding year does not exceed

[15] per cent. Where no adjustment was made in the previous year because the ratio was less than [15] per cent the comparison shall be made with [19] or with the last year on the basis of which an adjustment was made, whichever is later.

3. By the first day of April of each year the [depositary] shall notify each Contracting Party and each State which has signed this [Convention-Protocol] of the amounts to be in force as of the first day of July following, rounded to the nearest number of Special Drawing Rights and monetary units and, after the entry into force of this [Convention-Protocol], the [depositary] shall at the same time transmit to the Secretariat of the United Nations a notice of the amounts to be in force as from the first day of July following for registration and publication under Article 102 of the Charter of the United Nations.*

ANNEX IV

Hamburg Rules**

Revision of the limitation amounts and unit of account or monetary unit

Article 33.—1. Notwithstanding the provisions of article 32, a conference only for the purpose of altering the amount specified in article 6 and paragraph 2 of article 26, or of substituting either or both of the units defined in paragraphs 1 and 3 of article 2 by other units is to be convened by the depositary in accordance with paragraph 2 of this article. An alteration of the amounts shall be made only because of a significant change in their real value.

2. A revision conference is to be convened by the depositary when not less than one-fourth of the Contracting States so request.

3. Any decision by the conference must be taken by a two-thirds majority of the participating States. The amendment is communicated by the depositary to all the Contracting States for acceptance and to all the States signatories of the Convention for information.

4. Any amendment adopted enters into force on the first day of the month following one year after its acceptance by two-thirds of the Contracting States. Acceptance is to be effected by the deposit of a formal instrument to that effect, with the depositary.

5. After entry into force of an amendment a Contracting State which has accepted the amendment is entitled to apply the Convention as amended in its relations with Contracting States which have not within six months after the adoption of the amendment notified the depositary that they are not bound by the amendment.

6. Any instrument of ratification, acceptance, approval or accession deposited after the entry into force of an amendment to this Convention, is deemed to apply to the Convention as amended.

ANNEX V

Convention on Civil Liability for Oil Pollution Damage Resulting from Exploration for and Exploitation of Seabed Mineral Resources

Article 9.—1. A Committee composed of a representative of each State Party is hereby established.

2. If a State Party considers that any of the amounts currently applicable under Article 6 or 8 is no longer adequate, or is otherwise unrealistic, it may convene a meeting of the Committee to consider the matter. States which have signed this Convention but are not yet

* It would also be necessary to provide in the final clauses that when the Convention enters into force and the depositary transmits a certified copy of the Convention to the Secretariat of the United Nations for registration and publication under Article 102 of the Charter, he also indicates the amounts then in force under the various articles (Footnote in original.)

** Yearbook . . . 1978, part three, I, B.

* Yearbook . . . 1978, part three, I, B.

Parties will be invited to participate in the work of the Committee as observers. The Committee may recommend to the States Parties an amendment to any of the amounts if representatives of at least three-quarters of the States Parties to this Convention vote in favour of such a recommendation. In making such a recommendation, the Committee shall take into account:

(a) Any information concerning events causing or likely to cause pollution damage having a bearing on the objects of this Convention;

(b) Any information on increases and decreases occurring after the entry into force of this Convention in the costs of goods and services of the kinds involved in the treatment and remedying of marine oil spillages;

(c) The availability of reliable insurance cover against the risk of liability for pollution damage.

3. Any amount recommended in accordance with paragraph 2 of this Article shall be notified by the depositary Government to all States Parties. It shall replace the amount currently applicable thirty days after its acceptance by all States Parties. A State Party which has not, within six months of such notification or such other period as has been specified in the recommendation, notified the depositary Government that it is unable to accept the recommended amount, shall be deemed to have accepted it.

4. If the recommended amount has not been accepted by all States Parties within six months, or such other period as has been specified in the recommendation, after it has been notified by the depositary Government it shall, thirty days thereafter, replace the amount currently applicable as between those States Parties which have accepted it. Any other State Party may subsequently accept the recommended amount which shall become applicable to it thirty days thereafter.

5. A State acceding to this Convention shall be bound by any recommendation of the Committee which has been unanimously accepted by States Parties. Where a recommendation has not been so accepted, an acceding State shall be deemed to have accepted it unless, at the time of its accession, that State notifies the depositary Government that it does not accept such a recommendation.

ANNEX VI

Transport and Liability Conventions and Protocols to such Conventions which use the SDR for the Unit of Account*

Conventions

Convention on Limitation of Liability for Maritime Claims, London, 19 November 1976

European Convention on Products Liability in Regard to Personal Injury and Death, Strasbourg, 27 January 1977

Convention on Civil Liability for Oil Pollution Damage Resulting from Exploration for and Exploitation of Seabed Mineral Resources, London, 1 May 1977

* The listing contains the conventions and protocols of which the Secretariat of the Commission is aware and has a copy. It does not purport to be definitive. (Footnote in original.)

United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules), Hamburg, 31 March 1978*

Convention Relative aux Transports Internationaux Ferroviaires (COTIF), Berne, 9 May 1980

United Nations Convention on International Multimodal Transport of Goods, Geneva, 24 May 1980**

Protocols

Additional Protocol No. 1 to Amend the Convention for the Unification of Certain Rules Relating to International Carriage by Air Signed at Warsaw on 12 October 1929, Montreal, 25 September 1975 (Protocols No. 2 and 3 introduced the SDR as the unit of account into the Convention as amended by the Protocol done at The Hague on 28 September 1955 and into the Convention as amended by the Protocols done at The Hague on 28 September 1955 and at Guatemala City on 8 March 1971. Protocol No. 4 made substantive amendments to the Convention as amended by the Protocol done at The Hague and also introduced the use of the SDR.)

Protocol to the International Convention on Civil Liability for Oil Pollution Damage, 1969, London, 19 November 1976

Protocol to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971, London, 19 November 1976

Protocol to the Athens Convention Relating to the Carriage of Passengers and their Luggage by Sea, 1974, London, 19 November 1976

Protocol to the Convention on the Contract for the International Carriage of Passengers and Luggage by Inland Waterway (CVN), Geneva, 5 July 1978

Protocol to the Convention Relating to the Limitation of the Liability of Owners of Inland Navigation Vessels (CLN), Geneva, 5 July 1978

Protocol to the Convention on the Contract for the International Carriage of Goods by Road (CMR), Geneva, 5 July 1978

Protocol to the Convention on the Contract for the International Carriage of Passengers and Luggage by Road (CVR), Geneva, 5 July 1978

Protocol to Amend the Convention on Damage Caused by Foreign Aircraft to Third Parties on the Surface Signed at Rome on 7 October 1952, Montreal, 23 September 1978

Protocol Amending the International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading, 25 August 1924 as Amended by the Protocol of 23 February 1968, Brussels, 21 December 1979

Protocol Amending the International Convention Relating to the Limitation of Liability of Owners of Sea-Going Ships dated 10 October 1957, Brussels, 21 December 1979

* Yearbook... 1978, part three, I, B.

** Final Act of the United Nations Conference on a Convention on International Multimodal Transport and Convention on International Multimodal Transport of Goods, TD/MT/CONF/17, 1981.

3. NOTE BY THE SECRETARIAT: UNIVERSAL UNIT OF ACCOUNT FOR INTERNATIONAL PAYMENTS (A/CN.9/220)*

1. The report of the Working Group on International Negotiable Instruments on the work of its twelfth session, at which the subject of a universal unit of account of con-

stant value for use in international conventions was considered (A/CN.9/215),* is before the Commission at this session. The background for the action on this subject is

* 18 May 1982.

* Reproduced in this volume, part two, II, B, 1.

described in paragraphs 1 to 4 of the Working Group's report. This note is intended to make certain suggestions in respect of the recommendations of the Working Group.

Two alternative means of adjusting for inflation

2. In conformity with the request of the Commission the Working Group prepared and recommended to the Commission two texts which provide alternative means for adjusting the limits of liability in a transport or liability convention for the effects of inflation. The first of these two alternatives, found in paragraph 53 of the report, is a sample price index provision. The second, in paragraph 90, provides for an expedited revision process for the limited purpose of revising the limits of liability.

3. Following the meeting of the Working Group the UNCITRAL Secretariat requested the comments of the Treaty Section of the Office of Legal Affairs, the office which exercises the responsibilities of the Secretary-General as the depositary of certain international conventions and for the registration of other international conventions under Article 102 of the Charter of the United Nations. The Treaty Section made several drafting suggestions based upon its experience.

4. It recommended that paragraph 3 of the sample price index provision in paragraph 53 of the report be changed to read as follows:

"3. By the first day of April of each year the Depositary shall notify each Contracting State and each State which has signed the [Protocol-Convention] of the amounts to be in force as of the first day of July following. Changes in the amounts shall be registered with the Secretariat of the United Nations in accordance with General Assembly regulations to give effect to Article 102 of the Charter of the United Nations."

The suggested wording is simpler than the existing wording and covers all cases, including that where the Secretary-General is himself the depositary. Furthermore, it eliminates the need for the footnote to the suggested text.

5. In respect of the sample amendment procedure for limit of liability in paragraph 90 of the report it was pointed out that the term "Party" to the convention, i.e. a State for which the convention was in force, was used in paragraph 6 while "Contracting State", i.e. a State which has done all that is required in order to be bound by the convention but for which the necessary period of time has not passed, was used throughout the rest of the provision.

6. Paragraph 6 of the sample amendment procedure is in implementation of paragraph 4 which provides that only those States which had the right to participate in the meeting of the committee provided for in paragraphs 1 and 2 have the right during the following six months to object to an amendment adopted by the committee. Paragraph 5 goes on to say that all States which had the right

to attend the meeting of the committee are bound by the amendment once it goes into effect, unless they denounce the convention. Paragraph 6 provides that a State that joins at a later time is also bound by the amendment. It has been suggested that for the sake of consistency such a State should be described as "a State which becomes a Contracting State".¹

Sample provision for universal unit of account for limit of liability

7. During the session of the Working Group the delegate of the Soviet Union stated that, although the Soviet Union was not a member of the International Monetary Fund and under its law the Special Drawing Right could not be used as a means of payment, the Soviet Union was prepared to agree to the use as a unit of account in international transport conventions of the SDR as calculated by the International Monetary Fund.² The Working Group expressed its hope that other States which were not members of the International Monetary Fund would also be able to rely on the SDR as the unit of account in limit of liability provisions in international conventions.³

8. As a consequence the Working Group recommended to the Commission that it recommend that in the preparation of future international conventions containing limit of liability provisions or in the revision of existing conventions the unit of account be substantially in the form of article 26, paragraph 1 of the Hamburg Rules and of paragraph 4 as modified to the extent necessary by the deletion of paragraphs 2 and 3 of that article.⁴

9. Paragraphs 95 and 96 of the report of the Working Group contain two different suggestions as to the means by which the first paragraph for a universal unit of account for use in connection with a limit of liability provision might be formulated on the basis of article 26, paragraph 1 of the Hamburg Rules.⁵

10. The Commission may wish to prepare such a provision as recommended by the Working Group. The Commission may also wish to prepare a second paragraph for

¹ A simplified procedure for the entry into force of amendments of the amounts laid down in the 1969 Convention on Civil Liability for Oil Pollution Damage and the 1971 Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage was before the Legal Committee of the Inter-Governmental Maritime Consultative Organization at its 48th session held from 1 to 5 March 1982. This simplified procedure was similar to that proposed by the UNCITRAL Working Group. The report of the UNCITRAL Working Group was also before the IMCO Legal Committee.

At the end of a substantial discussion which repeated many of the considerations expressed in the UNCITRAL Working Group, the IMCO Legal Committee accepted that some action was necessary and it agreed to give further consideration to the matter at a future session (IMCO document LEG/48/6).

² The full statement is reproduced in the annex to A/CN.9/215 (reproduced in this volume, part two, II, B, 1).

³ *Ibid.*, para. 93.

⁴ *Ibid.*, para. 97.

⁵ Article 26 of the Hamburg Rules is reproduced in A/CN.9/WG.IV/WP.27, annex IV (reproduced in this volume, part two, II, B, 2), which will be available at the session of the Commission.

such a provision, consistent in terminology with that used in the first paragraph, based upon article 26, paragraph 4 of the Hamburg Rules as modified to the extent necessary by the deletion of paragraphs 2 and 3 of that article.

Recommendation to the General Assembly

11. The Commission may wish to invite the General

Assembly to recommend that, in the preparation of future international conventions containing limit of liability provisions or in the revision of existing conventions, the Contracting States use the unit of account provision and one of the two alternative provisions for adjusting the limit of liability for the effects of price changes, as adopted by the Commission.

C. Electronic funds transfer*

REPORT OF THE SECRETARY-GENERAL: ELECTRONIC FUNDS TRANSFER (A/CN.9/221** AND CORR. 1—FRENCH ONLY)

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* For consideration by the Commission see Report, chapter III, C.

** 17 May 1982.

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Introduction

1. At its eleventh session the Commission placed the subject of electronic funds transfers on its priority list.¹ At its twelfth session the Commission, recognizing the complex technical aspects of the topic, requested the Secretariat to do the preparatory work within the framework of the UNCITRAL Study Group on International Payments, a consultative body composed of representatives of banking and trade institutions.²

2. At its thirteenth session the Commission requested the Secretariat to submit at a future session a progress report on the matter, so that it might give directives on the scope of further work after having considered the Study Group's conclusions.³

3. The present report, a draft of which was prepared by the Secretariat, was examined by the Study Group at a meeting held in The Hague from 26 to 28 April 1982.

I. Description of electronic funds transfer systems

4. The distinguishing element in an electronic funds transfer is that the payment instruction transmitted to or between the banks is made in an electronic form rather than by the physical transmission of a paper-based payment instruction.⁴ This substitution of electronic impulses for paper is made in order to achieve an increase in speed of transmission of the payment instruction between the parties to the payment and to facilitate the handling of the volume of such messages, thereby reducing their cost.

5. Some electronic funds transfer systems are completely electronic from the entry of data by the originating bank to the processing of that data by the recipient bank. These systems may involve on-line computer net-

works, off-line batch-processed transfer systems, or the physical exchange of magnetic tapes or other electronic memory devices. Bank customers which have the necessary equipment may be allowed to submit their transfer instructions to their bank or to receive data from their bank in electronic form, extending the purely electronic nature of the transfer beyond the bank operations.

6. However, in most electronic funds transfer systems in use at the present time, the instructions received by the transmitting bank from its customer and the data given by the recipient bank to its customer are in paper form. In many cases only the message between the banks and the storage of the data by the banks are in electronic form.

7. The term "electronic funds transfer", therefore, is equivalent to the term "paper-based funds transfer" in that it describes the medium of communication but does not describe the banking or legal aspects of making a payment.

A. CREDIT TRANSFERS

8. In a credit transfer the transferor instructs his bank to pay a certain sum to the transferee.^{5,6} If the transferee does not have an account with the transferor bank, that bank instructs the transferee bank to pay the transferee. In some countries the credit transfer is the primary means of making non-cash payments.

9. A major advantage of the credit transfer is that the transferee bank can act on the payment instruction without concern as to the solvency of the transferor. The transferor bank is obligated to reimburse the transferee bank for the payment. Any doubts as to the solvency of the transferor are the concern of the transferor bank.

10. The credit transfer is particularly well suited to the use of electronic means of communication. In the normal case neither the transferor nor the transferee has any reason to object to the use of electronic means of transmission by

¹ *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, paras. 48 and 67 (c) (ii) (b) (Yearbook ... 1978, part one, II, A). The subject was discussed in the Report of the Secretary-General on the Programme of Work of the Commission (A/CN.9/149/Add. 3) (reproduced as annex III in Yearbook ... 1978, part two, IV, A).

² *Ibid.*, *Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 55 and 56 (Yearbook ... 1979, part one, II, A).

³ *Ibid.*, *Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 163 (Yearbook ... 1980, part one, II, A).

⁴ In the context of this report a "bank" is any institution which provides a funds transfer service, whether or not it is denominated as a bank under the applicable law. In addition to thrift, savings and other financial institutions which may offer such services, the postal service offers a funds transfer service in many countries. See, *Payment Systems in Eleven Developed Countries*. (Basle, Bank for International Settlements, 1980).

⁵ Throughout this report "transferor" refers to a person who pays a sum of money by a debit to his account in a bank. "Transferee" refers to a person receiving a sum of money by a credit to his account in a bank. The transferor may also pay the sum in cash to his bank while the transferee may receive the sum in cash from his bank.

⁶ For consistency of presentation, throughout this report it is assumed that the funds transfer is made by the bank for the account of a non-banking client, although in fact, many international electronic funds transfers are made by banks for their own account or for the account of other banks.

the bank. Since negotiable instruments are not used in credit transfers, the legal problems which must be overcome to collect negotiable instruments electronically do not arise.⁷

11. Credit transfers in electronic form have been widely used for international payments for over a hundred years in the form of cable transfers. Telex payment instructions and computer-to-computer links are but modern versions of this venerable device.⁸ Even in those countries in which the majority of domestic inter-bank transfers are made by the debit collection of cheques, wire and cable transfers are often used for business payments. In some of these countries the wire transfer facilities have been substantially improved in recent years and the majority of large business payments are made in this way.⁹

12. A recent development has been the payment of such obligations as salaries, pensions and monthly social security benefits to the transferee's bank account, a service available only by virtue of the increasing number of individuals who maintain current accounts in banks.¹⁰ This type of credit transfer is particularly suited to computer processing. Large volume transferors who possess equipment compatible with that used by the banking system may be encouraged to prepare themselves the magnetic tapes with the necessary payment data for use by their bank.

13. A new development, which is already in the experimental stage in several countries, is "home banking". With a computer terminal attached to a television set as well as to a central computer by means of electrical or telephone lines, an individual will be able to transfer funds from his account to another person's account in the same or a different bank.

B. DEBIT COLLECTIONS

14. In a debit collection the transferee instructs his bank to collect a specific sum of money from the transferor. He may attach to his instruction an instrument signed by the transferor, such as a cheque or a negotiable note payable at the transferor bank, which indicates that that bank should pay the sum and debit the transferor's account. Alternatively, the transferee may attach to this instruction a bill of exchange which he has drawn himself calling on the transferor or his bank to pay the sum indicated. The drawing of a bill of exchange by the transferee would normally have been previously authorized by the transferor, e.g. in a sales contract or by a letter of credit he has had opened for the benefit of the transferee.

⁷ Compare paras. 14 to 19 below.

⁸ The Society for Worldwide Interbank Financial Telecommunications S.A. (S.W.I.F.T.) operates a computer message switching network for various types of inter-bank messages.

⁹ See the reports on France and the United States in *Payment Systems in Eleven Developed Countries*, note 4 above.

¹⁰ In some countries, salaries and wages over a certain minimum must be paid directly to a bank account.

15. Before the transferor bank will pay to the transferee the sum indicated and debit the transferor's account, it will require specific instructions to do so. The cheque or note payable at the bank which has been presented for payment constitutes such an instruction, as does the application by the transferor to his bank to open a letter of credit for the benefit of the transferee. Other bills of exchange not drawn under a letter of credit are submitted by the transferor bank to the transferor for authorization to pay, unless that authorization has already been given in some other form.¹¹

16. Because it is the transferee who institutes the collection of funds he claims to be due to him, his bank — and every other bank in the collection chain — will seek assurances that any cheque, bill of exchange or note is genuine and that the transferor will have sufficient money in his account to pay the sum to be collected.¹² A significant portion of the law of cheques, bills of exchange, notes and other forms of debit collections is concerned with these problems.

17. The collection of cheques, bills of exchange and negotiable notes does not lend itself as well to electronic funds transfer procedures as do credit transfers. Under the law of many countries, such instruments must be presented to the drawee or maker, thereby requiring the physical movement of the paper from the transferee bank to the transferor bank, and perhaps to the transferor himself.

18. In some countries the law provides that a cheque may be presented at a clearing-house or that it may be retained by the original depositary bank, i.e. the transferee bank. In either case the pertinent payment information may then be transmitted to the transferor bank by electrical means of communication.¹³

19. In order to avoid problems arising out of the collection of bills of exchange, problems arising not only out of the legal regime of negotiable instruments but also out of stamp taxes and other considerations, an increasing share of debit collections in international trade involves a claim made by the seller-transferee without the use of a bill of exchange. Such claims may be suitable for transmission by electronic means, so long as they are not accompanied by commercial documents in a paper-based

¹¹ In trade between the member States of the Council for Mutual Economic Assistance payment is made by the buyer's bank without prior authorization from the buyer upon receipt of the seller's claim for payment, accompanied by the necessary documents. The buyer has the right for fourteen days from the receipt by his bank of the seller's invoice to demand return of all or part of the amount paid if the payment made was not in conformity with the contract. General Conditions of Delivery of Goods between Organizations of the Member Countries of the Council for Mutual Economic Assistance, 1968/1979, articles 49 and 52-55.

¹² For the purposes of this discussion, no distinction is made between an instrument which has been discounted by the bank and one which has been taken for collection.

¹³ In Belgium and Sweden cheques are retained by the depositary bank and presented for payment electronically. See the reports on Belgium and Sweden in *Payment Systems in Eleven Developed Countries*, note 4 above.

form.¹⁴ Experiments are currently in process to replace the traditional transport documents by electronic messages. The most difficult institutional problem has been to devise means of effectuating letter of credit transactions and bank financing, but several different solutions have been advanced and it can be expected that in the next few years these procedures will have passed from the experimental to the operational stage.¹⁵

20. Debit collections by electronic means have also been fostered by certain credit card operations as well as by the introduction of debit cards for use in automatic teller machines or for point-of-sale use. Although some credit card operations forward to the cardholder a copy of the paper receipt signed by him, other credit card operations retain the paper receipt at the first point of deposit and forward electronically the necessary payment information.

21. In addition to debit collections arising out of specific transactions, as have been described above, "direct debiting" may be instituted in favour of a transferee to whom large numbers of people are indebted on a regular basis. Direct debiting is particularly susceptible to electronic processing and large customers with their own computer facilities may themselves prepare the magnetic tapes for introduction into the system.

C. DIRECT TRANSMISSION, CORRESPONDENT RELATIONS AND CLEARING-HOUSES

22. Payment instructions, whether credit transfers or debit collections and whether paper-based or electronic, can be passed between the transferor bank and the transferee bank, through one of three types of routes. The payment may be transmitted directly between the two banks. If the two banks do not have a direct banking relationship, the transferor bank may send the payment instruction to a correspondent bank which does have a direct banking relationship with the transferee bank. It could happen, of course, that the payment instruction might pass through the hands of two or more correspondent banks. In order to handle the transmission of large numbers of payment instructions between banks, a clearing-house may be established.

23. An international cable or telex transfer, which is the traditional form of electronic funds transfer, is routed either

by direct transmission between the banks concerned or through correspondent banks. Transfers through S.W.I.F.T. are handled in the same way, as are many individualized high-value transfers in domestic electronic payment systems.¹⁶

D. SETTLEMENT

24. Settlement between banks for electronic funds transfers is accomplished in the same manner as for paper-based funds transfers. In the case of an individualized funds transfer, settlement is normally effectuated by off-setting debits and credits in the accounts of the two banks with one another, or in their accounts with the central bank or a bank which is a correspondent bank of both. In the case of a clearing-house, only the net debits and credits of the banks arising out of the clearing or at the end of the day's activities need be settled by debits and credits in the appropriate accounts.

25. The rules as to the time of settlement need not be different for electronic funds transfers than they are for paper-based funds transfers. However, the increasing speed of transfer by electronic means leads to an increasing volume of transfers. Therefore, the risk to a bank which has made payments at the request of another bank but which has not received settlement for those payments may become dangerously high.¹⁷ As a result, the introduction of electronic funds transfers has increased the pressures for quick settlement. At the same time the availability of computers has made it easier to move to same day settlement and even, in some cases, to simultaneous payment and settlement.

II. Legal issues

26. Electronic funds transfers raise three types of legal issues: those associated with the payment process, those associated with the electronic nature of the communication and record keeping and those associated with the institutional structure within which an electronic funds transfer system operates. Any national electronic funds transfer system must deal with all of these problems either explicitly or implicitly.

27. These legal issues also arise in respect of international electronic funds transfers. Many of them are so closely integrated with domestic funds transfers that it would not

¹⁴ The bill of exchange payable at term is a traditional form of supplier credit in France. The collection of these bills is highly labour intensive and, therefore, costly. After several experiments designed to remedy the situation, a new version of the bill of exchange was developed, the *lettre de change relevé*, which can be created in either paper or electronic form. In either case, however, transmission of the bill between the banks is made electronically. The original paper-based bill, if one exists, is retained by the transferee bank. For a description of the mechanics and a discussion of the legal problems involved, see M. Vasseur, *La lettre de change relevé*, 28 Rev. tr. dr. com., 203 (1975). See also, Trib. com. de Roubaix, 2 juillet 1980, D.S. 1980. Jur. 519, note Y. Letartre.

¹⁵ E.g., K. Grönfors, *Cargo Key Receipt and Transport Document Replacement* (Göteborg, 1979).

¹⁶ In this context a central bank which operates a wire-transfer service in which the transferor bank's account with the central bank is debited for each transaction and the transferee bank's account is credited functions as a correspondent bank of the transferor and the transferee bank.

¹⁷ Prior to the changeover from next day settlement to same day settlement on 1 October 1981, it was estimated that the eleven principal settling banks in the New York Clearinghouse Interbank Payment System, known as CHIPS, averaged \$US 14 to 28 thousand million in overnight credit risk. International Herald Tribune, 24 September 1981, p. 11.

be feasible to consider them separately. However, there are several legal issues which may be of particular concern in the context of international funds transfers. Among these are: (a) when payment becomes final and the consequences associated with finality of payment;¹⁸ (b) liability for loss caused by delayed or incorrect payment instructions; and (c) the evidential value of payment records kept in electronic form.

A. WHEN PAYMENT BECOMES FINAL

1. General considerations

28. Few legal systems have statutory rules which specify when payment of a funds transfer becomes final and the consequences of its becoming final.¹⁹ In most cases, such formalized rules as exist are to be found in inter-bank agreements, clearing-house rules and the general conditions of banks.²⁰ These sources, however, govern only a few of the possible contingencies.

29. The concept of payment in an inter-bank funds transfer is complex. There is no single act which can be said with assurance to be the act of payment. Instead, payment is made by a process which takes place over a period of time. Although this process includes certain basic procedures which must be followed in any funds transfer, the actual mechanics may differ from country to country, from bank to bank and, within a single bank, they may differ depending on the type of transfer.

30. As a result different points of time have been chosen in various contexts as the time when payment becomes final. The following paragraphs describe some of the more important possibilities in the context of a credit transfer.

2. Notice to the transferee bank of the transfer

31. The earliest point of time at which payment could be said to take place in an inter-bank credit transfer is the

¹⁸ The decision as to whether payment of certain international electronic funds transfers had become final was the determining element in the litigation in the United Kingdom and the United States following the insolvency of the Herstatt Bank in 1974. *Momm v. Barclays Bank International Ltd.*, [1976] 3 All E.R. 588 (Q.B.); *Delbrueck and Co. v. Manufacturers Hanover Trust Co.*, 464 F. Supp. 989 (S.D.N.Y. 1979), *aff'd* 609 F.2d 1047 (2d Cir. 1979).

¹⁹ This report considers when payment of the funds transfer becomes final, not when payment of the underlying obligation takes place. Although the two concepts may be related, different criteria may apply to each of them.

²⁰ In a questionnaire sent by the Study Group to central banks in the spring of 1980 the question was asked as to what laws or agreements determine when payment is final. Austria, Canada, Kuwait, Netherlands, New Zealand, Norway and United Kingdom replied that there were none. Australia, France, Germany, Federal Republic of, and Portugal referred to various inter-bank agreements covering aspects of the problem. The United States referred to the regulation governing the wire-transfer system operated by the Federal Reserve System. Czechoslovakia cited a provision in its Economic Code.

moment at which notice is sent to the transferee bank. This is the result in the United States for credit transfers made through the Federal Reserve System. The Federal Reserve operates a high-speed credit transfer service by which banks may transmit funds to other banks in the United States. The service is used by banks both to transmit funds for their own account and to effect transfers for the account of their customers. Nevertheless, from the viewpoint of the Federal Reserve and of the regulations governing the system, the only parties to the transfer are the banks concerned.²¹ Payment is made by crediting the account of the transferee bank and debiting the account of the transferor bank with the appropriate Federal Reserve Bank.

32. The regulation which governs these transfers provides that payment is final as to the two banks and is available for immediate use upon the sending of a notice of the transfer to the transferee bank.²² When the transferee bank is the final transferee, i.e. when it has no customer for whose account the transfer has been made, the rule is complete. The regulation gives no indication whether payment is also final at that time as regards the payment by the transferee bank to the transferee or between the transferor and the transferee.

33. Nevertheless, in a case such as this where the transferee bank has received irrevocable credit with the central bank at or before the time the transfer instruction has been sent to it and the credit is available for immediate use by the transferee bank, it might even be reasonable to consider payment as final at that time as to the transferee as well.²³ In this case, and in contrast to those discussed below, completion of the process by which the transferred sum was credited to the account of the transferee would be a mechanical act of no legal significance.

3. Decision that settlement offered is acceptable

34. It would be less acceptable to consider payment as final as to the transferee bank upon the sending of it of the transfer instruction if settlement for the transfer were by means other than an irrevocable credit with the central bank available for immediate use. In these cases perhaps the earliest point of time at which payment might be considered to be final is when the transferee bank decides that the means of settlement proposed by the transferor bank is acceptable. In the case of large individual transfers, such a decision may be made and indicated by an objective act of an officer of the transferee bank.

4. Posting of credit or notice to transferee

35. In routine transfers no such conscious decision is

²¹ "Transferor" means a member bank . . . 12 Code of Federal Regulations § 210.26 (g).

²² *Ibid.*, § 210.36.

²³ The regulations also provide that the transferee bank must "Credit promptly the beneficiary's account or otherwise make the amount available to the beneficiary". *Ibid.*, § 210.30 (b) (1).

made and the first objective act which can be relied upon to occur is the credit entry made to the transferee's account. It is that objective act which is considered to be the act of payment in many legal systems.²⁴ In some other legal systems payment is considered to have taken place only when a notice of the credit transfer has been sent to the transferee by the transferor bank. This, it should be noted, is an application of the same approach discussed above in respect of payment to the transferee bank by the Federal Reserve System in the United States.

5. Availability of funds to transferee

36. Since the relevance of payment to the transferee is that he has access to the funds, payment may be considered to be final at the time he has an unqualified right to use the funds. In many funds transfer systems settlement between the banks is made as a routine matter one, two or even more days after the payment instruction has been received by the transferee bank.²⁵ In such cases, it would be normal for the transferee bank to restrict the availability of those funds to the transferee until the bank itself had received settlement, even if the transferee bank had no cause to consider the transferor bank a credit risk.²⁶ It would, therefore, be a matter of internal decision by the transferee bank as to whether it would post the credit with a value date of the expected date of settlement or whether it would delay posting the credit until settlement had been received.

6. Debit collections

37. A similar set of possibilities exists as to the time of payment of a cheque, bill of exchange or other debit collection item. In a debit collection, however, it is the transferor bank which does the relevant acts which constitute payment of the item, and not the transferee bank as in a credit transfer. The item is received by the transferor bank and examined for apparent authenticity.²⁷ The files are checked to

see if payment is authorized, the account is examined to determine whether there is a sufficient credit balance to cover the item or whether a line of credit has been authorized and the amount of the item is debited to the transferor's account. Parallel to what was suggested in respect of the credit transfer, the point of time at which payment of the debit item is final can be the moment when the transferor bank has completed the necessary verifications and decided to pay by debiting the transferor's account or the moment when it has posted the debit to that account. As suggested below, payment of the debit item may also become final after the debit has been posted to the transferor's account.

7. Posting prior to verification

38. The acts which may be considered to constitute payment of credit transfers and debit collection items have so far been presented in the standard chronological order. However, in some countries it is standard banking procedure for incoming items, whether credit transfers or debit collections, to be posted to the relevant accounts prior to the time any verification is made of the item itself, or of the account to be debited in case of a debit collection or the means of settlement in the case of a credit transfer. In these countries, the book-keeping operations for the day's activities may be completed during the night. The next morning problem items are brought to the attention of the bank's management. If it is decided not to pay an item, the book-keeping entries are then reversed.²⁸

39. Such a procedure is of most significance in respect of debit collections where, after posting has been completed, it is found that the debit was not previously authorized by the transferor or that authorization had been withdrawn in time, the transferor had insufficient credit to his account to pay the item or for some other reason the item was not payable. However, where the bank has instituted such a book-keeping routine for debit collections, it may also find it convenient to use it for credit transfers. Only after the transferee bank had posted the credit to the account of the transferee would it decide whether the settlement for the transfer offered by the transferor bank was adequate. Where the transferee bank was uncertain that it would receive settlement from the transferor bank, it could reverse the credit entry to the transferee's account and return the payment instruction to the transferor bank.

40. In those countries in which this book-keeping procedure is recognized, the rules on payment must provide a legal justification for the bank to reverse the book-keeping entries it would not have made if it had followed the

²⁴ In the questionnaire sent by the Study Group to central banks in the spring of 1980, the question was asked when payment becomes final. Several respondents indicated that the answer was not clear. Several others indicated that "normally" it occurred at a specific time. Most respondents stated that in a credit transfer payment was made when the credit was posted to the transferee's account. One respondent replied that "it probably becomes final when money is passed between the banks involved in settlement of the transaction".

²⁵ Under the S.W.I.F.T. rules the "pay date" on which the transferor bank requests the transferee bank "to credit or pay the beneficiary customer . . . may not be earlier than the value date" on which the amount of the transfer is available to the transferee bank.

²⁶ In the "*Chikuma*", [1981] 1 Lloyd's Rep. 371 (H.L.), a correspondent bank provided the funds four days after it telexed payment instructions to the transferee bank. The effect of withholding settlement for four days "seems . . . to produce a situation, in accordance with Italian banking law and practice, which in the eyes of an English banker or lawyer, has some strikingly unusual features". *Ibid.*, at 374. The House of Lords, applying English law, held that under the particular terms of the contract payment between the parties had not been made until the transferee bank received settlement. As a result of late payment, a ship was withdrawn from a charter-party at a loss to the Norwegian charterer said to be over \$US 3,000,000.

²⁷ Rather than examining either the item for apparent authenticity or the files for an authorization to pay, the transferor bank in

many debit collection systems may rely upon an agreement by the transferee bank to indemnify the transferor bank if the item was not authentic or payment was not authorized by the transferor.

²⁸ This practice is widely used in the United States. See Uniform Commercial Code, § 4-301, Official Comment No. 1. For a description of the practice in New Zealand, see A. Tyree, *Electronic Funds Transfer in New Zealand*, 8 N.Z. Univ. L.R. 139 (1978).

standard chronological order. One way to achieve this result is to consider payment as having been made only when the transferee bank decides not to reverse the book-keeping entries which otherwise would have constituted payment. This might be expressed as the passage of a pre-determined amount of time at the close of which the book-keeping entries had not been reversed. For example, payment could be considered as having been made at midnight of the day after receipt of the item if the book-keeping entries had not been reversed by that time.

8. *Criteria for determining when payment is final*

41. This discussion of the appropriate moment to consider payment as final suggests that the dominant consideration is the decision by the transferee bank in the case of a credit transfer or the transferor bank in the case of a debit collection that the item is genuine, that payment was authorized and that the bank will be reimbursed for the payment. It has been noted that there is a broad range of points of time that would implement this dominant idea, depending on the nature of the proposed settlement, and the normal book-keeping procedures followed by banks. However, following this line of thought, it would seem that the moment at which payment is legally recognized as having occurred should be delayed until there remains only a minimal risk that the bank making payment will not be reimbursed.

42. On the other hand such a position would have the corollary effect of delaying the time of payment for all other purposes. The funds would belong to the transferor and not to the transferee and would be subject to legal process by the transferor's creditors until that later point of time. Any right the transferor might have to rescind the payment order until payment becomes final might continue to exist. Payment by the transferor to the transferee of the underlying contractual obligation might be understood not to take place until payment of the funds transfer as here determined had taken place.

43. These considerations might therefore lead to another conclusion, i.e. that it would be better to consider payment of the funds transfer as final for all purposes at some earlier point of time, with the exception that if the transferee bank failed to receive settlement for the item within a specified period of time, the transferee bank could revoke the payment to the transferee, debit his account, and return the transfer item to the transferor bank.

9. *Effect on clearing-house transfers*

44. The need for a clear rule on the effect of a transferor bank's failure to settle for an item which has been "paid" to the transferee by the transferee bank is particularly important when the transfer has been effected through a clearing-house at which settlement of each participating

bank's net debit or net credit balance is made periodically, such as at the end of the day, rather than at each clearing.

45. If a bank cannot settle for its net debit balance, it normally means that the bank is insolvent. Since the failure to settle is of a net debit balance, it cannot be allocated to any specific payment instruction submitted to or by the insolvent bank. No transferee bank is in a position to know at the time it receives a payment instruction through a clearing-house whether any other specific bank will end the day with a net credit or net debit balance or what the magnitude of that net balance might be. Therefore, it cannot protect itself by refusing to receive and process the transfer as it could if the transfer instructions had been received directly by telex or the like.²⁹

46. There are a variety of schemes which can be used to allocate this loss. Among those schemes is that all the transactions with the insolvent bank would be deleted from the day's activities and returned to the remitting bank.³⁰ New net balances would be struck between the remaining participants in the clearing-house.

47. This procedure would seem to indicate either that payment between the banks is not final until settlement has been completed or that, in spite of payment being final, payment between the banks could be reversed in case of a failure of one of the banks to settle with the clearing-house. Deletion of the day's transactions between the insolvent bank and the other banks in the clearing-house may have the effect of deleting those transactions as regards the customers of both the insolvent bank and of all the other banks in the clearing-house to which or from which transfer instructions were sent on the day in question.

10. *Conclusion*

48. The rules as to the point of time when payment is final are not clear. Few statutory rules exist and the various inter-bank agreements cover only limited aspects of the

²⁹ This problem does not arise at a clearing-house which requires settlement for all net debit balances in cash or in immediate credit on the books of the central bank before the clearing is completed. The disadvantages of such a procedure are beyond the scope of this report.

³⁰ Article 13 of the internal regulations of the automatic clearing-house operated by the Bank of France dated 29 July 1977 provides that

"If, for any reason, the current account at the Bank of France of a participant with a debit balance does not have sufficient funds to cover the balance at the close of operations, and if the cover is not produced, the Bank of France will advise the other participants to the extent possible on that day, and at the latest the day following before 11:30.

"The participants must consider the operations directed to the defaulting establishment (and its sub-participants) or coming from the latter (and its sub-participants) as null and void.

"In the light of the knowledge in its possession the Bank of France will determine the new net balances and send to the participants a corrected statement."

Compare the provisions in the CHIPS rules discussed in H. Lingl, *Risk Allocation in International Inter-bank Electronic Fund Transfers: CHIPS and SWIFT*, 22 Harv. Int. L. J. 621, 643-648 (1981).

problem. No agreed upon rules exist for international payments.

B. LIABILITY FOR LOSS CAUSED BY DELAYED OR INCORRECT PAYMENT INSTRUCTIONS

49. Customers and their banks alike may suffer a loss if a funds transfer is not carried out as expected. The nature of electronic funds transfers has introduced several new elements into this problem which are either unknown or are of less significance in paper-based funds transfers.

1. Loss-causing factors

(a) Non-standardized messages

50. In contrast to paper-based funds transfers which use broadly similar formats, there is no generally recognized standard format for electronic funds transfer messages. Each cable or telex is individually composed and contains the information thought to be relevant by the sender.³¹ The possibility of error in composition of the message by the sender and comprehension by the receiver is thereby increased.

51. Unstructured messages do not lend themselves to computer processing. Therefore, in order to facilitate the use of computer-processed electronic funds transfer systems standard message formats have been created. These formats, once adopted, are mandatory for use within that system.

52. Each computer-processed system has devised its own formats for its own purposes. Where a bank receives a funds transfer instruction through an international system which it must pass on through a domestic system, or the reverse, the message must be converted from the format used in the first system to the format used in the second. The use of interface programmes to do this automatically is possible when the two formats have equivalent message fields, which is not always the case.³² Therefore, until there is a standardization of the formats for use in domestic as well as international funds transfers, electronic funds transfer messages will continue to be received in human readable form and rekeyed into other transfer systems.

³¹ As of 31 December 1981, the Technical Committee on Banking of the International Organization for Standardization had prepared a working draft of standard telex formats for inter-bank payment messages.

³² CHIPS Administrative Procedure No. 6 gives instructions for a CHIPS/S.W.I.F.T. or S.W.I.F.T./CHIPS interface. A description of the method by which this is accomplished by one large American bank was described by A. Cacchioli, *Our Solution - High Volume Users*, in S.W.I.F.T. International Banking Operations Seminar 1980 (SIBOS '80), pp. 112-113. A criticism of automatic conversion between S.W.I.F.T. and CHIPS was made by I. Silfvast, *The Impact on European Banks of the Differences in the Banking Practice Concerning International Transfers in the USA*, in SIBOS '81, p. 125 "since the S.W.I.F.T. and the CHIPS formats are not compatible, the result becomes mutilated".

(b) Re-creation of messages

53. Rekeying a transfer message creates the possibility of error. This possibility of error is to some degree unavoidable in all electronic funds transfers. In contrast to paper-based funds transfers where the original paper form filled in by the customer can usually be forwarded through the banking system precluding the possibility that the payment instruction will be altered except by fraud, an electronic funds transfer message is re-created at each processing point. Payment instructions given to a bank in paper form are transformed into electronic messages which may again be reproduced on paper at receipt. Telex transfers through a correspondent bank require the correspondent bank to pass on a new message with a somewhat different data content. Messages sent over packet-switching networks are broken into segments of a uniform length which are sent by separate circuits and reassembled at the destination. Transfer instructions submitted on magnetic tapes to an automatic clearing-house are sorted and recorded on new magnetic tapes before being sent to the recipient bank. Each of these processes introduces the possibility of an inadvertent change in the content of the payment instruction through human error, an incorrect computer programme or a breakdown or defect in the equipment. However, these errors can be detected before they pass through the system if the necessary controls are designed into the system as well as into the operations of each bank and if those controls are rigorously applied.

(c) Non-standardized procedures

54. International funds transfers, whether electronic or paper, are more difficult for banks to handle without error than are domestic transfers because of the lack of international agreement on appropriate procedures. Each transfer message must, therefore, be read carefully to be sure as to the procedure being used by the transferor bank. That message may be unclear, especially when it is composed in unstructured cable language.³³

55. This confusion may be compounded when the local banking practices in the recipient country are different from those in the sending country. Expectations as to the time within which funds will be made available may turn out to be incorrect because of a local practice that a correspondent bank may withhold settlement for several days, thereby increasing its float,³⁴ or that remittance will be made to remote locations by mail or by check, even though the international payment instructions requested the highest priority be given to the payment.³⁵

³³ See the examples given by I. Silfvast, *ibid.*, and R. Polo, *The Quality of Today's International Transfers*, *ibid.*, p. 117.

³⁴ See the "Chikuma", note 26 above. The Court of Appeal estimated that the correspondent bank had earned between \$US 70 and 100 in interest on the payment of \$US 68,863 by delaying settlement for four days.

³⁵ See I. Silfvast, *op. cit.* p. 126.

2. Nature of the loss

(a) Loss of principal

56. When an electronic funds transfer is credited to the wrong account, credited to the correct account for the wrong amount or processed twice, the transferor risks losing the principal amount of the incorrect transfer. In most cases, the error can be rectified by a debit to the account of the incorrect transferee with a corresponding credit to the account of either the transferor or the correct transferee, as the case may be. The transferee bank may be authorized to debit the incorrect transferee's account without his prior consent.³⁶ It is only when recovery cannot be made from the incorrect transferee that questions of allocation of loss arise.

57. Fraud is probably a more important source of loss of principal in electronic funds transfers. All major electronic funds transfer systems take precautions against fraud ranging from the use of personal identification numbers (PIN) in connection with debit cards at an automatic cash dispenser, through test keys and encryption for inter-bank electronic funds transfers.³⁷ The degree of security these procedures afford is to some extent a measure of the effort and the money spent on them.

(b) Loss of interest

58. Interest claims for late payments, which were hardly known twenty years ago, are now a daily occurrence. Interest rates are high. Major funds transfers are less often than before made by the physical movement of paper, which is slow and uncertain as to the time required. Cash management techniques have made public and corporate treasurers throughout the world conscious of the interest earning potential of their cash balances.

59. Banks share this concern. S.W.I.F.T., for example, has adopted rules for the allocation of loss of interest for delays in payments made through that system.³⁸ These rules present no innovation as to theory. Their main value is to set forth in detail the operating procedures which must be followed by the sending and receiving bank and by S.W.I.F.T. as a system to avoid liability for interest arising out of a late payment.³⁹

³⁶ In the Federal Republic of Germany the Banks' General Business Conditions art. 4 (3) provide that "Where credit entries are made in consequence of a mistake or clerical error, or for any other reason, without corresponding instructions having been given, the bank may reverse them by simple entry." Compare the regulations governing credit transfers in the United States through the Federal Reserve System which provide that in the case of an error the Federal Reserve Bank may request the transferee to return the funds. 12 Code of Federal Regulations § 210.35 (b).

³⁷ See *Security and Reliability in Electronic Systems for Payments*, (Basle, Bank for International Settlements, revised ed. 1978).

³⁸ The rules were originally published in S.W.I.F.T. Board Paper No. 185, *Responsibility and Liability*, and were reprinted in S.W.I.F.T. Newsletter, April 1979. Board Paper No. 185 has been incorporated in the S.W.I.F.T. User Handbook.

³⁹ The transmitting bank is responsible in five circumstances: (a) when S.W.I.F.T. fails to acknowledge the transmission of a message;

(c) Changes in exchange rates

60. Under the regime of fixed exchange rates of the Bretton Woods system, exchange losses were an episodic event arising out of a devaluation or revaluation of a currency. With exchange rates currently fluctuating daily, customer claims for reimbursement of exchange losses arising out of late payments are a more frequent occurrence.

61. No international electronic funds transfer system has rules which allocate the responsibility for these losses.⁴⁰ It has been suggested that the S.W.I.F.T. rules for allocation of interest losses could serve as a model for allocating the exchange losses arising out of similar events.⁴¹

(d) Consequential damages

62. The least frequent, but potentially the most serious, losses are the indirect damages suffered when a contract is lost, a penalty is incurred or a ship is withdrawn from a charter-party because a required payment was improperly handled.⁴² When these events occur, the damages can easily amount to many times the size of the transfer. The infrequency of the reported cases may indicate that transferors normally allow a margin of safety for their payments when they anticipate such drastic consequences.⁴³

(b) when S.W.I.F.T. acknowledges it, but the message appears on the report of undelivered messages; (c) when the transmitting bank enters an urgent message, but receives no delivery notification from S.W.I.F.T.; (d) when it enters a message in an inappropriate format; or (e) when it fails to react promptly to notification by S.W.I.F.T. that a bank regional processor, or operating centre is not functioning.

The receiving bank is responsible in four circumstances: (a) when it fails to carry out the payment date instructions in the message; (b) when it fails to react promptly to system messages; (c) when it fails to reconcile adequately incoming messages according to sequence numbers; or (d) when it fails to follow S.W.I.F.T.'s terminal connection policy.

S.W.I.F.T. is responsible in three circumstances: (a) when it acknowledges a message to the sender, but fails to put the message on the undelivered message report and fails to deliver the message; (b) when it or its personnel perform improperly; or (c) when it fails to notify members promptly of failures of banks, operating centres, or regional processors.

⁴⁰ Compare Draft Convention on International Bills of Exchange and International Promissory Notes, arts. 71 and 72, A/CN.9/211 (reproduced in this volume, part two, II, A, 3), and Draft Convention on International Cheques, arts. 64 and 65, A/CN.9/212 (reproduced in this volume, part two, II, A, 5), for rate of exchange to be applied in case of dishonour of the instrument. See also the Commentaries on the two draft conventions, A/CN.9/213 (reproduced in this volume, part two, II, A, 4) and A/CN.9/214 (reproduced in this volume, part two, II, A, 6) respectively.

⁴¹ R. Polo, note 33 above, p. 117; *New S.W.I.F.T. Rules on the Liability of Financial Institutions for Interest Losses Caused by Delay in International Fund Transfers*, 13 Cornell Int. L.J. pp.311, 325 (1980).

⁴² See, for example, *Evra Corp. v. Swiss Bank Corp.*, 522 F. Supp. 820 (N.D. Ill. 1981), rev. 673 F.2d 951 (7th Cir. 1982), in which the trial court held the defendant correspondent bank liable for over \$US 2,000,000 for negligence in failing to transmit payment instructions for \$US 27,000 to the transferee bank by the pay date.

⁴³ See, e.g. H. Schroder, *Fulfilling the Client's Needs*, SIBOS '80, p. 170 where he complained that because of the long and uncertain delays from the time they give a payment order till the time it is received in a foreign country "we very often have to build in considerable time contingencies if we are contractually committed to our suppliers for payment at the disposal of the supplier's account at a given date". The court of appeals in reversing the decision of the trial court in *Evra Corp. v. Swiss Bank Corp.*, note 42 above p. 957, said in part that "it was imprudent . . . for [the plaintiff] . . . to wait till arguably the last day before payment was due to instruct its bank to transfer the necessary funds overseas".

3. *Standardization and liability*

63. The actions being taken within the international banking community to standardize message formats and, more hesitantly, to standardize banking procedures, will not only reduce the incidence of delayed and incorrect transfers, they will ease the task of assigning responsibility for the losses which do occur. In this respect the S.W.I.F.T. rules on interest losses are revealing. They could not have assigned responsibility between the three participants in a S.W.I.F.T. transfer on the basis of failure to follow one of the operating rules of the system unless there already had existed operating rules that the participating banks were required to follow.

64. At the same time these rules reveal that even within S.W.I.F.T. international agreement on procedures does not yet go beyond the technical elements of the transfer process. These rules make the bank receiving the message responsible if the message was properly addressed to it and received prior to the cut-off time but was not processed with appropriate value by the "pay date" indicated in the message, which date may not be earlier than the date on which the amount of the transfer is at the disposal of the receiving bank.⁴⁴ The "pay date" is, however, only "the day on which the receiving or a third bank is requested to credit or pay the beneficiary (private person or any other non-banking institution) subject to national convention and exchange control regulations, if any".⁴⁵ S.W.I.F.T. gives two explanations for this rule. The first is that "it is possible that the receiving bank is not able to meet the 'pay date' because time between 'value date' and 'pay date' is not sufficient according to the bank's normal business conditions".⁴⁶ The second, which is related to the first but independent of it, is that "Obviously each bank has its own terms of business related to the relationship with its correspondents".⁴⁷ These rules accept, therefore, a "national convention" or the "terms of business" of a bank which would limit the obligation of the transferee bank to make the funds available to the beneficiary by the pay date indicated by the transferor bank in the message.

4. *Responsibility of bank for acts of others*

65. Two separate approaches are taken to the responsibility of a bank to its customer for loss arising out of events which occur somewhere in the system. Under one approach each bank is responsible to the transferor only for losses arising out of its own wrongful acts. Under a second approach the transferor bank is responsible to the transferor for

losses arising throughout the system. In the normal case the transferor bank would seek reimbursement from the party who caused the loss.⁴⁸

66. The first approach recognizes that no bank has control over the operations of any other bank. While instructions can be given in respect of anticipated problems, no bank can be expected to be aware of all foreign banking practices. It cannot avoid the possibility that another bank may be negligent in regard to the transaction, so long as that bank is not so consistently negligent as to be an inappropriate channel through which to pass payment instructions.

67. The second approach emphasizes the responsibility of a bank to its customer to perform a service that requires the participation of other banks, clearing-houses and communications facilities. With rare exceptions the bank makes all the operational decisions affecting the transfer. It transforms the payment instructions as they are received from the customer into the message to be transmitted electronically, chooses the communications facilities (e.g. telex or S.W.I.F.T.) and the correspondent banks. The customer relies upon his bank to have established, or to have associated itself with, a network of foreign banks that will permit the payment instructions to be performed as requested.

68. This approach encourages banks which participate in international electronic funds transfers to support improvements in funds transfer procedures which reduce the incidence of loss.

5. *Conclusion*

69. The rules adopted by S.W.I.F.T. illustrate the perceived need for guidance as to the responsibility for losses arising out of electronic funds transfers. What may have been an occasional problem in the past which could be satisfactorily settled by reference to the applicable national law under traditional conflicts of law doctrines has become an everyday problem. The least satisfactory aspect of the current situation is the uncertainty as to the rights of the customer when payment was not made as expected in a foreign country.

C. *LEGAL VALUE OF COMPUTER RECORDS*

1. *Background*

70. Bank records involving huge sums are maintained in computers. In international electronic funds transfers there may be no paper records to evidence the transaction other than those produced by the computer itself.⁴⁹ This is

⁴⁴ S.W.I.F.T. Board Paper No. 185, para. 5 (a). Although the new rules on responsibility relied upon the existing operating rules and, therefore, introduced no changes in S.W.I.F.T. procedures, it was found necessary, in order to fix responsibility, to clarify the terms "value date" and "pay date" as used in those operating rules.

⁴⁵ *Ibid.*, para. 2 (b).

⁴⁶ *Ibid.*, comments.

⁴⁷ *Ibid.*

⁴⁸ The second approach, which focuses on the immediate responsibility of the transferor bank to the transferor, need not preclude a direct claim by the injured transferor against the party known to be at fault.

⁴⁹ Nevertheless, a properly designed system will leave an audit trail which will make possible the detection of fraud or error.

not, however, unique to electronic funds transfers, whether international or domestic, since the computer is becoming the basic book-keeping machine used by business throughout the world.

71. In spite of the widespread use of computers in all fields of commercial activity, there remains a hesitancy in some countries to admit computer records as evidence before courts and arbitral tribunals. It is thought that the current state of techniques in the matter of recordings on computers does not give sufficient guarantees against falsification.⁵⁰ In addition, there are classical legal barriers concerning the use of such recordings as evidence, particularly in countries of common law tradition.⁵¹

2. *International actions taken to facilitate the use of automatic data processing*

72. Although the question of the evidential value of computer records in litigation is essentially a matter for domestic concern, the widespread and ever-increasing use of computers in international trade has led to provisions in a certain number of international legal texts intended to facilitate their use. The Hamburg Rules, which require that a signed bill of lading be issued if requested by the shipper, provides that:

"The signature on the bill of lading may be in handwriting, printed in facsimile, perforated, stamped, in symbols, or made by any other mechanical or electronic means, if not inconsistent with the law of the country where the bill of lading is issued."⁵²

An identical provision is to be found in the United Nations Convention on International Multimodal Transport of Goods.⁵³

73. Montreal Protocol No. 4 of 25 September 1975 to the Convention for the Unification of Certain Rules relating to International Carriage by Air would permit as a substitute for the delivery of an air waybill "any other means which would preserve a record of the carriage to be performed", so long as this was done with the consent of the consignor.⁵⁴

⁵⁰ See Council of Europe Explanatory Memorandum to Recommendation No. R (81) 20, adopted by the Committee of Ministers on 11 December 1981, para. 17.

⁵¹ See A/CN.9/149/Add. 3, paras. 16-20 (reproduced as annex III in Yearbook . . . 1978, part two, IV, A).

⁵² United Nations Convention on the International Carriage of Goods by Sea, 1978, Hamburg, 31 March 1978, art. 14 (3) (Yearbook . . . 1978, part three, I, B).

⁵³ Geneva, 24 May 1980, art. 5 (3) (Final Act of the United Nations Conference on a Convention on International Multimodal Transport and Convention on International Multimodal Transport of Goods, TD/MT/CONF/17, 1981). These texts reflect a diminution of the requirement of a manual signature on a piece of paper as a means of authenticating the document and its data content. See in this regard Recommendation No. 14 of the Working Party on Facilitation of International Trade Procedures entitled "Authentication of Trade Documents by Means other than Signatures". These texts are also a reflection of a decline in the importance of the concept of negotiability.

⁵⁴ Art. 5(2) of the Convention as it would be amended by art. III of the Protocol.

74. In the field of trade facilitation the International Civil Aviation Organization has recommended to its Contracting States to "make arrangements which would enable the use of commercial documents required for the clearance of air cargo produced by electronic data processing techniques in legible, understandable, and acceptable form".⁵⁵ Similarly the Inter-governmental Maritime Consultative Organization, now called the International Maritime Organization, has recommended that "Documents produced by electronic and other automatic data processing techniques, in legible and understandable form, shall be accepted".⁵⁶

75. The Customs Co-operation Council has recommended that States, whether or not members of the Council, should

"1. Allow under conditions to be laid down by the Customs authorities, declarants to use electronic or other automatic means to transmit to the Customs Goods declarations for automatic processing. Such declarations may be transmitted either by direct link between the data processing systems of the Customs and those of declarants or on magnetic or other ADP media;

"2. Accept, under conditions to be laid down by the Customs authorities, that Goods declarations which are transmitted by electronic or other automatic means to Customs be authenticated other than by handwritten signature."⁵⁷

3. *International actions in respect of evidential value of computer records*

76. This approach, by which legislative texts and recommendations of international organizations to facilitate the use of electronic and other automatic data processing in international trade are prepared on a sectoral basis, may however not be sufficient unless supported by an approach which is designed to ensure that the use of computer records as evidence in litigation is not prevented. This was noted by the Working Party on Facilitation of International Trade Procedures when it recommended to the Customs Co-operation Council that the Council make "a study of changes which are necessary to national laws to admit as evidence information stored on computer",⁵⁸ which the Council declined to do on the grounds that this was not purely a customs matter.⁵⁹

⁵⁵ Recommendation 4.4 in Chapter 4 of Annex 9, "Facilitation", to the Convention on International Civil Aviation (Chicago, 1944), Seventh edition, April 1974, reprinted in TRADE/WP.4/INF.63, annex II/I, TD/B/FAL/INF.63, annex II/I.

⁵⁶ Standard 2.15 as amended by the Final Act of the Conference of Contracting Governments to amend the annex to the Convention on Facilitation of International Maritime Traffic, 1965 (November 1977), reprinted in TRADE/WP.4/INF.63, annex II/II, TD/B/FAL/INF.63, annex II/II.

⁵⁷ Recommendation (16 June 1981) of the Customs Co-operation Council Concerning the Transmission and Authentication of Goods Declarations which are Processed by Computer, reprinted in TRADE/WP.4/R.148/Add. I.

⁵⁸ TRADE/WP.4/INF.62, para. 22(x), TD/B/FAL/INF.62, para. 22(x).

⁵⁹ TRADE/WP.4/R.148, para. 19.

77. The only international organization which has considered the evidential value of computer records is the Council of Europe. The Committee of Experts charged with studying the problem "came to the conclusion that, in view of the absence of general rules in several states and of the need for such rules because of the development of these practices, it would be useful to reach harmonized solutions in member States which would be justified by the international nature of the problem since documents or copies made in one state were increasingly likely to be presented as evidence in another".⁶⁰

78. As a result of the study conducted by the Committee of Experts, the Committee of Ministers of the Council of Europe, on the recommendation of the European Committee on Legal Co-operation, adopted a Recommendation to its member States which, *inter alia*, provided that each member State should "designate which books, documents and data may be recorded on computers".⁶¹ These records, if made in conformity with the Recommendation, would be admitted as evidence in judicial proceedings and "be presumed to be a correct and accurate reproduction of the original document or recording of the information it relates to, unless the contrary is proven".⁶²

79. The Recommendation of the Council of Europe is a recognition at the international level of the importance to commercial undertakings that the records of their transactions maintained in computers be admissible in evidence and that the international character of many of those transactions, of which international electronic funds transfers are a prime example, requires harmonized solutions to the problems involved.

4. Conclusion

80. International electronic funds transfers are increasingly made through computer-to-computer links. The admissibility in evidence of the records of those transactions is in doubt in some States. Moreover, few States have clear rules on the conditions which must be fulfilled in the preparation of those records for them to be admissible in evidence.⁶³ Where those rules exist, they may not be in harmony, leading to the possibility that the records prepared in accordance with the requirements of one State may not be admissible in litigation arising in another State.

81. The problem, while of particular importance to international electronic funds transfers, is one of general concern for all aspects of international trade. Generalized solutions would, therefore, be desirable.

III. Future work

82. Electronic funds transfer systems have developed in a partial legal vacuum. In many countries it has been assumed that the law relating to paper-based transfers also applies at least in part to electronic funds transfers. However, it is seldom clear to what extent this is the case.⁶⁴ Moreover, the law which was developed for the needs of paper-based funds transfers may not be appropriate in all respects for electronic funds transfers even when the law appears by its terms to apply.

83. The problems arising out of the uncertainty as to the legal rules applicable to electronic funds transfers are much greater when the funds transfer is international. When problems occur, there is no adequate legal framework within which they can be settled.

84. It would seem to be premature, however, to attempt to unify the law in respect of electronic funds transfers at present. Electronic funds transfer systems, especially those based on computer-to-computer transmissions, are still in their infancy. The technology and the associated banking practices are rapidly changing, threatening to make obsolete any new legal rules which might be developed even before they came into force. At the same time it is also foreseeable that electronic funds transfer systems will play a dominant role in international funds transfers in the near future with the increasing participation of the developing countries.⁶⁵

85. What would seem to be needed at this stage of development is a guide to the legal problems arising out of electronic funds transfers. Such a guide would identify the legal issues, describe the various approaches pointing out the advantages and disadvantages of each approach and suggest alternative solutions.

86. Such a legal guide would be of value to all legislative bodies which might contemplate coping with legal problems peculiar to electronic funds transfers or adjusting the current law governing paper-based transfers so as to cover the specific concerns arising out of electronic funds transfers. The guide would also be of value to those who might wish to regulate certain of the legal problems arising out of electronic funds transfers by contractual arrangements between the participants.

⁶⁰ Council of Europe Explanatory Memorandum, note 50 above, at para. 3.

⁶¹ Recommendation No. R (81) 20, appendix, art. 1(1), adopted by the Committee of Ministers on 11 December 1981.

⁶² *Ibid.*, art. 2. As regards the conditions under which computer records would be admissible as evidence, see annex I of this report.

⁶³ For rules in force in the Soviet Union, see document TRADE/WP.4/R.126, reprinted in annex II to this report, which contains rules that the State Arbitration Commission of the USSR has proposed for use by arbitration bodies, and document TRADE/WP.4/R.178, which contains the provisional instructions on the conditions to be observed to confer a legal value to documents established by computer on magnetic tape and on paper.

⁶⁴ The answers to the questionnaire sent out by the Study group in the spring of 1980 were particularly revealing in this regard. No clear pattern as to the general application of the law relating to paper-based funds transfers could be discerned.

⁶⁵ E.g. during 1981 S.W.I.F.T. extended its services to four countries in Latin America, Chile, Ecuador, Mexico and Uruguay, and was in the process of doing so in another three, Argentina, Brazil and Colombia.

87. If the Commission agrees that it should prepare a legal guide, it may wish to request the Secretariat, in consultation with the UNCITRAL Study Group on International Payments, to prepare a draft of a chapter on questions arising in the context of finality of payment and of a chapter concerning questions relating to responsibility as well as a checklist of other basic legal issues which should be borne in mind in the conduct of electronic funds transfers. Should the Commission so agree, the Secretariat will ensure that the views of banks and trade associations from all regions of the world are adequately reflected in the draft.

88. Harmonized rules as to the conditions under which computer records must be produced to be admissible as evidence and the evidential value of computer records are necessary to give legal security to international electronic funds transfers. The problem, however, goes beyond electronic funds transfers and concerns all aspects of international trade in which computers might be used. Since rules of evidence are part of the procedural law, and are linked to the rest of the legal structure in a State, uniformity of law would be difficult to attain at present. However, if guidelines are established as to the conditions under which computer records are admitted in evidence, it may influence the legal development in this field. The Commission may, therefore, wish to request the Secretariat to submit to a future session of the Commission a draft of such guidelines.

ANNEX I

Council of Europe recommendation No. R (81) 20;
Adopted 11 December 1981

Appendix

Article 3

1. Reproductions or recordings made under the responsibility of [a commercial undertaking or other person designated by national law] must conform to the following general rules. They must:

(a) Correspond faithfully to the original document or the information to which the recording relates, as the case may be;

(b) Be reproduced or recorded in a systematic way and without gaps;

(c) Be made in accordance with the working instructions, laid down consistently with national law and preserved as long as the preservation of the reproductions or recordings;

(d) Be preserved with care, in a systematic order, and be protected against any alteration.

2. When a document which has been reproduced or has been used for a recording is destroyed, the following particulars must be preserved together with the recording and in the reproduction, if possible, or otherwise with it:

(a) The identity of the persons under whose responsibility the reproduction or recording has been made and of the person effecting it;

(b) The nature of the document;

(c) The place and date of the reproduction or recording;

(d) Any defects observed during the reproduction or recording.

Article 5

1. The following rules shall apply to computer programmes:

(a) The programme write-up, files description and programme instructions must be directly legible and kept carefully up to date under the responsibility of the [commercial undertaking or other person designated by national law];

(b) The documents referred to in (a) above must be preserved in a communicable form for so long a time as the recordings to which they relate.

2. If, for whatever reason, the data recorded are transferred from one computer to another, the [commercial undertaking or other person designated by national law] must establish that there is concordance.

3. The following rules apply to computer systems generally:

(a) The system must contain the safeguards necessary in order to avoid any alteration of the recording;

(b) The system must also make it possible to reproduce at any moment the information recorded in a directly legible form.

ANNEX II

State Arbitration Commission of the USSR

The use as evidence in arbitration matters of documents prepared by computers

(Reproduced from TRADE/WP.4/R.126)

With a view to the standardization of arbitration practice on matters in which documents prepared with the help of computer technology are used as evidence, the State Arbitration Commission of the USSR has proposed that arbitration bodies should apply the following rules:

1. Parties to arbitration are entitled to submit, in substantiation of their claims or objections, documents prepared with the help of a computer. Insofar as they contain information on circumstances relevant to the case, such documents should be generally accepted as written evidence by arbitration bodies. The acceptance, examination and appraisal of such documents should be governed by the general legislation for consideration of economic disputes. The parties may submit to the arbitration body any copy of a document prepared with the help of a computer. Should the original of a document be required for the settlement of the dispute, it must be submitted.

2. For the purpose of determining whether a contractual relationship exists between the parties, an agreement whose terms have been transmitted or established with the help of a computer shall be deemed to have the same status as an agreement concluded in writing.

3. In the settlement of disputes arising with regard to conditions of contracts, it should be borne in mind that contracts may provide for the production of accounts and the addition by parties of penalties by means of a computer. In such a case, the form of the records or other documents to be prepared with the help of the computer must be stipulated in the contract.

4. Parties should be required to ensure that all their documentary evidence prepared with the help of a computer is drawn up in good and due form. The documents should show at what computer centre and on what date they were prepared. That information may be recorded automatically by a computer or added by any other means. Should regulations binding on the parties, or the contract, prescribe that a document prepared with the help of a computer must be signed by the competent authorities, the parties should be asked to submit documents bearing the appropriate signatures.

5. Documents prepared with the help of a computer and sub-

mitted to an arbitration body as evidence must be so set out that their contents can be clearly understood. They must bear the appropriate inscriptions, column and paragraph headings etc.

6. When they contain handwritten corrections, documents prepared with the help of a computer must show the reasons for the corrections, the date they were made and the signature of the official who made them.

7. Should the arbitration body order the checking of accounts, the party which has submitted as evidence documents prepared with the help of a computer must make it possible for the other party to

carry out the checking and must, if necessary, arrange for it to be done in the relevant computer centre.

8. In cases of need, an arbitration body shall be entitled to appoint, on its own initiative or at the request of the parties, an expert body to review questions connected with the verification of the accounting programme in the computer centre.

9. Electronically-stored data (kept on magnetic tape, magnetic discs etc.) may be used as evidence for the purposes of the case only when converted into a form suitable for general comprehension and conventional file storage.

III. INTERNATIONAL COMMERCIAL ARBITRATION

A. Report of the Working Group on International Contract Practices on the work of its third session (New York, 16-26 February 1982) (A/CN.9/216)*

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Introduction

1. At its fourteenth session, the United Nations Commission on International Trade Law entrusted to the Working Group on International Contract Practices a new mandate which relates to the field of international commercial arbitration. This mandate is laid down in the following decision adopted by the Commission at that session:

"The Commission

"1. Takes note of the report of the Secretary-General entitled 'Possible features of a model law on international commercial arbitration' (A/CN.9/207)**;

"2. Decides to proceed with the work towards the preparation of a draft model law on international commercial arbitration;

"3. Decides to entrust this work to its Working Group on International Contract Practices with its present composition;

"4. Requests the Secretary-General to prepare such background studies and draft articles as may be required by the Working Group."¹

2. The Commission also decided that in preparing a draft model law the conclusions reached by it should be taken into account, in particular, that the scope of application be restricted to international commercial arbitration and that due account be taken of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) and of the UNCITRAL Arbitration Rules.² The Commission was agreed that the above report of the Secretary-General (A/CN.9/207) setting forth the concerns, purposes and possible contents of a model law would provide a useful basis for the preparation of a model law.

3. The Working Group consists of the following States members of the Commission: Austria, Czechoslovakia, France, Ghana, Guatemala, Hungary, India, Japan, Kenya, Philippines, Sierra Leone, Trinidad and Tobago, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America.

4. The Working Group held its third session at United Nations Headquarters from 16 to 26 February 1982.³ All

* Yearbook . . . 1976, part one, II, A, para. 57.

² *Ibid.*, para. 65, and report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 81 (Yearbook . . . 1979, part one, II, A).

³ At its first two sessions, the Working Group considered the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.

* 23 March 1982. For consideration by the Commission see Report, chapter IV, B.

** Yearbook . . . 1981, part two, III.

¹ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 70 (Yearbook . . . 1981, part one, A).

the members of the Working Group were represented except Ghana.

5. The session was attended by observers from the following States: Australia, Brazil, Burma, Canada, Chile, China, Colombia, Cuba, Cyprus, Ecuador, Egypt, Finland, German Democratic Republic, Germany, Federal Republic of, Greece, Indonesia, Italy, Ivory Coast, Norway, Republic of Korea, Sweden, Switzerland, Thailand, Turkey, Uganda, Venezuela and Yugoslavia.

6. The session was attended by observers from the following international organizations: United Nations Industrial Development Organization, Asian-African Legal Consultative Committee, Commission of the European Communities, Inter-American Juridical Committee, International Chamber of Commerce and International Council for Commercial Arbitration.

7. The Working Group elected the following officers:

Chairman: Mr. I. Szasz (Hungary)

Rapporteur: Mr. J. Skinner-Klee (Guatemala)

8. The following documents were placed before the session:

- (a) Report of the Secretary-General entitled "Possible features of a model law on international commercial arbitration" (A/CN.9/207)*;
- (b) Note by the Secretariat entitled "Possible features of a model law on international commercial arbitration: Questions for discussion by the Working Group" (A/CN.9/WG.II/WP.35)**; and
- (c) Provisional agenda of the session (A/CN.9/WG.II/WP.34).

9. The Working Group adopted the following agenda:

- 1. Election of officers
- 2. Adoption of the agenda
- 3. Consideration of possible features of a draft model law on international commercial arbitration to be prepared by the Working Group
- 4. Other business
- 5. Adoption of the report

Deliberations and decisions

10. The Working Group commenced its work of preparing a draft model law on international commercial arbitration by a preliminary exchange of views on the questions contained in the note by the Secretariat (A/CN.9/WG.II/WP.35).^{*} The deliberations and decisions on the questions considered (questions 1-1 to 6-5) are set forth below.

11. The Working Group decided to continue, at its next session, its exchange of views on the questions not yet

considered (questions 6-6 to 6-9) and then to consider the draft provisions and studies which the Secretariat would prepare in accordance with the conclusions reached by the Group at the present session.

12. The Working Group expressed the view that in order to expedite the work, it was desirable to hold two sessions of the Working Group each year. The Working Group noted that the Commission at its fourteenth session had envisaged such a need, but had postponed to its fifteenth session (New York, 26 July to 6 August 1982) a final decision on whether there should be a further session of the Working Group in 1982. The Working Group decided, subject to the approval of the Commission, to hold its next session from 4 to 15 October at Vienna.

Consideration of possible features of a draft model law on international commercial arbitration

13. The Working Group considered the possible features of a draft model law on international commercial arbitration. The Working Group based its deliberations on a report of the Secretary-General (A/CN.9/207, hereinafter referred to as "the report")^{*} and on a note by the Secretariat (A/CN.9/WG.II/WP.35, hereinafter referred to as "the working paper")^{**} setting forth questions for discussion by the Working Group.

A. CONCERNS AND PRINCIPLES OF A MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION

14. The Working Group considered the concerns which should be met by the model law and the principles which should underlie it as set forth in paragraphs 9 to 27 of the report. After hearing general statements from several delegations emphasizing the value of the project, the Group expressed its agreement with the analysis of the concerns and principles set forth in the report.

B. IDENTIFICATION OF ISSUES POSSIBLY TO BE DEALT WITH IN THE MODEL LAW

15. The Working Group considered these issues using the list of questions set forth in the working paper.

I. Scope of application

1. "Arbitration"

Question 1-1: Should the model law expressly state that it applies to institutional as well as *ad hoc* arbitration?

* Yearbook ... 1981, part two, III.

** Reproduced in this volume, part two, III, B.

* Yearbook ... 1981, part two, III.

** Reproduced in this volume, part two, III, B.

Question 1-2: Apart from the clarification referred to in question 1-1, should the model law contain a definition of the term "arbitration"?

16. There was general agreement that the model law should apply to *ad hoc* and institutional arbitration. However, it was felt that the terms *ad hoc* arbitration and institutional arbitration were not easily defined, and that accordingly no attempt should be made to give definitions of those terms in the model law. The Working Group concluded that the model law should have a wide scope of application, and should indicate that it covered all forms of arbitration.

17. It was agreed, however, that certain forms of arbitration should fall outside the scope of the model law. For example, since the model law is designed for consensual arbitration, i.e. arbitration based on voluntary agreement of the parties, it should not cover compulsory arbitration. Furthermore, the various types of free arbitration, noted in paragraph 29 of the report,* should not be covered. However, such limitations in scope need not necessarily be expressed in the model law. An appeal could be made to States to incorporate such limitations when adopting the model law. The Group concluded that a definition of the term "arbitration" was unnecessary.

18. In the context of that discussion, it was observed that the answers to the questions considered by the Group might depend on the final form of the draft text to be prepared by the Working Group, e.g., model law or convention. The Working Group noted that the task entrusted to it by the Commission was to prepare a draft model law, and decided that, if it wished to make any recommendations as to the final form of the text prepared by it, it would do so after having completed its consideration of the possible features of the model law.

2. "Commercial"

Question 1-3: Should the term "commercial" be defined in the model law?

19. There was general agreement that the term "commercial" should be given a wide meaning in order to meet the concern that, in certain legal systems, the term might be construed in an unduly restrictive manner. The Working Group noted the difficulty of devising a clear-cut formula for defining that aspect of the scope of application of the model law. Various suggestions were made for possible elements of an appropriate formula, including (international) "trade", "commerce" and "economic transactions". It was also suggested that for different language versions, different terms might be used to ensure that the term "commercial" would have a wide meaning. It was also suggested that the wide scope to be given to the term "commercial" might be indicated by excluding arbitration of certain disputes (e.g. labour disputes) from the scope of the law.

* Yearbook . . . 1981, part two, III.

3. "International"

Question 1-4: Would it be sufficient to refer simply, i.e. without definition, to the international nature of the commercial matter in dispute (or of the arbitration agreement)?

Question 1-5: If a definition is desirable, should one formula (e.g., parties from different States) be adopted for all phases covered by the model law?

20. There was general agreement that it would not suffice for the model law to refer simply, without definition, to the international nature of the commercial matter in dispute. The criterion of the international nature of the matter in dispute would determine whether in a given case the special regime embodied in the model law would govern, or whether the rules for strictly domestic arbitrations would apply. As to how the definition should be formulated, there was general agreement that the definition contained in the European Convention (Geneva 1961) formed a good starting point. The details of the definition might be aligned to the corresponding definition used in the Vienna Sales Convention of 1980.*

21. It was agreed that further consideration should be given to the possibility of expanding the scope of application of the model law, by adding to the situations covered by the definition of the international nature of a dispute (parties from different States) other cases (e.g. where a contract is to be performed outside the country in which both parties are resident, or where property in dispute is situated outside such country). Such expansion might either be reflected in the definition contained in the model law, or it could be left to the decision of States when adopting the model law to expand the scope of the definition.

II. Arbitration agreement

1. Form, validity and contents

Question 2-1: Is it sufficient to require (as, e.g., article II of the 1958 New York Convention) only one arbitration agreement irrespective of whether it concerns existing or future disputes or should some additional act be envisaged in certain cases?

22. There was general agreement that the model law should require only one arbitration agreement irrespective of whether it concerned existing or future disputes. This solution is in conformity with that adopted in article II, paragraph 1, of the 1958 New York Convention.

Question 2-2: Should the model law specify the required form of the arbitration agreement and, if so, require that it be "in writing"?

Question 2-3: If writing were required, should the term "in writing" be defined, for example, as in article II

* Yearbook . . . 1980, part three, I, B.

of the 1958 New York Convention ("agreement signed by the parties or contained in an exchange of letters or telegrams") or should a more extensive and refined definition be sought which should reduce the difficulties encountered in practice with the above definition (see report, paragraph 43)?*

23. The Working Group was agreed that the model law should require the arbitration agreement to be in writing, and that this formal requirement should be defined along the lines of article II, paragraph 2 of the 1958 New York Convention. It was suggested that the model law give a more detailed definition than the one in article II, paragraph 2 of the 1958 New York Convention, so as to make clear that it encompasses, for example, modern means of communication and frequently used contract practices, e.g., use of standard form contracts or reference to general conditions. In the preparation of such a detailed definition, it was suggested that article I, paragraph 2 (a) of the European Convention (Geneva 1961) might be taken into account.

24. In this connection, the question was raised whether a party which had appeared before an arbitral tribunal without contesting its jurisdiction, may later invoke the lack of a written arbitration agreement. The prevailing view was that such a party could not in those circumstances invoke the lack of a written agreement. However, it was agreed that the question should not be dealt with in the model law, as it was a question which could be adequately dealt with by domestic law.

Question 2-4: Which points relating to the validity of the arbitration agreement should be included in the model law? For example, should a provision be included guaranteeing equality of the parties as regards the appointment of arbitrators (see report, paragraph 44)?*

25. There was general agreement that the model law should not set forth grounds for the invalidity of an arbitration agreement, including grounds specially directed to arbitration agreements. It was noted that the formulation of an exhaustive list of clearly defined grounds was extremely difficult. Consequently, the question of validity should be left to the applicable law. The Group noted that, in view of this decision, the question whether the model law should include rules to determine which law was applicable assumed greater importance. The Group decided to consider this question, together with other questions as to the conflict of laws, at a later stage.

Question 2-5: What should be the minimum contents of an arbitration agreement? For example, would a provision like article II, paragraph 1 of the 1958 New York Convention be appropriate and sufficient (see report, paragraphs 46-47)?*

26. The Working Group was agreed that the model law should state the minimum contents of an arbitration agreement along the lines of article II, paragraph 1 of the 1958 New York Convention, since that provision was appropriate and sufficient. However, doubts were expressed as to the appropriateness of adopting the last part of that provision (i.e. "concerning a subject matter capable of settlement by arbitration"). It was noted that this requirement related to the domain of arbitration, which was dealt with separately (question 2-9). The Group decided to defer its decision on whether to retain that phrase until after it had considered and decided the issue of the domain of arbitration.

2. Parties to the agreement

Question 2-6: Should the model law contain a provision on who may be a party to an arbitration agreement?

Question 2-7: If so, should the model law state, for example, that it applies to "arbitration agreements concluded by physical or legal persons of private or public law" or should a provision be added according to which even "legal persons of public law have the right to conclude valid arbitration agreements" (as, e.g., article II, paragraph 1 of the 1961 Geneva Convention)?

27. There was general agreement that access to arbitration should be unrestricted. However, divergent views were expressed as to how to achieve this end. Under one view, this purpose would best be served by not incorporating in the model law any provision on who might be party to an arbitration agreement. Under another view, it was preferable to state expressly in the model law that it applied to arbitration agreements concluded by physical persons or legal persons of private or public law. The Working Group decided to reconsider the matter in the light of a draft provision to be prepared by the Secretariat.

28. The Working Group noted that this question was to be clearly distinguished from the question whether a given person had the legal capacity to conclude an arbitration agreement. The Group decided that the question of capacity fell outside the scope of the model law, and that therefore no provision as, for example, article II, paragraph 1 of the 1961 Geneva Convention should be included.

Question 2-8: Should an attempt be made to deal in the model law with certain aspects of State immunity in the area of international commercial arbitration? For example, to mention only one out of many possibilities, should the model law construe the commitment to arbitrate by a Government or a State organ as containing an implied waiver of any right to invoke State immunity in the arbitration proceedings or arbitration-related court proceedings?

29. There was general agreement that the model law should not deal with questions of State immunity. The reason for this decision was that the issue of State immunity in

* Yearbook ... 1981, part two, III.

the context of arbitration was regarded as but a part of a more general and complex problem having an obviously political and public international law character.

3. *Domain of arbitration*

Question 2-9: Should the model law set forth a list of non-arbitrable subject matters, either as an exhaustive list or as an open list to be supplemented by the respective State, or would it be sufficient to express the restrictions merely by reference to "international public policy?"

30. There was general agreement that the model law should not set forth a list of non-arbitrable subject matters, either as an exhaustive list, or an open list to be supplemented by the State concerned. It was felt that it would be impracticable to compile an exhaustive list, and that provision for an open list would not further the cause of harmonization. It was also agreed that it would not be appropriate and sufficient to merely refer to "international public policy", as that term was not sufficiently precise.

31. The prevailing view was that the model law should not contain a provision delimiting non-arbitrable issues. However, it was noted that further thought could be given to the possibility of devising a general formula to determine non-arbitrability along the following lines — a subject matter is arbitrable if the issues in dispute can be settled by agreement of the parties.

Question 2-10: Should the model law deal with the "true filling of gaps" and, if so, should a special authorization by the parties be required or should it treat this task as lying outside the arbitrator's competence even where parties have given such special authorization?

Question 2-11: Should the arbitral tribunal be empowered to adapt a contract without special authorization by the parties or only if the parties have given such authorization?

32. The Working Group noted that the issues noted in questions 2-10 and 2-11 were of a complex nature. During the deliberations, the following matters were referred to. There was some uncertainty as to the scope of the function of filling of gaps, and in what way it differed from the function of adaptation of contracts (question 2-11). For example, it was not immediately clear what constituted a gap, and it was noted that the function of filling of gaps encompassed a variety of fact situations which should be distinguished. In each of those situations, different solutions might be envisaged as to the competence of the arbitral tribunal, and as to the legal status and enforceability of its decisions. In this regard, disparities existed between different legal systems.

33. Accordingly, the Working Group requested the Secretariat to prepare a study analysing the issues considered.

4. *Separability of arbitral clause*

Question 2-12: Should the model law adopt the principle of separability or autonomy of the arbitral clause?

34. There was general agreement that the model law should adopt the principle of separability or autonomy of the arbitral clause, as embodied in article 21 of the UNCITRAL Arbitration Rules.*

5. *Effect of the agreement*

Question 2-13: Should the model law contain a provision along the lines of article II, paragraph 3 of the 1958 New York Convention (report, paragraph 59).** Should it contain supplementary provisions on what points a court should examine and what type of decision it may render?

35. There was general agreement that the model law should contain a provision similar to article II, paragraph 3 of the 1958 New York Convention. It was noted that this provision was based on the assumption that an arbitration agreement was to exclude the jurisdiction of courts (whether or not it so stated).

36. As regards the question whether the model law should contain a provision concerning the type of decision the court should render when the arbitration agreement was invoked, a view was expressed that the model law might determine whether the court action should be stayed or dismissed. However, the Working Group agreed that the matter should be left to be determined by the court according to its procedural law.

Question 2-14: Should the model law deal with problems of consolidation in multi-party disputes (e.g. whether consolidation agreements should be given effect, or whether even without such agreements consolidation might be ordered)?

37. There was general agreement that the model law should not deal with problems of consolidation in multi-party disputes. While it was agreed that parties had the freedom to conclude consolidation agreements if they so wished, the Working Group was of the view that there was no real need to include a provision on consolidation in the model law.

Question 2-15: Should a stipulated time-period for submission of a dispute to arbitration be effective even if it would expire before a prescription period applicable to the underlying transaction which may not be shortened by the parties?

38. The Working Group was agreed that the effectiveness of a stipulated time period for submission of a dispute to arbitration was independent of any prescrip-

* Yearbook . . . 1976, part one, II, A, para. 57.

** Yearbook . . . 1981, part two, III.

tion period concerning the underlying transaction. Accordingly, even a mandatory prescription period would not affect the stipulation of a shorter time-period for arbitration. The Group was of the view that the model law should not include a provision on this point, nor on related issues (such as the right of a party to resort to a court after expiry of that time-limit, or any effect on the prescription period). The solution to these issues would vary according to the specific circumstances of the case.

Question 2-16: Are pre-arbitration attachments and similar court measures of protection compatible with an arbitration agreement and should the model law state so?

39. There was general agreement that the resort by a party to a court in order to obtain interim measures of protection was not incompatible with an arbitration agreement, and that the model law should contain a statement to that effect. Such relief was normally sought before the arbitration had started, but it was agreed that the principle of compatibility should also prevail during arbitration proceedings. The Working Group noted that this latter issue was linked to the issues set forth in questions 4-10 and 4-11 (interim measures by arbitral tribunals or by courts). It was suggested that in drafting an appropriate provision, account should be taken of article 26, paragraph 3 of the UNCITRAL Arbitration Rules,* article VI, paragraph 4 of the 1961 Geneva Convention; and article 4 (2) of the 1966 Strasbourg Uniform law.

6. Termination

Question 2-17: Should the model law specify certain circumstances under which an arbitration agreement would be terminated (e.g. settlement on agreed terms; expiry of time-limit for making award) or would not be terminated (e.g. death of one party)?

40. The Working Group was of the view that instances which could conceivably terminate the arbitration agreement were often also relevant in the context of the procedure of arbitration, and that these instances could only be fully considered in the light of its later discussion on arbitral procedure. The Working Group requested the Secretariat to prepare a study on the issues relevant to termination, but only on those which were peculiar to arbitration.

III. Arbitrators

1. Qualifications

Question 3-1: Should the model law expressly state that foreign nationals shall not be precluded from acting

as arbitrators (cf., e.g., article 2 of the 1966 Strasbourg Convention, report, paragraph 64)?*

41. There was general agreement that parties should be free to choose arbitrators of any nationality. Different views were expressed as to how best to achieve the goal that foreign nationals are not precluded from acting as arbitrators. Under one view, the model law should state the above fundamental principle in a positive form. Under another view, silence could achieve the same result. It was agreed that the issue should be decided at a later stage after the Secretariat had prepared a draft text.

Question 3-2: Are the qualifications required of arbitrators an appropriate matter to be dealt with in the model law?

42. The Working Group was agreed that it was extremely difficult to deal in the model law with the varied qualifications required of arbitrators. Accordingly, the prevailing view was that the model law should not deal at all with the question of qualifications. However, under another view it was desirable to incorporate a general formula, as, for example, contained in article 9 of the UNCITRAL Arbitration Rules* (impartiality and independence). It was observed in this connection that this question was linked to the grounds on which an arbitrator may be challenged. The Working Group requested the Secretariat to prepare a study on these questions, and deferred a decision pending the submission of this study.

2. Challenge

Question 3-3: Should the model law deal with the grounds on which an arbitrator may be challenged? If so, should it list these grounds or would a general formula suffice?

Question 3-4: As regards the procedure of challenging an arbitrator, should the model law recognize any agreement of the parties thereon even if it would exclude (last) resort to a court?

Question 3-5: Should supplementary rules be included for those cases where parties have not regulated the challenge procedure?

Question 3-6: Should the model law adopt ancillary rules on disclosure and on restrictions to the right to challenge along the lines of articles 9 and 10 (2) of the UNCITRAL Arbitration Rules* and article 12 (2) of the 1966 Strasbourg Uniform Law (report, paragraph 66)?

43. The Working Group was agreed that the model law should deal with the grounds on which an arbitrator may be challenged only in the same general manner as it dealt with the qualifications of an arbitrator. It was suggested that a draft provision be prepared using the same formula (impartiality and independence). It was agreed that such

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1976, part one, II, A, para. 57.

general provision should form the sole basis for challenging an arbitrator. The Working Group was also agreed that the model law should contain a provision requiring a prospective arbitrator to disclose circumstances which could create doubts as to his impartiality or independence. The Working Group was agreed that this provision should be modelled on article 9 of the UNCITRAL Arbitration Rules.*

44. It was generally agreed that, as regards the procedure for challenging an arbitrator, stipulations of the parties regulating the procedure should be recognized by the model law. However, there was no agreement on whether a last resort to courts could be excluded by such stipulations. Under one view, the final decision on a challenge should always lie with a court. Under another view, the freedom of parties to agree on the procedure of challenge was to be recognized, but resort to courts should be provided in cases where the stipulated procedure led to a deadlock. It was noted that such resort could also be provided for during the arbitration proceedings (in order to avoid delays in these proceedings through a speedy court decision on the challenge), or incorporated in those procedures which provided to a party recourse against an award (where an alleged ground for challenge would constitute a reason for attacking the award). The Working Group agreed that this question needed further consideration. The Working Group requested the Secretariat to prepare a study on these issues.

45. Divergent views were expressed as to whether the model law should set forth supplementary rules for those cases where parties had not themselves regulated the challenge procedure. Under one view, it was not in accordance with the purpose of a model law to incorporate detailed rules on such a procedural issue. Under another view, it would be useful if the model law would set forth a mechanism for challenge in order to avoid protracted controversy and delay in the arbitration proceedings. The Secretariat was requested to include in its study on the issue of challenge the question of what supplementary rules might be appropriate.

3. Number of arbitrators

Question 3-7: Should the model law contain any mandatory provision on the number of arbitrators?

Question 3-8: Should supplementary rules be included for those cases where parties have not agreed on the number?

46. There was general agreement that the model law should not contain any mandatory provision specifying the number of arbitrators. It was suggested that thought might be given to expressly stating in the model law the principle of the freedom of the parties to determine the number of the arbitrators.

47. There was also general agreement that the model law should contain a supplementary rule for those cases where the parties had not agreed on the number, or on a mechanism for determining that number. Several views were expressed as to which number the model law should specify. The prevailing view was that the model law provide for three arbitrators, which would accord with article 5 of the UNCITRAL Arbitration Rules.* Another view was that in view of the frequency of multi-party arbitrations, it would be appropriate to allow each party to appoint one arbitrator, and for those cases where the result was an even number of arbitrators, to provide for one additional arbitrator. Yet another view was that the model law envisage arbitration by a sole arbitrator. In this context, a further supplementary rule was suggested for those cases where parties had agreed on arbitration by two arbitrators but where these two could not reach a decision. In order to avoid such a deadlock, the model law might envisage appointment of a third arbitrator (or an umpire).

48. The Working Group noted that the question of the number of arbitrators was linked with the question of the appointment procedure (questions 3-9 and 3-10) and decided to defer its decision on which number to include in the model law.

4. Appointment of arbitrators (and replacement)

Question 3-9: Should the parties be free to determine the appointment procedure, provided that equality is ensured?

Question 3-10: Should supplementary rules be adopted for cases where the appointment procedure, or a certain feature thereof, has not been agreed upon by the parties?

49. There was general agreement that the parties should be free to determine the procedure for appointing the arbitrator(s). Different views were expressed as to whether a provision in the model law recognizing such freedom of the parties should contain a restriction such as "provided that equality is ensured". The prevailing view was that the principle of equality of the parties need not be stated in such a provision. This was in accordance with the position which the Working Group had taken when discussing possible grounds for invalidity of an arbitration agreement, in particular the question whether an arbitration agreement which gave one party a privileged position with regard to the appointment of the arbitrators would be invalid (question 2-4). Under another view, it was desirable to express the principle of equality of the parties, despite its generality, in the model law in order to prevent a stronger party from abusing his position.

50. The Working Group was agreed that the model law should set forth supplementary rules for those cases where the parties had not agreed upon the appointment procedure.

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1976, part one, II, A, para. 57.

However, different views were expressed as to how detailed such supplementary provisions should be. Under one view, it sufficed to include a provision which merely stated that the appointment was to be made by an appointing authority (which would be designated by each State when adopting the model law). Under another view, it was desirable to incorporate a more elaborate system, for example, as embodied in articles 6 to 8 of the UNCITRAL Arbitration Rules.* An additional proposal was to include a rule on the replacement of an arbitrator (as for example, article 13 of the UNCITRAL Arbitration Rules*).

5. Liability

Question 3-11: Would it be appropriate for the model law to deal with questions relating to the liability of arbitrators?

51. There was general agreement that the question of the liability of an arbitrator could not appropriately be dealt with in a model law on international commercial arbitration. It was also agreed not to attempt the preparation of a code of ethics for arbitrators.

52. In connection with this issue, the Working Group considered whether the model law should contain any rule on the basic duties of arbitrators and of possible effects of the breach of such duties on the course of the arbitral proceedings. The prevailing view was to envisage the replacement of an arbitrator "if he failed to act" (article 13, paragraph 2 of the UNCITRAL Arbitration Rules*). Under another view, the reasons for replacement should be more widely stated so as to include, for example, any conduct which was not in accordance with the instructions of the parties, or was not of an impartial, proper and speedy character.

IV. Arbitral procedure

1. Place of arbitration

Question 4-1: Should the model law recognize the parties' freedom to determine the place of arbitration or to empower a third person to make that determination?

Question 4-2: In the absence of any agreement envisaged in question 4-1, should the model law empower the arbitral tribunal to determine the place of arbitration?

53. There was general agreement that the model law should contain a supplementary rule empowering the arbitral tribunal to determine the place of arbitration where freedom to authorize a third person or body (for example, the arbitral tribunal or a permanent arbitral institution) to determine the place of arbitration.

54. There was general agreement that the model law should contain a supplementary rule empowering the arbit-

ral tribunal to determine the place of arbitration where the parties had not agreed upon that place. It was suggested that such a provision should be modelled on article 16, paragraph 1 of the UNCITRAL Arbitration Rules,* with a possible modification of the last part of that provision ("having regard to the circumstances of the arbitration").

55. In this connection, the view was expressed that supplementary rules along the lines of article 16, paragraph 2 second sentence, paragraphs 3 and 4, might be appropriate, but that these provisions related to issues (arbitral procedure and award) to be discussed later.

2. Arbitral proceedings in general

Question 4-3: Should the model law expressly empower the arbitral tribunal to conduct the proceedings as it deems appropriate and, if so, what restrictions should be laid down?

56. There was general agreement that the arbitral tribunal should be empowered to conduct the arbitration as it considered appropriate, subject to the instructions of the parties, provided that the parties were treated with equality and that at every stage of the proceedings each party was given a full opportunity of presenting his case. It was agreed that such a provision, modelled after article 15, paragraph 1 of the UNCITRAL Arbitration Rules,* should be mandatory.

57. The Working Group was agreed that the model law should contain procedural provisions along the lines of article 15, paragraphs 2 and 3 of the UNCITRAL Arbitration Rules,* subject to the later decision of the Working Group on the general question as to what extent the model law should include supplementary procedural rules for those cases where parties had not agreed on the procedure. Divergent views were expressed as to whether the above provisions, if they were to be included, should be mandatory or not. The Working Group deferred its decision on that point and requested the Secretariat to draft a provision for consideration by it.

Question 4-4: As a general question which is also relevant to the following issues, it may be asked to what extent the model law should include supplementary rules on the arbitral procedure as usually contained in arbitration rules?

58. The Working Group discussed the general question as to what extent the model law should contain supplementary rules on arbitral procedure. It was noted that the purpose of such rules was to assist in those cases where parties had not agreed on the procedure, whether by reference to arbitration rules or in their arbitration agreement itself. It was also noted that not only those States whose arbitration law was less developed, but also all other States could benefit from the preparation of a model law since this law would

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1976, part one, II, A, para. 57.

lay down widely acceptable rules specifically adapted to international commercial arbitration. Therefore, an attempt should be made to devise a set of rules which would allow the commencement and functioning of arbitration proceedings even where parties had not made the necessary provision in their agreement. However, it was agreed that, for reasons of practicability, a decision on whether supplementary rules were appropriate could only be made with regard to each individual subject matter.

3. Evidence

Question 4-5: Should the arbitral tribunal be empowered to adopt its own rules on evidence, subject to contrary stipulation by the parties?

Question 4-7: What supplementary rules would be appropriate?

59. There was general agreement that the model law should empower the arbitral tribunal to adopt its own rules on evidence subject to contrary stipulation by the parties. It was noted that this view was in accordance with the decision concerning question 4-3, and that the question of evidence was an inherent and important part of the conduct of proceedings.

60. The Working Group was agreed that the model law should not contain any supplementary rule which would restrict the arbitral tribunal's power to adopt its own rules on evidence. Not only was such a restriction undesirable, but it was also extremely difficult to envisage detailed rules on evidence in view of the great disparity between legal systems. Accordingly, if a rule were to be adopted, it should be one supporting the power of the arbitrator, such as article 25, paragraph 6 of the UNCITRAL Arbitration Rules* ("The arbitral tribunal shall determine the admissibility, relevance, materiality and weight of the evidence offered").

Question 4-6: What kind of court assistance may be envisaged in enforcing procedural decisions of the arbitral tribunal, e.g. calling of a witness, taking of evidence?

61. There was general agreement that assistance by courts in enforcing procedural decisions of the arbitral tribunal could contribute to the proper and efficient functioning of international commercial arbitration. However, divergent views were expressed as to whether this issue of court assistance should be dealt with in the model law. Under one view, it should be possible to draft an appropriate provision which would envisage such court assistance, either in a general form or in a detailed manner. Under another view, such an approach was not feasible in view of the following difficulties and concerns:

(a) The procedures of such court assistance formed an integral part of the procedural law of the legal system concerned, and the relevant procedural laws varied considerably from one legal system to another;

(b) Where such court assistance was required in a country other than the one where the arbitration took place, the model law might not be able to secure such assistance. It was noted in this context that such assistance by foreign courts was normally governed by bilateral or multilateral treaties which, however, primarily covered matters which were the subject of court litigation;

(c) Assistance by courts would require a certain supervision by the courts over the arbitral tribunal as regards the justification for the tribunal's decision, since automatic court assistance would open the possibility of abuse of court process.

62. The Working Group concluded that the issue required further study, and requested the Secretariat to prepare a note taking into account the views expressed and suggestions made during the deliberations.

4. Experts

Question 4-8: Should the arbitral tribunal be empowered to appoint experts *ex officio*, unless the parties have agreed otherwise?

Question 4-9: What supplementary rules are appropriate, e.g. on the expert's terms of reference or on the parties' rights and obligations in respect of the expert's performance of his task (cf., e.g. article 27 of the UNCITRAL Arbitration Rules*)?

63. There was general agreement that the arbitral tribunal should be empowered to appoint experts *ex officio* even if the parties had not expressly authorized it to do so. However, divergent views were expressed as to whether this power could be excluded by a stipulation of the parties. Under one view, parties who had submitted a dispute to arbitration should not have the power to preclude the arbitral tribunal from *ex officio* calling an expert if that was needed for deciding the dispute. The prevailing view, however, was that the parties could at any stage of the proceedings preclude the arbitral tribunal from calling an expert without their agreement. It was noted that this issue was to be distinguished from the question whether a party could present the evidence of an expert witness. The Working Group was agreed that the arbitral tribunal should hear such expert witnesses as provided for in article 15, paragraph 2 of the UNCITRAL Arbitration Rules.*

64. The Working Group was also agreed that it was worthwhile to consider the feasibility of including in the model law some supplementary provisions of the type embodied in article 27 of the UNCITRAL Arbitration Rules.* It requested the Secretariat to prepare draft provisions for its consideration.

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1976, part one, II, A, para. 57.

5. *Interim measures of protection*

Question 4-10: Should the arbitral tribunal be empowered to take interim measures of protection even without special authorization by the parties?

65. The Working Group was of the view that the arbitral tribunal should have the power to take certain interim measures of protection. However, divergent views were expressed as to the scope of, and conditions to be attached to, such power.

66. As regards the scope, under one view the rule of the model law should be in accordance with article 26, paragraph 1 of the UNCITRAL Arbitration Rules.* The prevailing view, however, was that the scope should be more restrictively defined, either by limiting the power of the arbitral tribunal to those measures which the parties should or could themselves take, or by listing the specific permissible measures (e.g. conservation of goods, sale of perishable merchandise). In this connection, it was also noted that provisions concerning the duties of parties to preserve merchandise which are contained in the law applicable to the substance of the dispute may have some influence on the measures which the arbitral tribunal might take. A further possible restriction was to empower the arbitral tribunal only to order such conservation measures, but not to take them itself.

67. The Working Group was divided on whether the arbitral tribunal should be empowered to take interim measures of protection only upon authorization by both parties (including reference by the parties to arbitration rules setting forth such authorization, as e.g. article 26, paragraph 1 of the UNCITRAL Arbitration Rules*) or whether, failing such agreement, a request by one party sufficed. The Working Group deferred its decision on this question.

Question 4-11: Should the model law deal with the involvement of courts in this respect?

68. The Working Group reaffirmed the decision which it had taken in relation to question 2-16 (see above, paragraph 39). Under that decision, the model law should contain a provision along the lines of article 26, paragraph 3 of the UNCITRAL Arbitration Rules.* The principle of compatibility embodied therein would apply to resort to courts for interim measures before and during arbitration proceedings.

69. The Working Group was agreed, apart from such provision on compatibility, the model law should not contain any rule dealing with the involvement of courts in taking any interim measure of protection. As regards interim measures which only a court take (e.g. attachment or seizure of assets or those measures affecting third parties), it was thought that these were an integral part of the general procedural law applied by the court. As regards

interim measures which an arbitral tribunal might take (cf. paragraph 66 above), it should be left to the domestic procedural law to determine whether such measures could be enforced. It was suggested that parties who wanted enforceable measures of protection should directly resort to the courts. It was further noted that the legal justification and consequences of an interim measure taken by the arbitral tribunal were linked to issues to be discussed later, such as recourse against arbitral decisions and the effect of an (interim) award.

6. *Representation and assistance*

Question 4-12: Would it be appropriate for the model law to deal with questions relating to representation and assistance?

70. There was general agreement that parties may be represented or assisted by persons of their choice. Divergent views were expressed as to whether the model law should contain a provision to that effect. The prevailing view was that there was no real need to express such a principle, which seemed to be widely recognized. Under another view, it was desirable for the model law to reaffirm this principle, which included a party's right to be represented by counsel. There was support for the suggestion to include a provision according to which a party, if it intended to be represented by counsel, had to notify the other party thereof in advance.

7. *Default*

Question 4-13: If one of the parties fails to participate, would the arbitral tribunal be empowered to go ahead with the proceedings and make a binding award even without special authorization by the parties, including reference to arbitration rules which allow the arbitral tribunal to do so? If such special authorization were to be required, should the model law expressly recognize it as being effective, subject to any restrictions envisaged under question 4-14?

71. There was general agreement that, in principle, the arbitral tribunal should be empowered to continue the proceedings even if one of the parties fails to communicate his statement or to appear at a hearing. However, divergent views were expressed as to whether the model law should conditions for such continuation. Under one view, an attempt should be made to formulate the conditions for such continuation. Minimum requirements for continuing the proceedings and rendering an award in case of such failure would be that the party had been given due advance notice (possibly also requiring a statement of the legal consequences of default) and that the party had not shown sufficient cause for his failure. Under another view, it was not practical to regulate this issue in the model law, since such regulation might not be readily acceptable in some countries in view of their general position on *ex parte* judgements. If,

* Yearbook ... 1976, part one, II, A, para. 57.

however, there were to be a provision on this issue, one view was that it could provide that a court would decide, in the circumstances of each case, whether *ex parte* proceedings by the arbitral tribunal were permissible. Another view expressed concern over the delay and complications which might result from such court involvement. The Working Group decided to attempt to formulate the conditions that must be met for permitting *ex parte* proceedings, and to request the Secretariat to prepare draft provisions taking into account the suggestions made during the discussion. If such attempt proved to be fruitless, the issue would have to be left for decision to the procedural law of each State.

8. Further issues of arbitral procedure

72. The Working Group was agreed that, in addition to the procedural issues contained in questions 4-1 to 4-14, there were other issues of arbitral procedure possibly to be dealt with in the model law. The issues suggested for consideration were: minimum contents of a statement of claim and statement of defence (cf. articles 18 and 19 of the UNCITRAL Arbitration Rules*); language to be used in arbitration proceedings (cf. article 17 of the UNCITRAL Arbitration Rules*); notice of arbitration (cf. article 3 of the UNCITRAL Arbitration Rules*), and its effects on a prescription period; and termination of arbitral proceedings (cf. article 34 of the UNCITRAL Arbitration Rules*). The Working Group requested the Secretariat to prepare for its consideration draft provisions on these issues, with explanatory notes if appropriate.

V. Award

1. Types of award

Question 5-1: Would it be appropriate for the model law to deal with the different possible types of award (e.g. final, interim, interlocutory, partial)?

73. Divergent views were expressed as to whether the model law should deal with the different possible types of award (e.g. final, interim, interlocutory, partial). Under one view, it was not appropriate for the model law to deal with the above types of awards which were not clearly defined. Under another view, it served no useful purpose merely to list them as possible types of awards which an arbitral tribunal might render; it was necessary in addition to specify the legal qualifications and consequences of the different types, including possible means of recourse and enforceability. The main point in need of clarification was that the making of an interim award would not terminate the mandate of the arbitral tribunal, since there were national legal systems under which this result could ensue. The

Working Group decided to further consider this question on the basis of draft provisions to be prepared by the Secretariat.

2. Making of an award

Question 5-2: Would it be appropriate for the model law to deal with the question of setting a time-limit for the making of the award?

74. There was general agreement that parties were free to stipulate a time-limit for the making of an award, if they so wished. However, it was agreed that the model law should neither set such a time-limit nor deal with the legal consequences of the expiry of a time-limit stipulated by the parties, since in international commercial arbitration the circumstances varied considerably from one case to another.

75. In this context, the Working Group considered whether the model law should deal with the question of undue delay by an arbitrator in conducting the proceedings. It was suggested that a possible legal consequence of such misconduct could be either challenge or replacement of the arbitrator concerned. The Working Group was agreed that it might consider this issue at a later stage.

Question 5-3: Should the model law contain any mandatory provisions on the decision-making process in proceedings with more than one arbitrator? For example, should it require that an award be made by a majority of the arbitrators, provided that all arbitrators had the opportunity to take part in the deliberations leading to that award?

76. The Working Group was agreed that the model law should contain mandatory provisions on the decision-making process in proceedings with more than one arbitrator. In this connection, it was agreed that a provision should be included that, in proceedings with an uneven number of arbitrators, an award shall be made by a majority of arbitrators, provided that all the arbitrators had taken part in the deliberations leading to that award.

77. It was noted that the content of provisions on the decision-making process would be related to the number of arbitrators forming the arbitral tribunal, and it was recalled that the Working Group had concluded that the model law should not contain any mandatory provision specifying the number of arbitrators (question 3-7, above, paragraph 46). It was noted that there were proceedings conducted by an even number of arbitrators and that the practice of appointing an arbitral tribunal consisting of one arbitrator appointed by each party, with an umpire to decide if the two arbitrators failed to agree, was well established in the commercial practice of some countries. It was accepted that provisions on decision-making in the model law should not exclude these practices.

* Yearbook . . . 1976, part one, II, A, para. 57.

3. Form of award

Question 5-4: Should the model law require that the award, which must be in writing, be signed by all arbitrators or should it allow any exception, e.g., require that at least a majority of the arbitrators has signed and the fact of a missing signature of a named arbitrator and the reasons therefor be stated (above the signatures of the other arbitrators)?

Question 5-5: Should the model law require that the date and place of the award be stated therein?

Question 5-6: Should the model law require that the award state the reasons upon which it is based, unless the parties have agreed that no reasons are to be given?

78. There was general agreement that, in the interests of certainty, the model law should require that the award be in writing. As regards the signing of the award by the arbitrators, the model law should include a provision envisaging signature by all the arbitrators. However, provisions should also be included dealing with the cases where, exceptionally, the award was not signed by all the arbitrators (e.g. where one arbitrator was unable or unwilling to sign). Under the prevailing view, in such cases it should be sufficient if a majority of the arbitrators had signed, and that the fact of the missing signature, and the reasons therefor, were stated. Such a solution was found in several national laws, and was in accord with article 32, paragraph 4 of the UNCITRAL Arbitration Rules*. In relation to this issue, it was pointed out that an arbitrator who was unable to sign could authorize another person (e.g., the chairman of the tribunal) to sign on his behalf.

79. There was general agreement that the model law require that the date and place of the award be stated therein. It was noted that the identity of the place of the award might be relevant in enforcement proceedings under the 1958 New York Convention (e.g., article V, 1 (e) – award set aside by a competent authority of the country in which the award was made). If the date and place of the award was not stated therein, however, the prevailing view was that the model law should not on that account declare the award invalid. In this connection, it was noted that this question had also to be considered subsequently in connection with the setting aside or annulment of awards (questions 6-6 *et seq.*). A suggestion was made that thought might be given to formulating a rule under which the award was to be deemed made on the date and at the place indicated therein, even though the award may, for convenience, have been signed in different places and at different times by the arbitrators.

80. There was wide support for the view that the model law should require that the award state the reasons upon which it is based. Such a requirement was found in many national arbitration laws, and would also have a beneficial

influence on the decisions of the arbitrators. Under another view, however, not requiring reasons to be stated also had advantages: the award could be rendered speedily, could not easily be challenged, and was appropriate for certain types of arbitrations (e.g., quality arbitrations). During the deliberations, it was suggested that an acceptable solution might be to require the statement of reasons, but to permit parties to waive this requirement. Such waiver might take place expressly, or even by usage where the arbitration was conducted under rules which did not contemplate the giving of reasons. It was noted that this solution was in accordance with article 32, paragraph 3 of the UNCITRAL Arbitration Rules,* and it received very wide support.

4. Pleas as to arbitrator's jurisdiction

Question 5-7: Should the arbitral tribunal be empowered to decide on any pleas as to its jurisdiction including those based on non-existence or invalidity of an arbitration agreement?

Question 5-8: Should a ruling by the arbitral tribunal on its jurisdiction be final and binding or should it be subject to any review by a court?

81. The Working Group noted that it had decided that the model law should adopt the principle of the separability or autonomy of the arbitral clause (question 2-12, above, paragraph 34). In accordance with that decision, there was general agreement that the model law should empower the arbitral tribunal to decide on any pleas as to its jurisdiction, including those based on non-existence or invalidity of an arbitration agreement. Such a power was also contemplated in article 21, paragraph 1 of the UNCITRAL Arbitration Rules,* and in article V, paragraph 3 of the 1961 Geneva Convention. It was noted that thought might be given to imposing limitations on the stage of the proceedings at which a plea as to jurisdiction might be raised, as provided in article 21, paragraph 3 of the UNCITRAL Arbitration Rules.*

82. There was also general agreement that a ruling by the arbitral tribunal on its jurisdiction is subject to review by a court. It was noted in this connection that both the 1958 New York Convention (article V, paragraph 1 (e)) and the 1961 Geneva Convention (article V, paragraph 3) contemplated the existence of such court review. Divergent views were expressed, however, as to whether provisions on such review should be included in the model law. Under one view, it was impossible to formulate provisions covering the variety of circumstances in which review by courts should take place. Accordingly, the model law should not contain any such provision. Under another view, however, the model law might contain some provisions on this issue. Thus, it might be desirable to include a provision as to the stage at which court review should be permissible following article

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1976, part one, II, A, para. 57.

18 of the uniform law annexed to the 1966 Strasbourg Convention, or article VI, paragraph 3 of the 1961 Geneva Convention. Another suggestion was that provisions might be included empowering the court to compel the continuance of arbitral proceedings, where the arbitral tribunal had ruled that it had no jurisdiction, or to discontinue arbitral proceedings, where the arbitral tribunal had ruled that it had jurisdiction.

83. The Working Group decided that an attempt should be made to formulate provisions on court review, taking into account the discussion which had taken place on the issue, and to reconsider the issue at a later stage.

5. Law applicable to substance of dispute

Question 5-9: Should the model law recognize as binding on the arbitral tribunal an agreement by the parties that the case be decided *ex aequo et bono*? If so, should an attempt be made to define such mandate in the model law (e.g. "*amiables compositeurs*" must observe those mandatory provisions of law regarded in the respective country as ensuring its *ordre public international*)?

84. There was general agreement that the model law should recognize as binding on the arbitral tribunal an agreement by the parties that the case be decided *ex aequo et bono*. It was noted that the term "*ex aequo et bono*" and the other term "*amiables compositeurs*" often used in this connection (e.g., article 33, paragraph 2 UNCITRAL Arbitration Rules*) were not clearly demarcated and sometimes given varying interpretations in different legal systems. It was also noted that the consideration of this issue could not be completely separated from the discussion on question 5-10 (parties' choice of the law applicable to the substance of the dispute).

85. The Group agreed, therefore, though only on a tentative basis, to follow the approach adopted in article 33, paragraph 2 of the UNCITRAL Arbitration Rules,* with two modifications. One was to use only the term "*ex aequo et bono*" although some support was expressed for also retaining the words "*amiables compositeurs*". The other was not to retain the last part of the paragraph which reads "if the law applicable to the arbitral procedure permits such arbitration". It was thought that such a requirement, while meaningful in arbitration rules, was not appropriate in the model law which itself was to be, for most cases, the very law determining the permissibility.

86. The Working Group was agreed that it was extremely difficult to define in a practicable manner the mandate, and its limits, of arbitrators authorized to decide *ex aequo et bono* (or as *amiables compositeurs*). However, in view of the desirability of a clarification, it did not wish to exclude the possibility of a later attempt to draft a suitable provision. In this respect, a proposal was made according to

which the model law should expressly state that arbitrators, even when deciding *ex aequo et bono*, should to the largest possible extent ensure the enforceability of the decision within the States with which the dispute has a significant connection.

Question 5-10: Should the model law recognize as binding on the arbitral tribunal an agreement by the parties that a certain law be applicable to the substance of the dispute?

87. There was general agreement that the model law should recognize as binding on the arbitral tribunal an agreement by the parties that a certain law be applicable to the substance of the dispute. There was some support for the proposal (set forth in the report, paragraph 91*) that parties may not only be given the facility of designating a specific national law, but also of choosing an international convention or uniform law even if it was not yet in force, or not in force in their countries.

Question 5-11: Failing an agreement envisaged under question 5-10, should the arbitral tribunal apply the law it deems appropriate (as, e.g., under article 1496 of the French New Code of Civil Procedure) or the law determined by the conflict of laws rules which it considers applicable (as, e.g., under article 33 (1) of the UNCITRAL Arbitration Rules**)?

88. Divergent views were expressed on the question of how the arbitral tribunal should determine the law applicable to the substance of the dispute, where the parties had not designated such law. Under one view, the model law should follow the rule embodied in article 33, paragraph 1 of the UNCITRAL Arbitration Rules,** according to which "the arbitral tribunal shall apply the law determined by the conflict of laws rules which it considers applicable".

89. Under another view, the arbitral tribunal would directly determine the applicable substantive law which it considered appropriate (e.g. because it was the law most closely related to the transaction). Such determination would relate to the substantive law of a given State. However, some support was expressed for the idea of allowing the arbitrators to select parts of the substantive law of different countries and to apply rules contained in relevant international conventions, even if not yet in force. A suggestion was made for giving the arbitral tribunal some guidance in determining the applicable legal rules by requiring it to take into account the interests and wishes of the parties and their national laws.

90. The Working Group requested the Secretariat to prepare alternative draft provisions reflecting the above views, and decided to reconsider the issue on the basis of those draft provisions.

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1981, part two, III.

** Yearbook . . . 1976, part one, II, A, para. 57.

Question 5-12: Should the arbitral tribunal be required to decide in accordance with the terms of the contract and to take into account the usages of the relevant trade? If so, should this also apply to decisions *ex aequo et bono*?

91. In considering this question, it was noted that different considerations applied depending on whether the arbitral tribunal was to decide the dispute according to law or *ex aequo et bono*. In respect of the first type of arbitration, it was agreed that an arbitral tribunal should have regard to the terms of the contract and relevant trade usages. However, divergent views were expressed as to whether this should be expressed in the model law, and if so in what manner. Concerning the regard to contract terms, the prevailing view was that no provision should be included in the model law since this requirement was self-evident. Furthermore, such a provision would be possibly misleading or incorrect since a contract provision could be invalid under the applicable substantive law. Under another view, however, it was advisable to require the arbitral tribunal to decide in accordance with the terms of the contract (or, at least, to take those terms into account).

92. Concerning the regard to trade usages, one view was not to include a provision in the model law, since this was a matter of substantive law and a provision in the model law could create a conflict with a national substantive law. The prevailing view was that an attempt be made to draft an appropriate provision. Such a provision might be modelled on article VII, paragraph 1 of the 1961 Geneva Convention ("take account of the . . . trade usages") or on article 33, paragraph 3 of the UNCITRAL Arbitration Rules* ("take into account the usages of the trade applicable to the transaction"). A further suggestion was to consider inclusion of a provision along the lines of article 9 of the 1980 Vienna Sales Convention.**

93. As regards arbitration *ex aequo et bono*, there was wide support for not including a provision in the model law according to which *amiable compositeurs* should have regard to the terms of the contract and trade usages. This was considered to be in accordance with the earlier decision concerning a possible definition of the mandate of such arbitrators (see question 5-9, above, paragraph 86). It was noted that if certain guidelines seemed desirable, regard to trade usages should not be given greater weight than regard to contract terms or observance of the applicable law.

94. The Working Group decided to take a final stand after considering alternative draft provisions to be prepared by the Secretariat which would reflect the above views.

6. Settlement

Question 5-13: Where parties settle their dispute amicably during arbitration proceedings, should the arbitral

tribunal be authorized (but not compelled) to record such settlement in an award ("*accord des parties*"), and should this type of award be treated like any other award?

95. There was general agreement that the arbitral tribunal should be authorized to record a settlement, which parties had reached during arbitration proceedings, in an award. It was thought that arbitrators would normally accede to a request by the parties to enter the settlement in an award. However, they should not be compelled to do so in all circumstances. Divergent views were expressed as to the extent of the discretion to be given to the arbitrators in this respect.

96. A suggestion was made that the arbitral tribunal could be empowered to enter a settlement by the parties in an award upon the request of one party only, unless the parties had stipulated otherwise.

97. The Working Group was agreed that a settlement entered in an award should indicate that it was an award. It was also agreed that such an award should be treated like any other award.

7. Correction and interpretation of award

Question 5-14: Should the model law contain a provision according to which a party may request within a specific period of time that the arbitral tribunal give an interpretation of the award or correct technical errors therein?

98. There was general agreement that the model law should contain provisions concerning the correction and interpretation of an award. Such provisions could be modelled on articles 35 and 36 of the UNCITRAL Arbitration Rules.* However, it was agreed that a request for interpretation of the award should be limited to specific points in order to avoid possible abuses and delay.

8. Fees and costs

Question 5-15: Should the model law contain any provisions relating to fees and costs, for example, empowering the arbitral tribunal or any administering body to request deposits from each party?

Question 5-16: Would it be appropriate for the model law to envisage any review by a court (or its president) concerning the fees of arbitrators and, for example, allow readjustment in case of utterly unreasonable fees?

99. There was wide support for the view that questions concerning the fees and costs of arbitration were not an appropriate matter to be dealt with in the model law. This view left open the possibility for a State to provide for court control concerning fees and costs, and, for example, to allow readjustment of utterly unreasonable fees.

* Yearbook . . . 1976, part one, II, A, para. 57.

** Yearbook . . . 1980, part three, I, B.

* Yearbook . . . 1976, part one, II, A, para. 57.

9. *Delivery and registration of award*

Question 5-17: Should the model law state that the award shall be delivered to the parties and in what form (e.g. signed copies)?

100. There was general agreement that the model law should require that the award be delivered to the parties and should specify in what form.

Question 5-18: Should the model law require that the award be deposited or registered with a specified authority in the country where it was made? Or would it be preferable to adopt the system of the 1958 New York Convention, which allows recognition and enforcement of foreign arbitral awards without such deposit or registration, for all awards covered by the model law, i.e. international commercial arbitration awards?

101. There was wide support for not requiring that the award be deposited or registered in the country where it was made. This was to adopt the system of the 1958 New York Convention, which allows enforcement of foreign arbitral awards without such deposit or registration, for all awards covered by the model law, although in borderline cases it might be difficult to determine whether or not an award was covered by the model law.

102. Some support was expressed for requiring deposit or registration of an award. This requirement would benefit parties, by ensuring the continued availability of the original award or an authenticated copy thereof. A suggestion was made to provide for deposit or registration only if at least one party so requested.

10. *Executory force and enforcement of award*

Question 5-19: Should the model law adopt a uniform system of enforcement for all "international" awards irrespective of the place where they are rendered?

Question 5-20: Which rules of procedure on recognition and enforcement should the model law lay down? For example, should it adopt a provision along the lines of article IV of the 1958 New York Convention on what an applying party shall supply? Should it specify the formalities of the recognition and enforcement order and name the authority competent to issue such order?

103. There was wide support for the idea of adopting a uniform system of enforcement for all awards covered by the model law. This would result in all awards rendered in international commercial arbitration being uniformly enforced irrespective of where they were made. However, divergent views were expressed as to whether the model law should contain any procedural rule on recognition and enforcement. Under one view, the model law should not deal with these procedures which were idiosyncratic to the law of civil procedure of each country. Furthermore, the model law was not an appropriate means for furthering the unifying effect already achieved by the 1958 New York Conven-

tion. Under another view, it was desirable that the model law should not be silent on that issue. One suggestion was to include in the model law merely a reference to the relevant provisions of the 1958 New York Convention. Another suggestion was to incorporate into the model law procedural provisions taking into account article III, and in particular article IV, of that Convention. Yet another proposal was to call upon States to establish a uniform system.

104. The Working Group was agreed that its exchange of views on the matter was of a tentative nature, and that further careful study was needed on the issues considered. It requested the Secretariat to draft alternative draft provisions which could assist the Working Group in reaching a decision.

11. *Publication of award*

Question 5-21: Would it be appropriate for the model law to deal with the question whether an award may be published and, if so, should an express consent of the parties be required?

105. There was general agreement that the model law should not deal with the question whether an award may be published.

VI. *Means of recourse*

1. *Appeal against arbitral award*

Question 6-1: Should the model law recognize any agreement by the parties that the arbitration award may be appealed before another arbitral tribunal (of second instance)?

106. There was wide support for the view that parties were free to agree that the award may be appealed before another arbitral tribunal (of second instance), and that the model law should not exclude such practice although it was not used in all countries. However, the Working Group was agreed that there was no need to include in the model law a provision recognizing such practice. It was noted, however, that this conclusion might have to be reconsidered in the light of the ultimate contents of the model law, and in particular its chapter on means of recourse against an award.

Question 6-2: Should the model law allow any appeal to a court for review of the award on the merits (apart from the setting aside procedure considered in question 6-6)?

107. There was very wide support for the view that an award rendered in international commercial arbitration should not be subject to court review on its merits. It was noted that this reflected the legal position in most States, and that a trend was discernible to further reduce the remaining instances where court review was still allowed.

108. Divergent views were expressed as to whether this policy should be stated in the model law. The prevailing view was not to incorporate a provision to that effect. While the model law itself would then not contribute to unification, the hope was expressed that the above-mentioned trend would continue. Another view was that the model law should expressly exclude any court review of awards on the merits, in order to further the above policy. A suggestion was made to consider including a provision according to which an award was final (or had the effect of *res judicata*), subject to certain conditions (e.g. it was not contrary to *ordre public*).

2. Remedies against leave for enforcement (*exequatur*)

Question 6-3: Should the model law adopt a uniform, appeal system concerning decisions refusing recognition or enforcement irrespective of where the award was made?

Question 6-4: Should the model law adopt a uniform appeal system concerning decisions granting recognition and enforcement irrespective of where the award was

made (subject to a possible modification regarding awards against which a setting aside action may be brought, see question 6-8)? In particular, should the grounds on which recognition and enforcement may be refused under article V of the 1958 New York Convention be the same under the model law irrespective of where the award was made?

Question 6-5: Which rules of procedure concerning recourse against an *exequatur*, or against refusal of *exequatur*, should the model law lay down, including specification of the court or authority to which a party may appeal?

109. There was wide support for the view that the model law should not set forth rules on remedies against decisions granting or refusing enforcement of awards. It was thought that the procedures for appeal or recourse against the decisions of a court were an integral part of the law of civil procedure of each State. Accordingly, the Working Group did not accept, at least for the time being, the suggestion to adopt in the model law a uniform system of appeal against decisions relating to the enforcement of awards rendered in international commercial arbitration.

B. Working paper submitted to the Working Group on International Contract Practices at its third session (New York, 16-26 February 1982): Note by the Secretariat: possible features of a model law on international commercial arbitration: questions for discussion by the Working Group (A/CN.9/WG.II/WP.35)*

A. NEW MANDATE OF THE WORKING GROUP

1. The Working Group on International Contract Practices has been given a new mandate which relates to the field of international commercial arbitration. It is laid down in the following decision adopted by the United Nations Commission on International Trade Law at its fourteenth session:

"The Commission

"1. *Takes note* of the report of the Secretary-General entitled "Possible features of a model law on international commercial arbitration" (A/CN.9/207)**;

"2. *Decides* to proceed with the work towards the preparation of a draft model law on international commercial arbitration;

"3. *Decides* to entrust this work to its Working Group on International Contract Practices with its present composition;

"4. *Requests* the Secretary-General to prepare such background studies and draft articles as may be required by the Working Group."¹

2. The Commission also decided that in preparing a draft model law the conclusions reached by it should be taken into account, in particular, that the scope of application be restricted to international commercial arbitration and that due account be taken of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) and of the UNCITRAL Arbitration Rules.² The Commission was agreed that the above report of the Secretary-General (A/CN.9/207)* setting forth the concerns, purposes and possible contents of a model law would provide a useful basis for the preparation of a model law.

* Yearbook . . . 1976, part one, II, A, para. 57.

¹ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-Sixth Session, Supplement No. 17* (A/36/17), para. 70 (Yearbook . . . 1981, part one, A).

² *Ibid.*, para. 65, and Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 81 (Yearbook . . . 1979, part one, II, A).

* 1 December 1981.

** Yearbook . . . 1981, part two, III.

B. SUGGESTED APPROACH AND METHODS OF WORK

3. The Working Group may wish to consider its methods of work and decide on the most appropriate approach for carrying out its task based on these decisions by the Commission. The following remarks are designed to assist the Working Group in this respect and to explain the purpose of the present note.

4. As regards the first step towards the preparation of a draft model law, there are essentially two possible approaches. One would be to select for the present session one of the subject areas covered by a chapter of the above report (A/CN.9/207),* e.g. chapter II Arbitration agreement, and to discuss in detail the various issues relating thereto. The Group might then incorporate into draft provisions the solutions adopted by it or request the Secretariat to prepare draft provisions in accordance with the conclusions reached by the Group. At future sessions, the other subject areas or chapters would be dealt with in the same manner and, after that, a complete set of the first draft provisions may be reviewed as a whole.

5. The other approach would be to have first a preliminary exchange of views on all issues and possible features of a model law and to turn only thereafter to the detailed work outlined in the preceding paragraph. This approach seems preferable for the following reasons. It would enable the Working Group to adopt a common basis as regards the principles, policies and directions of the model law. It would also help to get a better, though necessarily tentative, idea of the scope and contents of the envisaged law as a whole. Above all, many detailed issues are so closely connected with each other that the solution of one issue often depends on the position taken with regard to others. The suggested exchange of views on all points should help to reduce this difficulty since when it comes to deciding a particular question, and to drafting a provision of the model law, the attitude towards other points relevant thereto will have been ascertained at least on a tentative basis.

6. The present note has been prepared primarily as an aid in the suggested exchange of views but might be of some use even if the first approach were adopted. It is a working paper which has to be taken together with the above report by the Secretary-General (A/CN.9/207, hereinafter referred to as "the report").* It follows the order and classification of the issues used in the report (part B). As stated therein,³ this order in no way indicates the eventual structure of the model law but simply adopts the classification scheme used in the national reports as published in the *Yearbook Commercial Arbitration*.⁴

7. The working paper primarily refers to the corresponding discussion of the possible features of a model law set forth in the report. It contains some additional considerations and suggestions supplementing the discussion in the report. Above all, it provides a list of questions which the Working Group may wish to consider. The questions cover the issues identified in the report but should, of course, not be viewed as exhaustive.

8. The Working Group, in its exchange of views on these questions, may in some cases be ready to reach agreement on whether a certain issue should be dealt with in the model law and, if so, in what way. In other cases, any differences of opinion and the reasons therefor may become apparent and, thus, facilitate the search for an acceptable solution. The Group might then request the Secretariat to prepare studies on certain issues or to conduct inquiries, possibly in consultation with interested international organizations and arbitral institutions.

C. ISSUES POSSIBLY TO BE DEALT WITH IN THE MODEL LAW: ANNOTATED LIST OF QUESTIONS

I. Scope of application

1. "Arbitration"

9. According to a decision by the Commission, the model law is to apply to "international commercial arbitration" (see above, paragraph 2). While this would be stated in the law, it is less clear whether the three elements delimiting the scope of application, i.e. "arbitration", "commercial" and "international", should be defined and, if so, in what way.

10. As regards "arbitration" (see report, paragraphs 29-30),* it should be specified that institutional and *ad hoc* arbitration are covered. Whether the term "arbitration" should be further defined seems rather doubtful, not merely because it would involve the difficult task of drawing a clear line against the various types of "free arbitration". It may be noted that national statutes and international conventions usually contain no definition of the term "arbitration".

*Question 1-1:*⁵ Should the model law expressly state that it applies to institutional as well as *ad hoc* arbitration?

Question 1-2: Apart from the clarification referred to in question 1-1, should the model law contain a definition of the term "arbitration"?

2. "Commercial"

11. As suggested in the report (paragraph 31),* There seems to be no particular need for defining the term "com-

* Yearbook . . . 1981, part two, III.

³ A/CN.9/207, para. 8.

⁴ International Council for Commercial Arbitration, *Yearbook Commercial Arbitration*, Pieter Sanders, ed. Deventer, the Netherlands (Kluwer).

* Yearbook . . . 1981, part two, III.

⁵ The questions are numbered according to the chapters they relate to; in the above example, 1-1 stands for chapter I. Scope of application, first question.

mercial", which is the second element delimiting the scope of application of the model law. If, however, such a need were felt, it would be advisable to define the term in the model law but not to follow the approach taken in the 1958 New York Convention which refers to "relationships which are considered as commercial under the national law of the respective State" (article I, paragraph 3).

Question 1-3: Should the term "commercial" be defined in the model law?

3. "International"

12. As indicated in the discussion set forth in the report (paragraphs 32-38),* the third element delimiting the scope of application, i.e. "international", raises a number of difficult and complex questions. Not only is there a great variety of possible criteria for distinguishing between domestic and "international" cases (e.g. subject matter of dispute; nationality or domicile of parties; applicable procedural law; nationality of arbitrators; place of arbitral proceedings and award). There is also the difficulty that the distinction must be made with regard to the various phases covered by the model law (i.e. arbitration agreement, arbitral proceedings, arbitral award) which conceivably may call for different criteria. In addition, this issue may be viewed as being linked with questions of conflicts of laws or international jurisdiction.

13. In view of this, the Working Group may wish, during its first exchange of views, to tentatively agree on a simple formula applicable to all phases. This formula would serve as a working assumption for the discussion on the other issues and would then be reviewed and refined in the light of these discussions.

14. A simple formula is used, for example, in the most recent national arbitration law, establishing special rules for international cases: under article 1492 of the New Code of Civil Procedure of France, an "arbitration is international if it involves international commercial interests."⁶ Reference is, thus, made to the subject matter of the dispute, which has been said to explain best the special nature of, and need for, rules of international commercial arbitration.⁷ This formula, which is based on a notion developed in French case law,⁸ does not include a definition of the term "international".

15. If any definition were desired, a formula, still relatively simple, might be found along the lines of the notion used in the European Convention on International Commercial Arbitration (Geneva, 1961), article I, paragraph 1:

* Yearbook ... 1981, part two, III.

⁶ Décret no. 81-500 of 12 May 1981, *Journal Officiel* of 14 May 1981, p. 1402; repr. in *Dalloz-Chronique* 1981, p. 217.

⁷ E.g. Fouchard, "Quand un arbitrage est-il international?", *Revue de l'arbitrage* 1970, pp. 59, 75.

⁸ Robert, "L'arbitrage en matière internationale", *Dalloz-Chronique* 1981, p. 209.

"This Convention shall apply:

"(a) To arbitration agreements concluded for the purpose of settling disputes arising from international trade between physical or legal persons having, when concluding the agreement, their habitual place of residence or their seat in different Contracting States;

"(b) To arbitral procedures and awards based on agreements referred to in paragraph 1 (a) above."

Similarly, the model law might state that it applies to arbitration agreements, and to the arbitral proceedings and awards based thereon, between parties whose places of business are in different States.

Question 1-4: Would it be sufficient to refer simply, i.e. without definition, to the international nature of the commercial matter in dispute (or of the arbitration agreement)?

Question 1-5: If a definition is desirable, should one formula (e.g. parties from different States) be adopted for all phases covered by the model law?

II. Arbitration agreement

1. Form, validity and contents

16. The issues and possible features relating to form, validity and contents of the arbitration agreement are discussed in some detail in the report (paragraphs 41-47).^{*} Supplementary information should be given here, in particular to the reference to Latin-American States (paragraphs 41-42).^{*} The Fifth Conference of Ministers of Justice of the Hispanic-Portuguese-American Countries (Lima, 13-17 July 1981) adopted a model law of arbitration and recommended to the Governments of its Member States to take it into consideration when reforming their domestic law.⁹

17. Article 4 of that model law requires for every arbitration a written agreement; and it is this arbitration agreement ("convenio arbitral") which precludes resort to courts as laid down in article 6. Article 5, then, speaks of a submission ("compromiso") which is to be formalized in writing at the same time as or subsequent to the arbitration agreement; it must set forth certain information on the act of submission and the parties thereto, the matters submitted to arbitration, the appointment of the arbitrators and whether the arbitration is *de jure* or *ex aequo et bono*, and it may contain other points agreed on by the parties.

Question 2-1: Is it sufficient to require (as, e.g., article II of the 1958 New York Convention) only one arbitration agreement irrespective of whether it concerns existing or future disputes or should some additional act be envisaged in certain cases?

* Yearbook ... 1981, part two, III.

⁹ Resolution No. 5, point 6.c.; Member States are, in addition to the Latin American countries, the Philippines, Portugal and Spain.

(The following questions are based on the assumption that no additional act is envisaged)

Question 2-2: Should the model law specify the required form of the arbitration agreement and, if so, require that it be "in writing"?

Question 2-3: If writing were required, should the term "in writing" be defined, for example, as article II of the 1958 New York Convention ("agreement signed by the parties or contained in an exchange of letters or telegrams") or should a more extensive and refined definition be sought which should reduce the difficulties encountered in practice with the above definition (see report, paragraph 43)?*

Question 2-4: Which points relating to the validity of the arbitration agreement should be included in the model law? For example, should a provision be included guaranteeing equality of the parties as regards the appointment of arbitrators (see report, paragraph 44)?*

(In this connection, it may be suggested that the question as to which law governs the validity of the arbitration agreement be considered, together with other conflicts questions, at a later stage when it will have to be decided whether the model law should include conflicts rules at all.)

Question 2-5: What should be the minimum contents of an arbitration agreement? For example, would a provision like article II, paragraph 1 of the 1958 New York Convention be appropriate and sufficient (see report, paragraphs 46-47)?*

2. Parties to the agreement

18. The question who may be a party to an arbitration agreement is discussed in the report (paragraphs 48-50),* including the difficult issue whether any restrictions should apply, or be recognized, to the capacity to arbitrate in the case of governmental agencies or other public entities. In this connection, the even more difficult question of State immunity is also submitted for consideration (see report, paragraphs 51-54).*

Question 2-6: Should the model law contain a provision on who may be a party to an arbitration agreement?

Question 2-7: If so, should the model law state, for example, that it applies to "arbitration agreements concluded by physical or legal persons of private or public law" or should a provision be added according to which even "legal persons of public law have the right to conclude valid arbitration agreements" (as,

e.g., article II, paragraph 1 of the 1961 Geneva Convention)?

Question 2-8: Should an attempt be made to deal in the model law with certain aspects of State immunity in the area of international commercial arbitration? For example, to mention only one out of many possibilities, should the model law construe the commitment to arbitrate by a Government or a State organ as containing an implied waiver of any right to invoke State immunity in the arbitration proceedings or arbitration-related court proceedings?

3. Domain of arbitration

19. The main question relating to the domain of arbitration is whether a certain subject matter is "arbitrable", i.e. capable of being settled by arbitration. In addition to this question (see report, paragraphs 55-56),* the report submits for consideration the problem often labelled "filling of gaps" which, in fact, comprises two problems (paragraph 57).

20. As regards the true filling of gaps, i.e. where parties, by intention or not, have left certain points open, it is submitted that the arbitral tribunal may not fill those gaps without special authorization by the parties. However, even with such special authorization in the arbitration agreement or a later agreement it is doubtful whether the arbitral tribunal should be empowered to carry out this function and whether its decision, which is more like a quality valuation than a dispute settlement, should be recognized and enforced as an award.

21. As regards the other issue, i.e. adaptation of contracts after unforeseeable change of circumstances, it is suggested that parties may validly authorize the arbitral tribunal to adapt their contract. The main question is whether an arbitral tribunal may do so even without special authorization by the parties, as the courts of most countries may do.

Question 2-9: Should the model law set forth a list of non-arbitrable subject matters, either as an exhaustive list or as an open list to be supplemented by the respective State, or would it be sufficient to express the restrictions merely by reference to "international public policy"?

Question 2-10: Should the model law deal with the "true filling of gaps" and, if so, should a special authorization by the parties be required or should it treat this task as lying outside the arbitrators' competence even where parties have given such special authorization?

Question 2-11: Should the arbitral tribunal be empowered to adapt a contract without special authori-

* Yearbook . . . 1981, part two, III.

* Yearbook . . . 1981, part two, III.

zation by the parties or only if the parties have given such authorization?

4. *Separability of arbitral clause* (report, paragraph 58)*

Question 2-12: Should the model law adopt the principle of separability or autonomy of the arbitral clause?

5. *Effect of the agreement*

22. In addition to the issues discussed in the report (paragraphs 59-61),* two points may be mentioned here. In connection with the situation (referred to in paragraph 60) where more than two parties are involved in a complex case, thought may be given to the topical issue of multi-party arbitration which was the subject of the ICCA-Interim Congress at Warsaw (1980). Questions for the model law could be, for example, whether consolidation clauses in related arbitration agreements should be given effect, and whether consolidation of proceedings may be ordered even without agreement by the various parties.

23. Another point to be considered could be whether the inclusion in an arbitration agreement of a time-period within which parties may resort to arbitration should, under the model law, be effective and valid even if this time-period expires before a prescription period applicable to the underlying transaction which cannot be shortened by the parties (cf., e.g., article 22 of the Convention on the Limitation Period in the International Sale of Goods¹⁰).

Question 2-13: Should the model law contain a provision along the lines of article II, paragraph (3) of the 1958 New York Convention (report, paragraph 59)?* Should it contain supplementary provisions on what points a court should examine and what type of decision it may render?

Question 2-14: Should the model law deal with problems of consolidation in multi-party disputes (e.g. whether consolidation agreements should be given effect, or whether even without such agreements consolidation might be ordered)?

Question 2-15: Should a stipulated time-period for submission of a dispute to arbitration be effective even if it would expire before a prescription period applicable to the underlying transaction which may not be shortened by the parties?

* Yearbook . . . 1981, part two, III.

¹⁰ Art. 22: "1. The limitation cannot be modified or affected by any declaration or agreement between the parties, except in the cases provided for in paragraph (2) of this article (Yearbook . . . 1974, part three, I, B).

"2. The debtor may at any time during the running of the limitation period extend the period by a declaration in writing to the creditor. This declaration may be renewed.

"3. The provisions of this article shall not affect the validity of a clause in the contract of sale which stipulates that arbitral proceedings shall be commenced within a shorter period of limitation than that prescribed by this Convention, provided that such clause is valid under the law applicable to the contract of sale."

Question 2-16: Are pre-arbitration attachments and similar court measures of protection compatible with an arbitration agreement and should the model law state so?

6. *Termination* (report, paragraphs 62-63)*

Question 2-17: Should the model law specify certain circumstances under which an arbitration agreement would be terminated (e.g. settlement on agreed terms; expiry of time-limit for making award) or would not be terminated (e.g. death of one party)?

III. Arbitrators

1. *Qualifications* (report, paragraph 64)*

Question 3-1: Should the model law expressly state that foreign nationals shall not be precluded from acting as arbitrators (cf., e.g., article 2 of the 1966 Strasbourg Convention, report, paragraph 64)?*

Question 3-2: Are the qualifications required of arbitrators an appropriate matter to be dealt with in the model law?

2. *Challenge* (report, paragraphs 65-66)*

Question 3-3: Should the model law deal with the grounds on which an arbitrator may be challenged? If so, should it list these grounds or would a general formula suffice?

Question 3-4: As regards the procedure of challenging an arbitrator, should the model law recognize any agreement of the parties thereon even if it would exclude (last) resort to a court?

Question 3-5: Should supplementary rules be included for those cases where parties have not regulated the challenge procedure?

Question 3-6: Should the model law adopt ancillary rules on disclosure and on restrictions to the right to challenge along the lines of articles 9 and 10 (2) of the UNCITRAL Arbitration Rules** and article 12 (2) of the 1966 Strasbourg Uniform Law (report, paragraph 66)?**

3. *Number of arbitrators* (report, paragraph 67)*

Question 3-7: Should the model law contain any mandatory provision on the number of arbitrators?

Question 3-8: Should supplementary rules be included for those cases where parties have not agreed on the number?

* Yearbook . . . 1981, part two, III.

** Yearbook . . . 1976, part one, II, A, para. 57.

4. Appointment of arbitrators (and replacement)

24. As suggested in the report (paragraphs 68-69),* the model law should guarantee the parties' freedom to agree on the appointment procedure provided that equality is ensured (see report, paragraph 44, and above, question 2-4).* It may also provide supplementary rules for cases where parties have not, or not in all details, determined the appointment procedure.

Question 3-9: Should the parties be free to determine the appointment procedure, provided that equality is ensured?

Question 3-10: Should supplementary rules be adopted for cases where the appointment procedure, or a certain feature thereof, has not been agreed upon by the parties?

5. Liability (report, paragraph 70)*

Question 3-11: Would it be appropriate for the model law to deal with questions relating to the liability of arbitrators?

IV. Arbitral procedure

1. Place of arbitration (report, paragraphs 71-72)*

Question 4-1: Should the model law recognize the parties' freedom to determine the place of arbitration or to empower a third person to make that determination?

Question 4-2: In the absence of any agreement envisaged in question 4-1, should the model law empower the arbitral tribunal to determine the place of arbitration?

(It may be suggested here that any questions concerning the relevance of the place of arbitration to the determination of the applicable procedural law might appropriately be considered at a later stage in connection with other conflicts issues.)

2. Arbitral proceedings in general

25. As suggested in the report (paragraphs 73-74),* the arbitral tribunal may be empowered to conduct the proceedings as it considers appropriate, subject to instructions by the parties (including agreed arbitration rules), to principles of due process and to certain mandatory provisions adopted in the model law. In addition, it will have to be considered, in this and the following sections, to what extent the model law should provide supplementary rules on procedural points which the parties have not regulated.

Question 4-3: Should the model law expressly empower the arbitral tribunal to conduct the proceedings as it deems appropriate and, if so, what restrictions should be laid down?

Question 4-4: As a general question which is also relevant to the following issues, it may be asked to what extent the model law should include supplementary rules on the arbitral procedure as usually contained in arbitration rules?

3. Evidence (report, paragraph 75)*

Question 4-5: Should the arbitral tribunal be empowered to adopt its own rules on evidence, subject to contrary stipulation by the parties?

Question 4-6: What kind of court assistance may be envisaged in enforcing procedural decisions of the arbitral tribunal, e.g. calling of a witness, taking of evidence?

Question 4-7: What supplementary rules would be appropriate?

4. Experts (report, paragraph 76)*

Question 4-8: Should the arbitral tribunal be empowered to appoint experts *ex officio*, unless the parties have agreed otherwise?

Question 4-9: What supplementary rules are appropriate, e.g. on the expert's terms of reference or on the parties' rights and obligations in respect of the expert's performance of his task (cf. e.g., article 27 of the UNCITRAL Arbitration Rules)?**

5. Interim measures of protection

25. As indicated in the report (paragraphs 77-78),* there are two different types of interim measures possibly to be dealt with in the model law. First, there are interim measures of protection which may be taken by the arbitral tribunal (e.g. conservation of goods or sale of perishable goods). Here the main question is whether the arbitral tribunal may so act even without special authorization by the parties. Then, there are interim measures (e.g. attachment and seizure of assets) which a court may take. The question, here, is whether the availability of such relief and the procedure should be dealt with in the model law at all.

Question 4-10: Should the arbitral tribunal be empowered to take interim measures of protection even without special authorization by the parties?

Question 4-11: Should the model law deal with the involvement of courts in this respect?

* Yearbook . . . 1981, part two, III.

* Yearbook . . . 1981, part two, III.

** Yearbook . . . 1976, part one, II, A, para. 57.

6. *Representation and assistance* (report, paragraph 79)*

Question 4-12: Would it be appropriate for the model law to deal with questions relating to representation and assistance?

7. *Default* (report, paragraphs 80-81)*

Question 4-11: If one of the parties fails to participate, should the arbitral tribunal be empowered to go ahead with the proceedings and make a binding award even without special authorization by the parties, including reference to arbitration rules which allow the arbitral tribunal to do so? If such special authorization were to be required, should the model law expressly recognize it as being effective, subject to any restrictions envisaged under question 4-14?

Question 4-14: What conditions must be met, and laid down in the model law, for the arbitral tribunal to go ahead in case of default?

V. Award

1. *Types of award* (report, paragraph 82)*

Question 5-1: Would it be appropriate for the model law to deal with the different possible types of awards (e.g. final, interim, interlocutory, partial)?

2. *Making of award* (report, paragraphs 83-85)*

Question 5-2: Would it be appropriate for the model law to deal with the question of setting a time-limit for the making of the award?

Question 5-3: Should the model law contain any mandatory provisions on the decision-making process in proceedings with more than one arbitrator? For example, should it require that an award be made by a majority of the arbitrators, provided that all arbitrators had the opportunity to take part in the deliberations leading to that award?

3. *Form of award* (report, paragraphs 86-87)*

Question 5-4: Should the model law require that the award, which must be in writing, be signed by all arbitrators or should it allow any exception, e.g., require that at least a majority of the arbitrators has signed and that the fact of a missing signature of a named arbitrator and the reasons therefor be stated (above the signatures of the other arbitrators)?

Question 5-5: Should the model law require that the date and place of the award be stated therein?

Question 5-6: Should the model law require that the award state the reasons upon which it is based, unless the parties have agreed that no reasons are to be given?

4. *Pleas as to arbitrator's jurisdiction* (report, paragraphs 88-89)*

Question 5-7: Should the arbitral tribunal be empowered to decide on any pleas as to its jurisdiction including those based on non-existence or invalidity of an arbitration agreement?

Question 5-8: Should a ruling by the arbitral tribunal on its jurisdiction be final and binding or should it be subject to any review by a court?

5. *Law applicable to substance of dispute* (report, paragraphs 90-91)*

Question 5-9: Should the model law recognize as binding on the arbitral tribunal an agreement by the parties that the case be decided *ex aequo et bono*? If so, should an attempt be made to define such mandate in the model law (e.g. "*amiables compositeurs*") must observe those mandatory provisions of law regarded in the respective country as ensuring its *ordre public international*?

Question 5-10: Should the model law recognize as binding on the arbitral tribunal an agreement by the parties that a certain law be applicable to the substance of the dispute?

Question 5-11: Failing an agreement envisaged under question 5-10, should the arbitral tribunal apply the law it deems appropriate (as, e.g., under article 1496 of the French New Code of Civil Procedure) or the law determined by the conflict of laws rules which it considers applicable (as, e.g., under article 33 (1) of the UNCITRAL Arbitration Rules)?**

Question 5-12: Should the arbitral tribunal be required to decide in accordance with the terms of the contract and to take into account the usages of the relevant trade? If so, should this also apply to decisions *ex aequo et bono*?

6. *Settlement* (report paragraph 92)*

Question 5-13: Where parties settle their dispute amicably during arbitration proceedings, should the arbitral tribunal be authorized (but not compelled) to record such settlement in an award ("*accord des parties*"), and should this type of award be treated like any other award?

7. *Correction and interpretation of award* (report, paragraph 94)*

* Yearbook ... 1981, part two, III.

* Yearbook ... 1981, part two, III.

** Yearbook ... 1976, part one, II, A, para. 57.

Question 5-14: Should the model law contain a provision according to which a party may request within a specific period of time that the arbitral tribunal give an interpretation of the award or correct technical errors therein?

8. Fees and costs (report, paragraph 94)*

Question 5-15: Should the model law contain any provisions relating to fees and costs, for example, empowering the arbitral tribunal or any administering body to request deposits from each party?

Question 5-16: Would it be appropriate for the model law to envisage any review by a court (or its president) concerning the fees of arbitrators and, for example, allow readjustment in case of utterly unreasonable fees?

9. Delivery and registration of award

26. As indicated in the report (paragraphs 95-96),* it is clear that the award must be communicated or delivered to the parties, while it is less clear whether the model law should also require deposit or registration of the award. Here, a fundamental question arises which is closely connected with the enforcement of an "international" award under the model law.

27. As suggested in the report (paragraphs 96-100),* an attempt might be made to treat all "international" awards alike irrespective of whether recognition and enforcement is sought in the country of origin or abroad. If that approach were accepted, deposit or registration may not be required but merely an enforcement order (*exequatur*) in the country of enforcement, i.e. the system applicable under the 1958 New York Convention would be adopted for all "international" awards. It may be noted that the new French arbitration law has adopted such a unified approach in its articles 1498-1500 which govern the recognition and enforcement of arbitral awards whether rendered abroad or in international arbitration (in France).¹¹

* Yearbook . . . 1981, part two, III.

¹¹ "Chapter I: Recognition and enforcement of arbitral awards rendered abroad or in international arbitration

"Article 1498

"Arbitral awards shall be recognized in France if their existence is proven by the party relying thereon and if this recognition is not manifestly contrary to international public policy.

"Subject to the same conditions, such awards shall be declared enforceable in France by the enforcement judge.

"Article 1499

"The existence of an arbitral award is established by the production of its original text together with the arbitration agreement, or by copies of said documents accompanied by proof of their authenticity.

"If said documents are not in the French language, the party shall supply a translation certified by a translator who is on the list of court-appointed experts.

"Article 1500

"The provisions of Article 1476 through 1479 (d) are applicable."

Question 5-17: Should the model law state that the award shall be delivered to the parties and in what form (e.g. signed copies)?

Question 5-18: Should the model law require that the award be deposited or registered with a specified authority in the country where it was made? Or would it be preferable to adopt the system of the 1958 New York Convention, which allows recognition and enforcement of foreign arbitral awards without such deposit or registration, for all awards covered by the model law, i.e. international commercial arbitration awards?

10. Executory force and enforcement of award (report, paragraphs 87-100)*

Question 5-19: Should the model law adopt a uniform system of enforcement for all "international" awards irrespective of the place where they are rendered?

Question 5-20: Which rules of procedure on recognition and enforcement should the model law lay down? For example, should it adopt a provision along the lines of article IV of the 1958 New York Convention on what an applying party shall supply? Should it specify the formalities of the recognition and enforcement order and name the authority competent to issue such order?

11. Publication of award (report, paragraph 101)*

Question 5-21: Would it be appropriate for the model law to deal with the question whether an award may be published and, if so, should an express consent of the parties be required?

VI. Means of recourse

1. Appeal against arbitral award (report, paragraphs 102-104)*

Question 6-1: Should the model law recognize any agreement by the parties that the arbitration award may be appealed before another arbitral tribunal (of second instance)?

Question 6-2: Should the model law allow any appeal to a court for review of the award on the merits (apart from the setting aside procedure considered in question 6-6)?

2. Remedies against leave for enforcement (*exequatur*)

28. As suggested in the report (paragraphs 105-106),* the uniform approach recommended for the recognition and enforcement of international awards (see above, paragraph 27) may be adopted also in respect of the remedies

* Yearbook . . . 1981, part two, III.

against leave for enforcement and the remedies against refusal of *exequatur*. This approach has been adopted in the new French arbitration law, with one important modification. In its Chapter II, which deals with "recourse against arbitral awards rendered abroad or in international arbitration", an appeal is allowed against a decision refusing recognition or enforcement of an award (article 1501) and against a decision granting recognition or enforcement, based on a restricted number of reasons (article 1502),¹² which are reminiscent of the reasons set forth in article V, paragraphs (1) (a-d) and (2) (b) of the 1958 New York Convention.

29. However, under article 1504, an order to enforce an award rendered in France in international arbitration proceedings may not be appealed. This modification referred to above is, in fact, part of a further streamlining of the appeal system achieved by the following technique. Article 1504 allows against such an award an action to set aside on the same grounds as set forth in article 1502 and regards this action as implying *ipso jure* an appeal against the enforcement order. The result is that the mode of appeal is different depending on whether it is against leave for enforcement of a foreign award or against an international award rendered in France (and against its enforcement there) but that the reasons on which this appeal may be based are identical.

30. The Working Group may wish to consider whether such an approach would be desirable for the model law. If so, it may consider certain modifications. For example, it may require that in enforcement proceedings the party against whom enforcement is sought would have to be given an opportunity to raise objections and, if he does so, to transfer the case to setting aside proceedings. As regards the reasons on which an appeal against an enforcement order or an action to set aside may be based, it would seem desirable to adopt the reasons set forth in article V of the 1958 New York Convention (cf. report, paragraphs 109-111).^{*} Only one exception should be made, in conformity with a trend in recent case law, i.e. reference to "the public policy of the country where enforcement is sought" or, in case of setting aside proceedings, "the public policy of the country where the award was made" may be restricted to the "international public policy" (*ordre public international*) of the respective State (see report, paragraph 21).^{*}

Question 6-3: Should the model law adopt a uniform appeal system concerning decisions refusing recogni-

^{*} Yearbook . . . 1981, part two, III.

¹² "Article 1501: A decision that refuses recognition or enforcement of an award may be appealed.

"Article 1502: An appeal against a decision granting recognition or enforcement may be brought only in the following cases:

"1. If the arbitrator ruled without an arbitration agreement or on the basis of a void or expired agreement;

"2. If the arbitral tribunal was irregularly composed or a sole arbitrator irregularly appointed;

"3. If the arbitrator exceeded the authority conferred upon him;

"4. Whenever due process (literally: the principle of an adversary process) has not been respected;

"5. If the recognition or enforcement is contrary to international public policy."

tion or enforcement irrespective of where the award was made?

Question 6-4: Should the model law adopt a uniform appeal system concerning decisions granting recognition and enforcement irrespective of where the award was made (subject to a possible modification regarding awards against which a setting aside action may be brought, see question 6-8)? In particular, should the grounds on which recognition and enforcement may be refused under article V of the 1958 New York Convention be the same under the model law irrespective of where the award was made?

Question 6-5: Which rules of procedure concerning recourse against an *exequatur*, or against refusal of *exequatur*, should the model law lay down, including specification of the court or authority to which a party may appeal?

3. Setting aside or annulment of award (and similar procedures)

31. As regards the complex question of what remedy the model law should provide against arbitral awards, reference may be made to the discussion in the report (paragraphs 107-111)^{*} and to the above consideration of a possible streamlining of the appeal system concerning international awards made in the country of the model law (above, paragraphs 28-30).

Question 6-6: Should the model law provide for only one type of action of "attacking" an award, e.g. setting aside (leaving aside here recourse against *exequatur*, but see question 6-8)?

Question 6-7: If so, on what grounds should such an action be successful? For example, would it be acceptable to restrict the grounds to those listed in article V, paragraphs (1) (a-d) and (2) (b) of the 1958 New York Convention, with a possible restriction of the "public policy" ground to "international public policy"?

Question 6-8: Assuming that an action to set aside may be brought only on the same grounds as an appeal against the order of enforcement of the same award; should the recourse system be streamlined, e.g. by allowing only the action to set aside and regard it as implying an appeal against the *exequatur*, or by requiring in enforcement proceedings that the party against whom enforcement is sought would be given an opportunity to raise objections and, if he does so, to transfer the case to setting aside proceedings?

Question 6-9: Which rules of procedure concerning an action to set aside the award should the model law lay down, including any time-limits for bringing such action?

^{*} Yearbook . . . 1981, part two, III.

C. Note by the Secretary-General: recommendations concerning administrative services provided in arbitrations under the UNCITRAL Arbitration Rules (A/CN.9/222)*

1. The United Nations Commission on International Trade Law, at its twelfth session, requested the Secretary-General to prepare, if possible in consultation with interested international organizations, guidelines for administering arbitration under the UNCITRAL Arbitration Rules, or a check-list of issues which may arise when the UNCITRAL Arbitration Rules are used in administered arbitration.¹

2. Pursuant to this request, the Secretariat prepared a note entitled "Issues relating to the use of the UNCITRAL Arbitration Rules and the designation of an appointing authority" (A/CN.9/189), taking into account the views expressed by the Commission and information obtained in consultative meetings with members of the International Council for Commercial Arbitration and representatives of the International Chamber of Commerce. The Commission, after a brief exchange of views at its thirteenth session, discussed in more detail at its fourteenth session the draft administrative guidelines set forth in that note.²

3. The Commission, at its fourteenth session,³ agreed that the issuance of guidelines in the form of recommendations could serve a useful purpose in assisting institutions willing to act as appointing authority or to provide administrative services in cases conducted under the UNCITRAL Arbitration Rules. In support of this, it was stated that such guidelines might help to avoid disparity in the application of these Rules by different institutions and to enhance the parties' certainty as to what procedures to expect. Furthermore, it was agreed that such guidelines should be addressed not only to arbitral institutions but also to other bodies, e.g. chambers of commerce, which might also be willing to act as appointing authority or to provide administrative services as envisaged under the guidelines. In addition, some general amendments and specific proposals were made in respect of the draft text of the guidelines prepared by the Secretariat.⁴

4. The Commission, on 23 June 1981, adopted the following decision:

"The United Nations Commission on International Trade Law

"1. Decides that it would be desirable to issue guidelines in the form of recommendations to arbitral insti-

* 18 May 1982. For consideration by the Commission see Report, chapter IV, A.

¹ Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 71, subpara. 2 (a) (Yearbook . . . 1979, part one, II, A).

² Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), paras. 53-58 (Yearbook . . . 1981, part one, A).

³ *Ibid.*, para. 54.

⁴ *Ibid.*, paras. 55-58.

tutions and other relevant bodies, such as chambers of commerce, in order to assist them in adopting procedures for their acting as appointing authority of providing administrative services in cases to be conducted under the UNCITRAL Arbitration Rules;*

"2. Requests the Secretary-General to prepare, in the light of the views expressed during the discussion, a further note with a revised text of the draft guidelines and any explanations thereof, and to submit that note to the next session."⁵

5. Pursuant to that request, the Secretariat submits this note setting forth a revised draft text of recommendations concerning administrative services provided in arbitrations under the UNCITRAL Arbitration Rules* (see annex). The draft recommendations have been prepared with due regard to the observations and suggestions made by the Commission.

6. The Commission may wish to consider these draft recommendations in detail and finalize them at this session. The Commission may also wish to consider the manner in which the recommendations, as adopted, should be distributed. For example, it might request the Secretary-General to transmit the recommendations to all arbitral institutions and other interested bodies (e.g. chambers of commerce) known to him. In addition, it might request the Secretary-General to transmit copies of the recommendations to Governments suggesting that the recommendations be distributed to all interested institutions or bodies in their respective countries.

ANNEX

Revised draft

Recommendations concerning administrative services provided in arbitrations under the UNCITRAL Arbitration Rules

INTRODUCTORY NOTE

1. The United Nations Commission on International Trade Law (UNCITRAL) adopted, at its fifteenth session (1982), the following recommendations in order to assist arbitral institutions and other relevant bodies, such as chambers of commerce, in adopting procedures in connection with their acting as appointing authority or providing administrative services in cases to be conducted under the UNCITRAL Arbitration Rules.*

2. The UNCITRAL Arbitration Rules* were adopted by the Commission in 1976, after extensive consultations with arbitral institutions and arbitration experts. In the same year, the General Assembly of the United Nations, in its resolution 31/98,** recom-

* Yearbook . . . 1976, part one, II, A, para. 57.

** Yearbook . . . 1977, part one, I, C.

⁵ *Ibid.*, para. 59.

mended the use of these Rules in the settlement of disputes arising in the context of international commercial relations.

3. Since then, the UNCITRAL Arbitration Rules* have become well known and are widely used around the world. Not only do contracting parties increasingly refer to these Rules in their arbitration clauses or agreements, but the Rules have also been accepted or adopted by arbitral institutions and similar bodies in a variety of ways.

4. One way in which the UNCITRAL Arbitration Rules* have been accepted is that arbitral bodies have drawn on them in preparing their own institutional arbitration rules. This has taken two different forms. One has been to use the UNCITRAL Arbitration Rules* as a drafting model, either in full (e.g., the 1978 Rules of Procedure of the Inter-American Commercial Arbitration Commission) or in part (e.g., the 1980 Procedures for Arbitration and Additional Rules of the International Energy Agency Dispute Settlement Centre).

5. The other form has been to adopt the UNCITRAL Arbitration Rules* as such, maintaining their name, and to include in the statutes or administrative rules of an institution a provision that disputes referred to the institution shall be settled in accordance with the UNCITRAL Arbitration Rules,* subject to any modifications set forth in those statutes or administrative rules. Prime examples of institutions adopting this approach are the two arbitration centres established under the auspices of the Asian-African Legal Consultative Committee (see Rule I of the Rules for Arbitration of the Kuala Lumpur Regional Arbitration Centre; articles 4 and 11 of the Statutes of the Cairo Centre for International Commercial Arbitration). In addition, a provision similar to the one described above was included in the "Declaration of the Government of the Democratic and Popular Republic of Algeria concerning the settlement of claims by the Government of the United States of America and the Government of the Islamic Republic of Iran" of 19 January 1981 (article III, paragraph 2).

6. In addition to the above cases, all of which concern an arbitral body's own and only rules, the UNCITRAL Arbitration Rules* have been accepted by a number of institutions which have their own established arbitration rules as an alternative set of rules for optional use by parties. These institutions have, in different forms, declared their willingness to act as appointing authority and to provide other administrative services in arbitrations under the UNCITRAL Arbitration Rules* if parties to an arbitration so wish.

7. Such willingness has been declared, for example, by the American Arbitration Association, which has adopted a specific set of administrative "Procedures for Cases under the UNCITRAL Arbitration Rules". These Procedures set forth in detail how the American Arbitration Association would perform the functions of an appointing authority and provide administrative services in conformity with the UNCITRAL Arbitration Rules.* They also include model clauses and a fee schedule for these two kinds of services. The Arbitration Institute of the Stockholm Chamber of Commerce is also prepared to act as appointing authority and to provide administrative services in arbitrations conducted under the UNCITRAL Arbitration Rules.* This facility has already been incorporated in the first international arrangement to include the UNCITRAL Arbitration Rules,* i.e. the "Optional Arbitration Clause for use in contracts in USA-USSR Trade-1977 (Prepared by American Arbitration Association and USSR Chamber of Commerce and Industry)". Other institutions willing to provide the above services include, for example, the Foreign Trade Arbitration of the Federal Economic Chamber, Belgrade, Yugoslavia (Rules of 9 November 1981) and the London Court of Arbitration (1981 International Arbitration Rules).

POSSIBLE WAYS FOR INSTITUTIONS TO OFFER SERVICES FOR CASES UNDER THE UNCITRAL ARBITRATION RULES

8. In view of the promising trend in favour of the use of the UNCITRAL Arbitration Rules,* the Commission invites those arbitral institutions and other relevant bodies, such as chamber of

commerce, which have not yet done so, to consider the possibility of offering services for cases conducted under the UNCITRAL Arbitration Rules.* It further recommends that institutions, in adopting or applying the UNCITRAL Arbitration Rules,* should, as far as possible, refrain from modifying them. Parties who agree to the use of the UNCITRAL Arbitration Rules* by referring to them in an arbitral clause or agreement, or by submitting a dispute to an institution whose own institutional rules or statutes refer to these Rules, rely on the uniform application of the Rules. This is particularly apparent, for example, in the case of an international trading firm which has been involved in a number of arbitrations administered under the UNCITRAL Arbitration Rules* and which thereby has gained familiarity with and confidence in the use of the Rules. Another example is the situation in which parties to a contract agree to use these Rules in arbitration under the contract, but postpone the selection of the administering body to the time when a dispute arises. In these and similar situations, the parties have an interest in the uniform application of the UNCITRAL Arbitration Rules* irrespective of which particular institution is to administer the arbitration. In order to protect the interests of parties who rely on the UNCITRAL Arbitration Rules,* and to promote the certainty of the parties with respect to the application of these Rules, institutions are requested to leave, as much as possible, the Rules unchanged and to adopt administrative procedures which implement the Rules and which are in conformity with them.

9. Of course, this request does not mean that the particular organizational structure and needs of a given institution should be neglected. However, such specific features often relate to matters not regulated in the UNCITRAL Arbitration Rules.* For example, there are no special provisions in these Rules concerning the various possible facilities and procedures for providing administrative services or on such particular matters as fee schedules. Nor are there special rules on the organizations of a body acting as appointing authority (e.g. specifying which organ is to perform a task entrusted to such authority under the Rules). It should, therefore, be possible to adopt administrative procedures which are tailored to the particular needs and organization of the institution without modifying the UNCITRAL Arbitration Rules.*

10. If in exceptional circumstances an institution deems it necessary to adopt an administrative procedure which modifies the UNCITRAL Arbitration Rules,* it is recommended that every effort be made to refrain from making substantive changes in the Rules. Also, it is strongly suggested that any administrative procedure which modifies a provision of these Rules should clearly indicate the modification which is made. An appropriate way of doing so is to specify the provision which it replaces, as was done, for example, in the Rules for Arbitration of the Kuala Lumpur Regional Arbitration Centre (opening words of Rule 8: "In lieu of the provisions of article 41 of the UNCITRAL Arbitration Rules the following provisions shall apply: ..."). This specification would be of great help to the reader and potential user who would otherwise have to embark on a comparative analysis of the administrative procedures and all provisions of the UNCITRAL Arbitration Rules* in order to discover any disparity between them.

11. An arbitral institution might wish to consider whether to accept the UNCITRAL Arbitration Rules* as its own and only institutional rules or as an alternative set of rules for optional use by parties. The first approach may commend itself when a new institution is created. The second approach may be appropriate for national arbitral bodies with institutional rules which are primarily intended for domestic arbitrations. Even an institution which already has rules for international commercial arbitration could enhance its appeal by broadening its range of services to include arbitration under the UNCITRAL Rules.*

12. Although such latter arbitral institutions normally have administrative procedures for cases conducted under their own rules, it is recommended that they establish special administrative procedures for cases under the UNCITRAL Rules.* This is advisable for the sake of clarity and parties' certainty, even if these special

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1976, part one, II, A, para. 57.

procedures for cases under the UNCITRAL Rules* are, in substance, similar to the procedures for cases governed by other rules of that institution.

13. An institution willing to provide services for arbitrations conducted under the UNCITRAL Arbitration Rules* is invited to make its willingness known to the interested public and to describe in detail the services offered and the relevant administrative procedures.^a

^a In an introductory part, the institution may wish to provide, in addition to the customary description of its aims and traditional activities, some information regarding the UNCITRAL Arbitration Rules. In particular, it may state that these Rules were adopted in 1976, after extensive deliberations, by the United Nations Commission on International Trade Law; that this Commission consists of 36 member States representing the different legal, economic and social systems and geographic regions of the world; that in the preparation of these Rules, various interested international organizations and leading arbitration experts were consulted; that the General Assembly of the United Nations has recommended the use of these Rules for inclusion in international commercial contracts; and that these Rules have become widely known and been accepted around the world. (Footnote in original).

POSSIBLE CONTENTS OF ADMINISTRATIVE PROCEDURES

1. Offer of services

14. Services which may be provided in connection with arbitrations conducted under the UNCITRAL Arbitration Rules* are the performance of the functions of an appointing authority as specified in the UNCITRAL Arbitration Rules,* and the provision of administrative services of a technical, secretarial nature. These services could be provided not only by arbitral institutions but also by other bodies, in particular chambers of commerce or trade associations.

15. It is recommended that the administrative procedures of the institution distinguish clearly between the functions of an appointing authority as envisaged under the UNCITRAL Arbitration Rules* and other administrative assistance of a technical, secretarial nature. The institution should declare whether it is offering both or only one of these types of service. When offering both types the institution may declare its willingness to provide only one of these services in a given case, if so requested.

16. The distinction between these two types of services is also of relevance to the question of which party may request these services. On the one hand, an institution may act as appointing authority under the UNCITRAL Arbitration Rules* only if it has been so designated by the parties, whether in the arbitral clause or in a separate agreement. An institution should so state in its administrative procedures, possibly with the additional provision (as a rule of interpretation) that it would also act as appointing authority if the parties submit a dispute to it without specifically designating it as the appointing authority. On the other hand, administrative services of a technical, secretarial nature might be requested not only by the parties, but also by the arbitral tribunal (cf. article 15, paragraph (1) and article 38, paragraph (c) of the UNCITRAL Arbitration Rules*).

17. In order to assist parties, the institution may wish to set forth in its administrative procedures model arbitration clauses covering the above services. The first part of any such model clause should be identical with the model clause of the UNCITRAL Arbitration Rules.*

"Any dispute, controversy or claim arising out of or relating to this contract, or the breach, termination or invalidity thereof, shall be settled by arbitration in accordance with the UNCITRAL Arbitration Rules as at present in force."

The agreement as to the services which are requested should follow. For example:

"The appointing authority shall be the XYZ-Institution."

or:

"The XYZ-Institution shall act as appointing authority and provide administrative services in accordance with its administrative procedures for cases under the UNCITRAL Arbitration Rules."

As suggested in the UNCITRAL Model Arbitration Clause, the following note may be added:

"Note — Parties may wish to consider adding:

- "(a) The number of arbitrators shall be . . . (one or three);
- "(b) The place of arbitration shall be . . . (town or country);
- "(c) The language(s) to be used in the arbitral proceedings shall be . . ."

II. Functions as appointing authority

18. An institution which is willing to act as appointed authority under the UNCITRAL Arbitration Rules* should specify in its administrative procedures the various functions of an appointing authority envisaged by these Rules which it will perform. It might also describe the manner in which it intends to perform these functions.

(a) Appointment of arbitrators

19. The UNCITRAL Arbitration Rules* envisage various possibilities concerning the appointment of an arbitrator by an appointing authority. Under article 6, paragraph (2), the appointing authority may be requested to appoint a sole arbitrator, in accordance with certain procedures and criteria set forth in article 6, paragraphs (3) and (4). Further, it may be requested, under article 7, paragraph (2), to appoint the second of three arbitrators. Finally, it may be called upon to appoint a substitute arbitrator under articles 11, 12 and 13 (successful challenge and other reasons for replacement).

20. For each of these cases, the institution may indicate details as to how it would select the arbitrator in accordance with the UNCITRAL Arbitration Rules.* In particular, it may state whether it maintains a panel or list of arbitrators, from which it would select appropriate candidates; and may provide information on the composition of such panel. It may also specify which person or organ within the institution would in fact make the appointment (e.g. president, director, secretary or a committee).

(b) Decision on challenge of arbitrator

21. Under article 10 of the UNCITRAL Arbitration Rules,* any arbitrator may be challenged if circumstances exist that give rise to justifiable doubts as to his impartiality or independence. When such a challenge is contested (e.g. if the other party does not agree to the challenge or the challenged arbitrator does not withdraw), the decision on the challenge is to be made by the appointing authority according to article 12, paragraph (1). If the appointing authority sustains the challenge, it may also be called upon to appoint the substitute arbitrator.

22. The institution may indicate details as to how it would make the decision on such a challenge in accordance with the UNCITRAL Arbitration Rules.* In particular, it may state which person or organ within the institution would make the decision. The institution may also wish to identify any code of ethics or other written principles which it would apply in ascertaining the independence and impartiality of arbitrators.

(c) Replacement of arbitrator

23. In the event that an arbitrator fails to act or in the event of the *de jure* or *de facto* impossibility of his performing his functions, the appointing authority may, under article 13, paragraph (2), be called upon to decide on whether such a reason for replacement exists, and it may be involved in appointing a substitute arbitrator. What has been said above in regard to the challenge of an arbitrator applies also to such cases of replacement of an arbitrator.

* Yearbook . . . 1976, part one, II, A, para. 57.

* Yearbook . . . 1976, part one, II, A, para. 57.

24. The situation is different with regard to those cases of replacement covered by paragraph (1) of article 13. In the event of the death or resignation of an arbitrator during the course of the arbitral proceedings, the only task which may be entrusted to an appointing authority is to appoint a substitute arbitrator.

(d) *Assistance in fixing fees of arbitrators*

25. Under the UNCITRAL Arbitration Rules,* the arbitral tribunal fixes its fees, which shall be reasonable in amount, taking into account the amount in dispute, the complexity of the subject-matter, the time spent by the arbitrators and any other relevant circumstances of the case. In this task, the arbitral tribunal may be assisted by an appointing authority in three different ways:

- (i) If the appointing authority has issued a schedule of fees for arbitrators in international cases which it administers, the arbitral tribunal in fixing its fees shall take that schedule of fees into account to the extent that it considers appropriate in the circumstances of the case (article 39, paragraph (2));
- (ii) In the absence of such a schedule of fees, the appointing authority may provide, upon a party's request, a statement setting forth the basis for establishing fees which is customarily followed in international cases in which the authority appoints arbitrators (article 39, paragraph (3));
- (iii) In cases referred to under (i) and (ii), when a party so requests and the appointing authority consents, the arbitral tribunal shall fix its fees only after consultation with the appointing authority, which may make any comment it deems appropriate to the arbitral tribunal concerning the fees (article 39, paragraph (4)).

26. An institution willing to act as appointing authority may indicate, in its administrative procedures, any relevant details in respect of these three possible ways of assistance in fixing fees. In particular, it may state whether it has issued a schedule of fees as envisaged under (i). The institution might also declare its willingness to perform the function envisaged under (ii), if it has not issued a fee schedule, and to perform the function under (iii).

(e) *Advisory comments regarding deposits*

27. Under article 41, paragraph (3) of the UNCITRAL Arbitration Rules,* the arbitral tribunal shall fix the amounts of any initial or supplementary deposits only after consultation with the appointing authority, which may make any pertinent comment it deems appropriate, if a party so requests and the appointing authority consents to perform this function. The institution may wish to indicate in its administrative procedures its general willingness to do so.

28. It should be noted that, under the UNCITRAL Arbitration Rules*, this kind of advice is the only task relating to deposits which an appointing authority may be requested to fulfill. Thus, if an institution offers to perform any other function (e.g. to hold deposits, to render an accounting thereof), it should be pointed out that this is a modification of article 41 of the UNCITRAL Arbitration Rules.*

* Yearbook . . . 1976, part one, II, A, para. 57.

III. *Administrative services*

29. An institution which is prepared to provide administrative services of a technical, secretarial nature may describe in its administrative procedures the various services offered. Such services may be rendered upon request of the parties or the arbitral tribunal.

30. In describing the various services, the institution should specify those services which would not be covered by its general administrative fee and which, therefore, would be billed separately (e.g. interpretation services). The institution may also wish to indicate which of the services it can provide itself, with its own facilities, and which it might merely arrange to be rendered by others.

31. The following list of possible administrative services, which is not intended to be exhaustive, may assist institutions in considering and publicizing which services it may offer:

- (i) Forwarding of written communications of a party or the arbitrators;
- (ii) Assisting the arbitral tribunal in establishing the date, time and place of hearings, and giving advance notice to the parties (cf. article 25, paragraph (1) UNCITRAL Arbitration Rules)*;
- (iii) Providing, or arranging for, meeting rooms for hearings or deliberations of the arbitral tribunal;
- (iv) Arranging for stenographic transcripts of hearings;
- (v) Assisting in filing or registering arbitral awards in those countries where such filing or registration is required by law;
- (vi) Providing secretarial or clerical assistance in other respects.

IV. *Administrative fee schedule*

32. The institution may wish to state the fees which it charges for its services. It might reproduce its administrative fee schedule or, in the absence thereof, indicate the basis for calculating its administrative fees.

33. In view of the two possible categories of services an institution may offer, it is recommended that the fee for each category be stated separately. Thus, if an institution offers both categories of service, it may indicate its fees for the following three functions:

- (i) Acting as appointing authority and providing administrative services;
- (ii) Acting as appointing authority only;
- (iii) Providing administrative services without acting as appointing authority.

(In addition to the information and suggestions set forth herein, assistance may be obtained from the Secretariat of the Commission (International Trade Law Branch, Office of Legal Affairs, United Nations, Vienna International Centre, P. O. Box 500, A-1400 Vienna, Austria). The Secretariat could, for example, provide any interested institution with copies of the institutional rules or administrative procedures of a given other institution. It may also, if so requested, assist in the drafting of an administrative provision or make suggestions in this regard.)

* Yearbook . . . 1976, part one, II, A, para. 57.

IV. NEW INTERNATIONAL ECONOMIC ORDER*

A. Report of the Working Group on the New International Economic Order on the work of its third session (New York, 12-23 July 1982) (A/CN.9/217)**

INTRODUCTION

1. At its eleventh session the United Nations Commission on International Trade Law decided to include in its work programme a topic entitled "The legal implications of the new international economic order" and established a Working Group to deal with this subject.¹ At its twelfth session the Commission designated member States of the Working Group.² At its thirteenth session the Commission decided that the Working Group should be composed of all States members of the Commission.³

2. The Working Group held its first session in New York from 14 to 25 January 1980 and recommended to the Commission for possible inclusion in its programme, *inter alia*, the harmonization, unification and review of contractual provisions commonly occurring in international contracts in the field of industrial development.⁴ The Commission at its thirteenth session agreed to accord priority to work related to these contracts and requested the Secretary-General to undertake a study concerning contracts on supply and construction of large industrial works.⁵

3. A study on clauses related to contracts for the supply and construction of large industrial works⁶ was submitted to the second session of the Working Group which was held from 9 to 18 June 1981 in Vienna. At this session issues concerning exoneration, renegotiation, quality, inspection and tests, completion, take-over and acceptance, guarantees, rectification of defects, delays and remedies, damages and

limitation of liability, termination of contract and transfer of technology were discussed.⁷

4. At its second session, the Working Group requested the Secretariat to prepare a further study covering topics noted but which had not been analysed in that study⁸ and also to include a number of other topics as the Secretariat deemed appropriate in the light of the discussion at that session.⁹

5. At its fourteenth session, the Commission endorsed the request of the Working Group to complete the study on clauses to be found in contracts for the supply and construction of large industrial works and entrusted to the Secretary-General the drafting of a legal guide that should identify the legal issues involved in such contracts and suggest possible solutions to assist parties, in particular from developing countries, in their negotiations.¹⁰

6. The Working Group held its third session in New York from 12 to 23 July 1982. All the members of the Working Group were represented except Burundi, Cuba, Cyprus, Hungary, Senegal, Singapore, Spain and the United Republic of Tanzania.

7. The session was attended by observers of the following States: Argentina, Belgium, Bulgaria, Burma, Canada, China, Ecuador, El Salvador, Gabon, Jamaica, Liberia, Mexico, Netherlands, Nicaragua, Poland, Republic of Korea, Sudan, Sweden, Switzerland, Turkey and Venezuela.

8. The session was attended by observers from the following United Nations organs: Economic and Social Commission for Asia and the Pacific, United Nations Conference on Trade and Development, United Nations Industrial Development Organization and United Nations Centre on Transnational Corporations.

9. The session was also attended by observers from the following international governmental and non-governmental

* For consideration by the Commission see Report, chapter V (part one, A, above).

** 27 July 1982.

¹ Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17* (A/33/17), para. 71 (Yearbook . . . 1978, part one, II, A).

² Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 100 (Yearbook . . . 1979, part one, II, A).

³ Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 143 (Yearbook . . . 1980, part one, II, A).

⁴ A/CN.9/176, para. 31 (Yearbook . . . 1980, part two, V, A).

⁵ Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 143 (Yearbook . . . 1980, part one, II, A).

⁶ A/CN.9/WG.V/WP.4 and Add. 1-8 (Yearbook . . . 1981, part two, IV, B, 1).

⁷ A/CN.9/198, paras. 11-88 (Yearbook . . . 1981, part two, IV, A).

⁸ A/CN.9/WG.V/WP.4, para. 36 (Yearbook . . . 1981, part two, IV, B, 1).

⁹ A/CN.9/198, paras. 89-91 (Yearbook . . . 1981, part two, IV, A).

¹⁰ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 84 (Yearbook . . . 1981, part one, A).

organizations: The Hague Conference on Private International Law, International Chamber of Commerce and International Federation of Consulting Engineers.

10. The Working Group elected the following officers:

Chairman: Mr. Leif Sevon (Finland)

Rapporteur: Mr. Peter Kihara Mathanjuki (Kenya)

11. The Working Group had before it the study of the Secretary-General on clauses related to contracts for the supply and construction of large industrial works (A/CN.9/WG.V/WP.4 and Add.1-8)* which was submitted to the second session of the Working Group (hereinafter referred to as Study I) and Study II on clauses related to contracts for the supply and construction of large industrial works (A/CN.9/WG.V/WP.7 and Add.1-6)** which had been prepared by the Secretariat for the present session. The purpose of the discussion on the basis of these studies was to assist the Secretariat in drafting a legal guide which would identify the legal issues involved in contracts for the supply and construction of large industrial works and suggest possible solutions to assist parties, particularly from developing countries, in their negotiations.

12. The Working Group adopted the following agenda:

1. Election of officers
2. Adoption of the agenda
3. Consideration of contracts for the supply and construction of large industrial works
4. Other business
5. Adoption of the report

CONSIDERATION OF CONTRACTUAL PROVISIONS RELATING TO CONTRACTS FOR THE SUPPLY AND CONSTRUCTION OF LARGE INDUSTRIAL WORKS

13. The Working Group began its deliberations with a discussion of those topics in Study I which had not been considered at the second session (i.e. drawings and descriptive documents, supply, erection, passing of risks, transfer of property and applicable law).

*Drawings and descriptive documents*¹¹

14. It was observed that these documents were one of many types of documents which may form part of the contract (e.g., tenders, general conditions) and that the legal guide should indicate the importance of clarifying the legal relationship between the various types of documents.

15. There was general agreement that it was impossible to give an exhaustive list of documents of this type to be provided by each party, as the documents which a party

should provide would vary with the nature of the contract. As regards documents which the purchaser might provide prior to the formation of the contract, it was noted that some of these (e.g., tender documents,¹² feasibility studies¹³) were dealt with in other parts of the study. As regards what documents the contractor should provide, it was suggested that this might depend on the requirements of the invitation to tender; the purchaser could protect himself by requiring detailed specifications to be incorporated in the contract. As a general principle, it was suggested that the contractor should be required to furnish all documents necessary for the proper functioning and maintenance of the works which were agreed upon in the contract. It was also pointed out that parties should be advised that an exchange of information and clarification of documents at the stage of negotiation might prevent later disputes.

16. As regards the ownership of these documents, it was noted that the relevant issue was the permitted use of the contents of such documents. Since such documents might contain know-how or trade secrets, the use to which such information might be put should be carefully defined.

17. It was noted that parties were free to formulate the legal consequences of failure to provide drawings and documents in a variety of ways, e.g., to stipulate that the works were not to be considered completed until the documents, for instance with respect to operation and maintenance, were provided, or to stipulate for a reduction in the price to be paid to the contractor who had not supplied the drawings.

*Supply*¹⁴

18. It was noted that the nature of the obligation of the contractor to supply would vary with the type of contract in question. While in some cases the obligation to supply would resemble the obligation of the seller under an ordinary contract of sale, in other cases (e.g., where the supply was ancillary to the erection of the works by the contractor, or where the contractor was a procuring agent for the purchaser) the obligation would be different. The nature of the responsibility of the contractor for defects in the equipment supplied would also depend on the terms of the contract in question.

19. While the contractor's obligation to transport materials would vary with the nature of the contract, there was general agreement that the legal guide should direct the attention of the parties to the issues involved (e.g., fixing of costs, responsibility for storage during transport). It was suggested that a reference by the parties to INCO-

* Yearbook ... 1981, part two, IV, B, 1.

** Reproduced in this volume, part two, IV, B.

¹¹ A/CN.9/WG.V/WP.4/Add.1, paras. 1-43 (Yearbook ... 1981, part two, IV, B, 1); A/CN.9/WG.V/WP.4/Add.8, paras. 4-8 (Yearbook ... 1981, part two, IV, B, 1).

¹² A/CN.9/WG.V/WP.7/Add.1, paras. 17-22 (reproduced in this volume, part two, IV, B).

¹³ *Ibid.*, paras. 1-12.

¹⁴ A/CN.9/WG.V/WP.4/Add.1, paras. 44-65 (Yearbook ... 1981, part two, IV, B, 1); A/CN.9/WG.V/WP.4/Add.8, paras. 9-17 (Yearbook ... 1981, part two, IV, B, 1).

TERMS might be of assistance, but it was also noted that INCOTERMS did not deal with all modes of transport which might be involved. Furthermore, INCOTERMS were intended for ordinary sales.

20. Under one view, responsibility for the storage of materials on site¹⁵ should rest with the contractor, as he may best be acquainted with the materials he was supplying. Under another view, however, it was noted that in some cases it might be preferable to place the responsibility on the purchaser, as he might be able to store cheaply, and provide better security. It was noted that, even when the contractor was to be responsible for storage, the purchaser might be placed under a duty to provide storage facilities, and access to such facilities. There was general agreement that the guide should examine the above issues, and also the issue of the allocation of the risk of loss during storage.

Erection¹⁶

21. It was pointed out that the nature and extent of the obligations of the parties with respect to the erection of the works could vary depending upon the type of works to be constructed. In some contracts all obligations in connection with erection are imposed on the contractor; in others, the purchaser assumes some of these obligations. In still other contracts the obligations of the contractor are limited to supervising erection performed by or on behalf of the purchaser. It was suggested that a division of responsibility with regard to erection could produce uncertainties, and the legal guide should recommend that in such cases the obligations of each party should be specified as clearly as possible.

22. It was generally agreed that if the obligation of the contractor is limited to supervising erection, he should not be responsible for the erection of the works, but merely for giving proper instructions. Furthermore, he should not be liable if these instructions are not obeyed.

23. It was noted that if the purchaser undertakes to provide equipment and supplies necessary to erect the plant he should bear the cost of these materials. It was also suggested that the contract should specify the consequences which would accrue from a delay by the purchaser in providing erection materials, or from providing defective materials.

24. With respect to the supervision of erection, it was pointed out that responsibility for such supervision could be imposed wholly on the contractor; alternatively, the purchaser or his engineer could also engage in supervision.

25. It was agreed that the contract should provide for

access to the works by the purchaser and his personnel, provided this does not interfere with the progress of the works. According to one view "reasonable" access should be provided; another view suggested that the scope of access should be clearly specified in the contract.

26. It was pointed out that in some contracts the purchaser provides labour for the erection of the works. It was suggested that the contract should specify how much labour is to be provided and how skilled it must be. Also, it was noted that in some areas labour supplied by the purchaser may not possess the skill or training required by the contractor, and that the contractor might have to provide training for this labour. It was suggested that the contractor should deal with the issues of the cost and of delay in performance occasioned by such training.

27. It was suggested that the parties to a works contract should agree upon a time schedule for the completion by the parties of the various stages of work, and should specify the consequences of the failure of a party to meet a time limit.

28. The view was expressed that the contract should contain an express promise by each party to co-operate with the other with respect to performance of the contract. Requirements for co-operation in particular respects might also be included.

Passing of risk¹⁷

29. It was suggested that the passing of risk concerns the risk of damage to the materials, equipment or plant for which neither party is liable. It was also agreed that the issue of passing of risk is distinct from the issue of *force majeure*.

30. There was general agreement that the time and consequences of the passing of risk should be defined in the contract because these may differ according to national law of various States, and, in the absence of agreement, may be settled by applicable law in ways contrary to the wishes of a party.

31. It was generally agreed that the degree to which the legal rules governing sales should apply to a works contract depends upon how closely the works contract resembles a sales contract. One view suggested that in a turnkey contract the risk should remain with the contractor until the date of acceptance or completion. Under another view certain risks should pass to the purchaser even before acceptance or completion. However, it was thought advisable for the legal guide to define these events clearly.

32. There was support for the view that the legal guide should deal with the consequences of the passing of risk. It was agreed that after the risk passes to the purchaser, he

¹⁵ The Working Group considered the section entitled "Storage on site" in Study II (A/CN.9/WG.V/WP.7/Add.3, XII) (reproduced in this volume, part two, IV, B) in conjunction with this section.

¹⁶ A/CN.9/WG.V/WP.4/Add.1, paras. 66-113 (Yearbook . . . 1981, part two, IV, B, 1); A/CN.9/WG.V/WP.4/Add.8, paras. 18-24 (Yearbook . . . 1981, part two, IV, B, 1).

¹⁷ A/CN.9/WG.V/WP.4/Add.1, paras. 114-129 (Yearbook . . . 1981, part two, IV, B, 1); A/CN.9/WG.V/WP.4/Add.8, paras. 25-34 (Yearbook . . . 1981, part two, IV, B, 1).

must pay for the plant unless the damage is due to an act or omission of the contractor.

33. It was generally agreed that it would not be advisable to have multiple passing of risk, as, for example, the passing to the purchaser of risk with respect to equipment delivered to the site, passing the risk back to the contractor upon installation of the equipment in the works, and then returning the risk to the purchaser upon acceptance or completion of the works.

34. It was suggested that it is important for the legal guide to inform the parties, particularly from developing countries, of the consequences of allocating risk. Risk is not always fully covered by insurance; and as more risk is imposed on the contractor, the cost to the purchaser may increase. Moreover, as purchasers undertake more of the work under a contract, they assume more of the risk.

35. There was considerable support for the view that the issue of passing of risk is separate from the issue of passing of ownership. However, another view was that in some cases there might be a link between the two issues.

Transfer of property¹⁸

36. It was generally agreed that the issue of transfer of property was not as important as passing of risk, although there were some factors in connection with transfer of property of which the parties should be aware. It was agreed that an agreement of the parties concerning the transfer of property might have only a limited effect, since mandatory rules of law might govern this issue, and since the parties could by agreement between them affect neither public obligations nor the rights of third parties, such as creditors. The legal guide should advise parties to explore the applicable law to determine any mandatory rules relevant to the transfer of property.

37. With respect to the question of reservation of title, a distinction was drawn between transfer of the plant itself and transfer of equipment and machinery to be incorporated in the works. Opinions differed concerning the importance of the question of reservation by the contractor of title to the plant after delivery to the purchaser. One view pointed out that the works are often tailored to the specific needs of the purchaser, and would have little value to the contractor even if the title were retained by him.

38. A view was expressed that the question of transfer of property might be discussed by the legal guide in the context of other substantive issues, such as acceptance and passing of risk.

Applicable law¹⁹

39. It was generally agreed that the legal guide should

clarify the importance and the scope of the choice of applicable law by the parties. It should mention the factors which the parties should take into account in choosing the applicable law. It was suggested that the legal guide should deal with the problem of applicable law in close connection with the problem of settlement of disputes.

40. Some views were expressed that the guide should recommend a model clause on choice of law, without mentioning the law to be chosen. However, it was noted that under many legal systems the law of the place of construction is the applicable law. One view suggested that the law of the place of the construction of the works should be recommended to the parties. Another view suggested that the law of the forum be recommended coupled with the inclusion of an exclusive jurisdiction clause in the absence of an arbitration clause, as otherwise expertise on the foreign law to be applied would be needed and proceedings would be longer and more expensive. It was suggested that preference should be given to a law known to both parties. One view suggested that the legal guide should mention the possibility of resorting to general legal and equitable principles in the event the parties are unable to agree on national law. Under another view the parties should be cautioned against such a choice.

41. It was suggested that the applicable law should be chosen by the parties before drafting the contract as the applicable law should be taken into account in this connection.

42. It was pointed out that under the conflict rules of some countries the freedom of the parties to choose the applicable law is limited. It was suggested that the parties should take into consideration the conflict rules of the country where the court or arbitration proceedings are to take place.

43. It was pointed out that the ability of the parties to choose the applicable law is limited to the law governing the rights and duties between the parties and some administrative municipal laws apply regardless of the choice of the parties.

44. The mandatory requirements of administrative laws (e.g., in the fields of environment protection, safety regulations) being in force in the country of the erection of the works may affect the performance of the contract. The opinion of the Working Group was divided on the issue whether the purchaser should be obliged to inform the contractor of such requirements. The view was expressed that the purchaser should not have such an obligation since such rules are published. Another view was that some of these requirements are not available to foreign enterprises and therefore the purchaser should inform the contractor of them. It was suggested that the legal guide recommend collaboration between the parties and should only draw attention of the parties to these problems and indicate possible solutions.

¹⁸ A/CN.9/WG.V/WP.4/Add.1, paras. 130-140 (Yearbook . . . 1981, part two, IV, B, 1); A/CN.9/WG.V/WP.4/Add.8, paras. 35-37 (Yearbook . . . 1981, part two, IV, B, 1).

¹⁹ A/CN.9/WG.V/WP.4/Add.7, paras. 87-110 (Yearbook . . . 1981, part two, IV, B, 1); A/CN.9/WG.V/WP.4/Add.8, paras. 158-162 (Yearbook . . . 1981, part two, IV, B, 1).

45. It was agreed that the legal guide should deal with the effects of changes of law on the contractor's obligations.

*Feasibility studies*²⁰

46. There was general agreement that the contractor cannot be responsible for feasibility studies and should not be obligated to check the correctness of feasibility studies or information which he received from the purchaser. Feasibility studies are not usually in the possession of the contractor and do not form part of the contract. In the legal guide there should be only a short reference to these problems.

47. It was pointed out that the contractor should not be obliged to make studies and obtain information concerning the feasibility of the works. Evident errors in tender conditions in respect of technical issues should be notified by the contractor to the purchaser. There was agreement that the guide should recommend that the issue of responsibility for a change of physical conditions after preparation of the feasibility studies which affects implementation of the contract should be settled by the parties.

*Formation of contract*²¹

48. It was pointed out that it was advisable to distinguish between the conclusion of the contract and its entry into force. This distinction is important in particular if the contract is subject to a condition (e.g., an approval by authorities).

49. It was observed that the legal guide should recommend that the parties follow the example of article 29 of the United Nations Convention on Contracts for the International Sale of Goods in drafting provisions concerning the form of modification of the contract.

*Variation*²²

50. With respect to variation of the contract, one view was suggested that the contract might be changed only by mutual agreement of the parties. Unilateral change would cause problems as to the ability of the contractor to meet the purchaser's requirements and would have consequences for the price and time of performance.

51. According to another view the purchaser should be entitled to vary the scope of the contract unilaterally if the contractor is able to fulfil the new obligation.

52. It was noted that a distinction should be made between variation of the contract and rectification of errors in

drawings and descriptive documents. The contractor should be responsible for such errors provided that they are not due to incorrect information furnished by the purchaser.

53. It was stressed that the legal guide should recommend a solution to the question of variation which could enable the work to go on without any interruption.

54. It was suggested that the contractor should be entitled to vary the scope of the work undertaken by him if it is in the interest of the purchaser (e.g., improvement of the quality of the works). According to another view the purchaser should have the right to consider what is in his interest and mutual agreement should be required in such cases.

*Interpretation of contract*²³

55. There was general agreement that the power of the parties to determine rules for interpreting the contract could be limited if mandatory rules of the applicable law would to some extent regulate such interpretation. It was agreed that the parties should be encouraged to identify documents which formed the contract. In particular, parties should determine which documents prepared, and proposals made, by the contractor at the pre-contractual stage were to be part of the contract, and should take steps to achieve this. Since the negotiations leading to the conclusion of works contracts might clarify the terms of the contract, it was also agreed that it would be desirable that some documents not forming part of the contract (e.g., correspondence containing negotiations) could be used to clarify the terms.

56. There was general agreement that parties should be advised to eliminate inconsistencies between the various documents which formed the contract. Under one view, it would be advisable to recommend a rule as to which documents were to prevail in case of inconsistency. Under another view, the formulation of a rule was inadvisable, as the rule might not lead to appropriate results in some cases. It was agreed, however, that written contract provisions should prevail over general conditions incorporated by reference.

57. There was wide support for the view that, when general conditions were made part of a contract, pre-printed headings and marginal notes in the general conditions were not normally intended to be part of the contract and could not be used to interpret it. When, however, such headings and marginal notes were intended to be part of the contract (e.g., added to the contract and initialled by the parties) they could be so used.

58. There was general agreement that parties should be advised clearly to define, whenever possible, import-

²⁰ A/CN.9/WG.V/WP.7/Add.1, paras. 1-12 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 1-7 (reproduced in this volume, part two, IV, B).

²¹ A/CN.9/WG.V/WP.7/Add.1, paras. 13-22 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 8-9 (reproduced in this volume, part two, IV, B).

²² A/CN.9/WG.V/WP.7/Add.1, paras. 23-43 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 10-12 (Reproduced in this volume, part two, IV, B).

²³ A/CN.9/WG.V/WP.7/Add.1, paras. 44-103 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 13-16 (reproduced in this volume, part two, IV, B).

ant terms used in the contract. It was also noted that the legal guide should call the attention of parties to the fact that, under some national laws, the use of certain terms may not be appropriate.

59. In this connection it was noted that the preparation of the legal guide would require a clarification of certain terms or notions commonly occurring in contract practice, and possibly require the formulation of new terms acceptable to the various legal systems and in contract practice in order to avoid unnecessary misunderstandings which otherwise might accrue. It was agreed that such clarification and formulation would be of great assistance to parties in drafting contracts, and might in the long term lead to a unification in contract practice. There was therefore general agreement that the legal guide should include a glossary which would define as many as possible of these common legal and technical terms because these definitions would not only be essential to understand the guide but could be incorporated by reference by the parties into their contracts.

60. The Working Group considered the definition of certain terms commonly used in works contracts. With regard to the term "writing", it was noted that the applicable law might require the contract to be in writing and contain a definition of that term which required the writing to be authenticated. Furthermore the contract itself might require certain communications to be made in writing. It was agreed that the attention of the parties should be drawn to difficulties which might arise from the use of certain forms of communication, such as telex. It was also agreed that problems created by modern electronic forms of communication should be examined. With regard to the term "purchaser", a view was expressed that the Secretariat might evaluate the possible use of "employer", "owner" and "client".²⁴

61. The Working Group considered the frequent use of more than one language in drafting a contract and its annexures. There was general agreement that the use of more than one language was often inevitable, because the parties to the contract were not equally familiar with the same language versions should be accorded equal authenticity, as in the case of some international conventions. A suggestion was made that thought should be given to selecting the language of the country whose law would govern the contract, or whose courts would adjudicate on disputes, as such a selection would facilitate dispute settlement.

Assignment or transfer of contract²⁵

62. There was general agreement that the legal guide

should clarify the distinction between assignment and sub-contracting. There was also general agreement that it was inadvisable that a contract should permit a party, without the consent of the other party, to assign the contract to a third party, substituting for himself the third party as a party to the contract.

63. As regards the assignment of contractual duties by either party, there was general agreement that, following the provisions of most legal systems, the contract should not permit a party to assign his duties without the consent of the other party. There was considerable support for the view that the position should be the same in regard to the assignment of contractual rights, as a unilateral assignment could lead to difficulties (e.g., the non-assignment party might be prevented by the law or policy of his country from dealing with the assignee). It was suggested, however, that permitting unilateral assignment in a limited class of case might be useful (e.g., where a contractor was permitted to assign his right to the proceeds to the bank financing the contractor).

Sub-contracting²⁶

64. There was general agreement that the legal guide should address the question of the extent to which a contractor should be permitted to use sub-contractors for discharging his obligations under the contract. It was noted that there may be mandatory laws regulating this question. It was also noted that there was a variety of ways in which sub-contracting could be regulated (e.g., choice of sub-contractors to be approved by the purchaser, sub-contractors to be proposed by the purchaser). Which way was most appropriate would depend on the circumstances of each contract, and perhaps even on the stage which the project had reached at the time sub-contractors were to be used.

65. It was noted that the legal guide should deal with the subject of joint ventures or consortia of contractors, dealing with such aspects as communication between the purchaser and the joint venture and the question of joint and several liability of contractors. This question might be governed by applicable law. It was also suggested that the future programme of work of the Working Group might deal with the question of consortia and joint ventures on a larger base. It was also noted that the purchaser should be informed of the composition of the consortia.

66. There was general agreement that the legal guide should not discuss in detail the relationship between the contractor and sub-contractor. One view suggested that the legal guide should recommend that if the main contract contains provisions concerning settlement of disputes and applicable law, the parties should consider whether the

²⁴ The Working Group decided to consider the definitions of the terms "subcontractor" and "engineer" in connection with the sections in Study II entitled "Sub-contracting" and "Engineer" (A/CN.9/WG.V/WP.7/Add.2: VI and VIII) (reproduced in this volume, part two, IV, B).

²⁵ A/CN.9/WG.V/WP.7/Add.2, paras. 1-7 (reproduced in this

volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 17-19 (reproduced in this volume, part two, IV, B).

²⁶ A/CN.9/WG.V/WP.7/Add.2, paras. 8-41 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 20-27 (reproduced in this volume, part two, IV, B).

same provisions should be included in a sub-contract. Another view was that this might be unwise in some cases where the nationality of the sub-contractors might differ from that of the purchaser.

67. According to one view, if the contractor without reasonable cause fails to pay a sub-contractor, the purchaser should be able to pay the sub-contractor directly. The contract should contain a specific provision defining the circumstances when this could be done, since without such a provision payment of the sub-contractor by the purchaser would be entirely at the purchaser's risk. According to one view the risk borne by the sub-contractor should be proportionate to his share of the work.

68. It was generally agreed that the subject of contracts entered into by the purchaser with third parties is separate from the issue of sub-contracting. The legal guide should therefore discuss this subject separately from sub-contracting.

Co-ordination and liaison agents²⁷

69. There was general agreement that co-ordination of the day-to-day operations under the contract is important for the expeditious completion of the work at low cost. The legal guide should encourage parties to establish means and procedures for co-ordination and co-operation between the parties. One view suggested that the authority of liaison agents appointed by each party should be delineated in the contract. Another view suggested that the legal guide clarify the differing terminology used in practice to refer to these agents.

Engineer²⁸

70. It was generally agreed that the legal guide should recommend that parties clearly define in the contract the role of the engineer if any. Under one view, the engineer should be regarded as a representative of the purchaser alone.

71. According to one view, where the engineer represented the purchaser, the legal guide should recommend that the engineer represent the purchaser only in respect of technical matters arising from the contract. Another view suggested that the role of the engineer should be broader (e.g., determining the amount to be paid for extra work).

72. It was noted that the relationship between the purchaser and the engineer is outside the scope of the contract between the contractor and the purchaser.

73. It was suggested that the legal guide recommend that the parties provide a mechanism to settle provisionally problems in connection with the work so as to enable the work to continue. In this regard, a view was expressed that such a role could be played by an engineer.

Parties' liabilities in respect of third parties²⁹

74. There was some support for the view that the contractor should be fully liable for the acts and omissions of his sub-contractors. There was general agreement that the legal guide should recommend that the contract deal with the question of damage caused to third parties by the acts or omissions of contractors or sub-contractors. It was suggested that the legal guide should recommend that the contract require the contractor to indemnify the purchaser against claims by such third parties. Another view suggested that the legal guide should note that the parties could safeguard themselves against such damage through co-insurance of the contractor and the purchaser.

75. It was noted that the liability of the purchaser and contractor to third parties would be governed by the applicable law. It was suggested that this brought to the parties' attention since the law relating to this issue may vary from country to country.

76. One view suggested that it was advisable for the contract to allocate responsibility for the safety of persons coming onto the worksite. Another view suggested that this was not necessary because it would be governed by applicable law.

77. It was generally agreed that the legal guide should not deal with the subject of agency because the issue is more related to the stage of procurement; the guide should limit itself to the responsibility of the parties in respect of their performance of the contract.

Training and acquisition of skills³⁰

78. It was suggested that the expression "technical assistance" was inappropriate and that the legal guide should establish the terminology with regard to training and other services provided by the contractor in respect of the operation and management of the works.

79. According to one view the contract should deal with questions such as the nature of training, duration of training, the qualifications of trainers and trainees, lodging of trainees, the place of training and the cost of training. Another view suggested that the contract should contain only a general provision with regard to training, and that details regarding these services be dealt with in a separate

²⁷ A/CN.9/WG.V/WP.7/Add.2, paras. 42-49 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 28-30 (reproduced in this volume, part two, IV, B).

²⁸ A/CN.9/WG.V/WP.7/Add.2, paras. 50-66 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 31-33 (reproduced in this volume, part two, IV, B). See also paras. 120-132, "settlement of disputes".

²⁹ A/CN.9/WG.V/WP.7/Add.2, paras. 67-79 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 34-37 (reproduced in this volume, part two, IV, B).

³⁰ A/CN.9/WG.V/WP.7/Add.3, paras. 1-21 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 38-42 (reproduced in this volume, part two, IV, B).

agreement to be concluded at the same time as the main contract.

80. There was some support for the view that the training should take place in the country of the purchaser.

81. With respect to management services, it was suggested that only services after take-over could be considered management services.

*Maintenance and spare parts*³¹

82. There was general agreement that the issues concerning maintenance and spare parts are important for the purchaser, in particular in the developing countries. There was support for the suggestion to distinguish between repairs covered by a warranty binding on the contractor and other repairs which the contractor undertakes without being in breach of any of his obligations.

83. It was noted that the main issue to be addressed by the legal guide was that of maintenance not covered by the warranty period. Under one view, it would be advisable to settle this issue in the contract, while under another view it would be preferable to settle this issue in a separate contract. It was pointed out that the period of maintenance should not be too short, and sanctions should be agreed upon for cases where the contractor failed to perform his obligations.

84. It was pointed out that it might be desirable to distinguish various types of spare parts in the contract, and that the contractor might be asked to guarantee the availability of certain critical items important for the operation of the works.

85. It was felt that tie-in clauses limiting the purchaser to buying spare parts from the contractor might in some circumstances be disadvantageous to the purchaser, and that the purchaser should be free in choosing a supplier. Furthermore, such clauses may be contrary to mandatory provisions of the applicable law on restrictive practices. Under one view, a restriction on choosing a supplier of spare parts other than the contractor might be justified during the warranty period.

86. There was support for the suggestion that the contractor should be obligated to supply the spare parts during a reasonable period of time, and after its expiration the purchaser should be able to produce the spare parts. The contractor should advise the purchaser where to obtain the spare parts not produced by the contractor and the spare parts should be supplied at market prices and within a short delivery period. However, the contractor should not be obligated to procure spare parts manufactured by third parties after the expiration of the warranty period.

³¹ A/CN.9/WG.V/WP.7/Add.3., paras. 22-49 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 43-47 (reproduced in this volume, part two, IV, B).

87. It was suggested that the attention of the parties should be drawn to the interest of purchasers in developing their own capabilities to maintain and repair the works and produce spare parts.

*Price*³²

88. There was general agreement that there is a lack of uniformity in terminology used in connection with different kinds of prices (e.g., lump-sum price, cost-reimbursable price, fixed price, firm price or unit price). It was suggested that an attempt should be made to unify this terminology, and to define the terms used in the legal guide.

89. It was pointed out that the problems connected with inflation should be separated in the legal guide from the issues concerning currency fluctuations.

90. The opinion of the Working Group was divided on the issue whether, and to what extent, the legal guide should deal with criteria used in pricing. One view was that these problems were important, and the elaboration of such criteria, without recommending any solutions, would be of assistance to procurement officers in developing countries, while another view preferred to limit the legal guide only to the legal aspects of pricing because the determination of price was more closely connected to economic factors. It was also noted that the applicable law may also have relevance to the fixing of price.

91. It was suggested that the legal guide should analyse what methods of pricing are advisable in various types of contracts. It was pointed out that the purchaser might be interested in knowing in advance what financial commitments would arise from the contract, and that cost-reimbursable contracts would not give such advance knowledge. Another view was that there should not be a recommendation for a general approach to this problem, as all circumstances should be taken into consideration in determining the appropriate method of pricing.

92. There was general agreement that it would be advisable to specify the equipment and services covered by the agreed price to achieve certainty and eliminate potential disputes.

93. It was pointed out that the purchaser might be interested in agreeing that a part of the price should be paid in the currency of his country, in particular for costs incurred therein, and that the legal guide should deal with problems connected with such payments.

*Revision of price*³³

94. It was agreed that the legal guide should deal separately with revision of price claimed by either party and

³² A/CN.9/WG.V/WP.7/Add.4, paras. 1-24 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 51-54 (reproduced in this volume, part two, IV, B).

³³ A/CN.9/WG.V/WP.7/Add.4, paras. 25-62 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 55-56 (reproduced in this volume, part two, IV, B).

with adjustment of price. The suggestion was made to deal separately with the problems of changes in price consequent to changes in the extent and scope of work, and consequent to the furnishing of additional supplies and services. It was pointed out that it would be advisable not to deal in the legal guide with the revision of price in its own chapter, but in the chapters dealing with the various circumstances in which revision of price occurred.

95. In cases of changes in the extent or scope of the work, the parties should consider the financial consequences of such changes and agree upon a new price. The suggestion was made to pay attention in the legal guide to the problems of the procedure for revision of the price, as it would be advisable to stipulate in the contract clear consequences when circumstances occurred in which the price should be revised.

96. The question was raised whether the purchaser should pay all costs connected with changes in administrative laws affecting the scope of the works. It was pointed out that, in particular in the field of environment protection, the design of the works should set a standard which might be required by future legislation of the developing countries. It was also suggested that the legal guide should draw the attention of the parties to the problem of a revision of price required by technological innovations to the design of the works.

97. As regards currency fluctuations, it was pointed out that the legal guide should refer to these problems and may examine existing techniques aimed at protecting the parties. The legal guide should deal with problems in relation to index clauses.

*Payment conditions*³⁴

98. There was general agreement that the legal guide should address legal issues connected with payment conditions. It was noted that the payment conditions appropriate to a contract would depend on the circumstances of that contract.

99. The view was expressed that the legal guide should direct the attention of the parties to the possible need to provide remedies for anticipatory breach of the contract. It was noted, however, that the remedies to be recommended may not be those appropriate to an ordinary sales contract. It was also noted that the guide should consider problems which arise when legal restrictions on payment are imposed on the partner subsequent to the conclusion of the contract.

100. As regards the time of payment, it was noted that it would be impossible to advise on the actual sums to be paid at different stages of the work, as the amount of these sums would depend on the circumstances of each

contract. However, the legal guide could discuss factors relevant to determining the amounts. Thus the sums should bear a relation to the cash needs of the contractor to proceed with his work at the different stages, and to the need of the purchaser to retain moneys as security for due performance. Furthermore, the right to payment should be made to depend on due performance.

101. As regards payment documents, it was observed that the purchaser or his engineer sometimes delayed in certifying payments, or refused to certify payments without adequate reasons. It was noted that the contract could provide for this situation in various ways, e.g., by providing that the certification is deemed to be given after the lapse of a specified period, or that such matters should be referred to arbitration. In this connection it was pointed out that it would be desirable for the parties to define the circumstances when certification could be refused.

102. As regards methods of securing payment to the contractor, it was noted that a letter of credit was not the only method used, and that other methods (e.g., cash deposits) should also be discussed.

*Performance guarantees*³⁵

103. There was general agreement that the term guarantees were often necessary, as the solvency or stability of the contractor might be in doubt. The terms of such guarantees should be agreed upon at the conclusion of the contract. It was also noted, however, that in view of the high cost of obtaining such guarantees, possible techniques for minimizing their use or reducing their cost should also be explored, e.g., by using revolving letters of credit. There contractor, the guide should also deal with guarantees for advance payment and for the contractor's obligations during the warranty period after completion.

104. There was general agreement that performance guarantees were often necessary, as the solvency or stability of the contractor might be in doubt. The terms of such guarantees should be agreed upon at the conclusion of the contract. It was also noted, however, that in view of the high cost of obtaining such guarantees, possible techniques for minimizing their use or reducing their cost should also be explored, e.g., by using revolving letters of credit. There was wide agreement that a progressive reduction in the amount of the guarantee as work progressed was beneficial as it would lessen the costs of the guarantee. A performance guarantee, however, should not be reduced to an amount so low as not to provide adequate security to the purchaser.

105. As regards the nature of the guarantor's obligation, the attention of the parties should be directed to the merits and demerits of each form of guarantee and of con-

³⁴ A/CN.9/WG.V/WP.7/Add.4, paras. 63-92 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 57-62 (reproduced in this volume, part two, IV, B).

³⁵ A/CN.9/WG.V/WP.7/Add.4, paras. 93-116 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 63-69 (reproduced in this volume, part two, IV, B).

ditions which might be inserted in the guarantee. Thus a first demand guarantee gave the purchaser considerable security, but might be abused. An accessory guarantee, on the other hand, might result in delay before the purchaser receives payment. It was noted that where a guarantor's obligation was not to pay money but to continue the performance of work, the manner in which the performance was to be carried out should be specified.

106. It was suggested that the period to be covered by the guarantee should be clearly indicated both in the contract and the guarantee. The guarantee should also deal with the effect on the guarantee of variations to the contract.

*Insurance*³⁶

107. It was suggested that the legal guide should draw the attention of the parties to the various types of insurance available to cover risks arising from the contract. One view suggested that the legal guide should advise the purchaser that he will ultimately have to bear the costs of insurance by the contractor and suggest that he might wish to consider whether he can obtain insurance himself at lower cost. It was also noted that in some cases the purchaser may require insurance to be purchased in his own country.

108. One view noted that it was common for contractors to carry general liability insurance, including third-party coverage, covering the liabilities arising in the course of its business. It was suggested that the legal guide should recommend that the purchaser consider whether it is necessary to require further third-party liability insurance in connection with the specific contract, which might result in double insurance.

109. One view suggested that the legal guide should consider various measures which a party may take if the other party fails to meet an obligation to provide insurance. According to one view, the legal guide should deal with the possibility of insurance to cover the liability of the contractor for his faulty performance of the contract and issues arising from such insurance.

110. With respect to the time period to be covered by insurance, one view suggested that this would vary with the nature of the risk covered. According to this view, liability insurance should cover the period from the start of erection to take-over of the works by the purchaser.

*Customs duties and taxes*³⁷

111. One view suggested that questions concerning customs duties and taxes should be carefully considered by

parties before entering into the contract because these duties are imposed by the applicable mandatory national law and the responsibility of each party in this regard usually cannot be changed by a contract. According to another view, it was nevertheless advisable to provide in the contract for the allocation of the ultimate burden concerning customs duties and taxes.

*Bankruptcy*³⁸

112. There was general agreement that the legal guide need not deal with bankruptcy in a separate chapter, but rather should consider bankruptcy in connection with other substantive aspects of the contract (e.g., termination, exoneration, modification and assignment) which may be affected by bankruptcy. In this connection, it was suggested that the legal guide should also refer to insolvency, liquidation and similar arrangements in addition to bankruptcy.

113. One view suggested that the legal guide should recommend that the parties consider whether the bankruptcy of sub-contractor should exonerate the contractor. If not, the parties should consider whether the contractor should be given a period of time within which to substitute a new sub-contractor.

114. It was suggested that the legal guide should recommend that the parties consider incorporating in the contract measures to avoid an interruption of work in the event of the bankruptcy of the contractor.

115. It was suggested that the legal guide should recommend that the parties take into account relevant rules of mandatory law in connection with bankruptcy. In this regard, the parties should be warned that with respect to certain matters (e.g., reservation of title) applicable law might contain mandatory rules.

116. It was generally agreed that the legal guide should deal with the relationship between bankruptcy of a party and the termination of the contract by the other party. It was suggested that the legal guide should advise the parties to consider whether the bankruptcy of a party should automatically result in termination, and also whether termination should depend upon the stage of the contract at which the bankruptcy occurs (e.g., immediately after conclusion of the contract or during the warranty period).

*Notification*³⁹

117. It was generally agreed that questions of notification should be dealt with when relevant in connection with other substantive matters concerning the contract. The legal guide might include a check-list to alert the parties to

³⁶ A/CN.9/WG.V/WP.7/Add.5, paras. 1-31 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.8/Add.5, paras. 70-76 (reproduced in this volume, part two, IV, B).

³⁷ A/CN.9/WG.V/WP.7/Add.5, paras. 32-44 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 77-78 (reproduced in this volume, part two, IV, B).

³⁸ A/CN.9/WG.V/WP.7/Add.5, paras. 45-54 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 79-80 (reproduced in this volume, part two, IV, B).

³⁹ A/CN.9/WG.V/WP.7/Add.5, paras. 55-95 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 81-85 (reproduced in this volume, part two, IV, B).

aspects of the contract for which formal notification might be required.

118. According to one view the legal guide should recommend that the parties consider including in the contract means for dealing with discrepancies between multiple modes of a particular notification (e.g., letter and telex).

119. It was suggested that the legal guide should advise the parties to avoid inconsistencies in notification requirements in the contract, and to bear in mind provisions of applicable law concerning notification and the extent to which parties may modify these provisions by agreement.

120. It was generally agreed that the parties should be advised to consider whether notification should be deemed effective upon dispatch or upon receipt. One view suggested that the legal guide should take note of the requirement in some legal systems that the notice takes effect when the recipient takes cognizance of the contents of the notification.

Settlement of disputes⁴⁰

121. There was general agreement on negotiation as the first step in the settlement of disputes. The opinion of the Working Group was, however, divided whether the amicable settlement of disputes should be provided for in the contract. It was pointed out that it would not be advisable to stipulate in the contract a time-limit for initiation of legal proceedings as the parties should have a reasonable time for their negotiations.

122. One view suggested that conciliation proceedings would not be advisable as it might postpone the settlement of disputes in legal proceedings. According to another view conciliation should be recommended in the legal guide as it might make possible the settlement of disputes by an agreement of the parties. According to one view joint conciliation might be conducted by conciliators of equal numbers appointed at the request of the disputing parties by the arbitration institutions of their respective countries. It was agreed only to draw the attention of the parties in the legal guide to the possibility of using conciliation and to recommend the application of the UNCITRAL Conciliation Rules for the solution of issues connected with conciliation proceedings. It was also pointed out that conciliation might be used even in cases where a conciliation clause was not included in the contract.

123. The settlement of technical questions by technical experts was discussed. Under one view, these experts might speed up the solution of technical problems without any interruption of the construction of the works. Another view was that it is difficult to distinguish technical and legal problems and that, in some cases, independent or qualified

technical experts might not be available. If technical experts are used it would be advisable to provide that their opinion should not be binding.

124. It was agreed that the legal guide should mention only the main problems connected with agreeing upon exclusive jurisdiction clauses and should draw the attention of the parties to the possibility that public policy issues might be involved. It was noted that in formulating exclusive jurisdiction clauses the problem of the recognition and enforceability of court decisions should be taken into account. One view suggested that the choice of the courts of the purchaser's country might be more convenient. Problems connected with the immunity of States where also mentioned in this connection.

125. Under one view arbitration proceedings offer advantages over judicial proceedings as they are better adapted to the specific features of international trade and arbitral awards can be recognized and enforced abroad often more easily than court decisions. The suggestion was made to recommend the application of the UNCITRAL Arbitration Rules, but also to mention the possibility of using other arbitration rules.

126. The view was expressed that the arbitration proceedings should take place in the purchaser's country. It was suggested to draw the attention of the parties to the existence of arbitration centres in the developing countries. Another view stressed the importance of the choice of qualified arbitrators.

127. It was noted that the enforceability of the arbitral award should be taken into account in choosing the place of arbitration. A suggestion was made to indicate in the legal guide that administered arbitration had certain advantages.

128. It was pointed out that the legal guide should recommend to the parties to provide for the possibility of third parties (e.g., sub-contractors) participating in arbitration proceedings with a view to securing the settlement of interrelated disputes in a single proceeding.

129. There was an exchange of views on the function of the engineer in connection with the settlement of disputes. Some views were expressed that an engineer nominated only by one party could not be considered a neutral person with the power to make final decisions affecting both parties. Another view was that in practice an engineer nominated by only one party had the confidence of both parties and was useful in speeding up the decision-making process in respect of technical questions.

FUTURE WORK

130. There was general agreement that the Secretariat should now commence the drafting of the legal guide. The aim of the work was to produce a guide which was properly researched, readable and well-balanced.

⁴⁰ A/CN.9/WG.V/WP.7/Add.5, paras. 96-149 (reproduced in this volume, part two, IV, B); A/CN.9/WG.V/WP.7/Add.6, paras. 86-93 (reproduced in this volume, part two, IV, B).

131. The Working Group briefly considered the possible structure of the legal guide⁴¹ and decided to examine this topic at its next session. In this connection it was suggested that the subject of scheduling also be considered for inclusion in the legal guide. Under one view the guide should not quote clauses from existing forms and models.

132. The Secretary of the Commission suggested that the next session of the Working Group might be of one week's duration and should be devoted to deciding on the structure of the guide and the approach to be adopted in its drafting. For this purpose, a few sample draft chapters and an outline of the structure of the guide would be submitted

⁴¹ A proposal for a possible structure was submitted by the German Democratic Republic: [A/CN.9/WG.V/III] CRP.3.

to the Working Group. Early decisions on structure and approach would prevent the waste of time and resources.

133. There was general agreement with this suggestion. It was observed, however, that the Governments of developing countries were unlikely to send delegates only to attend a session of one week's duration, and it was recognized that it was extremely important that developing countries should be adequately represented at the session. It was accordingly agreed that the Commission should be requested to decide that the next session of the Working Group should be held at Vienna in the week immediately preceding the commencement of the Commission's sixteenth session. It was recognized, however, that the decision of the Commission on the scheduling of the session of the Working Group might be affected by the Commission's decision as to the length of the sixteenth session.

B. Working paper submitted to the Working Group on the New International Economic Order at its third session (New York, 12-23 July 1982): Study II of the Secretary-General: clauses related to contracts for the supply and construction of large industrial works (A/CN.9/WG.V/WP.7 and Add. 1 to 6)

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Part One

[A/CN.9/WG.V/WP.7*]

INTRODUCTION

1. The present study (hereinafter referred to as "this study") is a supplement to the one submitted to the second session of the Working Group on clauses related to contracts for the supply and construction of large industrial works¹ (hereinafter referred to as "Study I"). The present study has been prepared in conformity with a request by the Working Group which was later endorsed by the Commission.²

2. The general observations contained in the Introduction to Study I³ equally apply to this study and the same approach has been used in preparing it. The discussion of the Working Group on the issues presented in Study I and this study will be taken into account in the drafting of a legal guide by the Secretariat.

3. This study is divided into three parts: introduction (Part One), analysis of topics covered (Part Two) and list

* 15 April 1982.

¹ A/CN.9/WG.V/WP.4 and Adds. 1-8 (Yearbook ... 1981, part two, IV, B, 1).

² A/CN.9/198, paras. 89-91; Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 84 (Yearbook ... 1981, part one, A).

³ A/CN.9/WG.V/WP.4, paras. 1-38 (Yearbook ... 1981, part two, IV, B, 1).

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[A/CN.9/WG.V/WP.7/Add.6]

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of questions on these topics (Part Three). Part Two is contained in Addenda 1-5 and Part Three in Addendum 6 to this document.

4. The same general conditions and model works contracts (hereinafter referred to as "the forms under study") used for Study I are also used as the basis for this study. However, this study further takes into consideration the fact that some issues are also regulated by the following general conditions agreed upon by member countries of the Council for Mutual Economic Assistance (CMEA) and refers to them in analyzing such issues:

(a) General Conditions of Delivery of Goods between Organizations of the Member Countries of the Council for Mutual Economic Assistance, hereinafter referred to as GCD-CMEA;

(b) General Conditions of Assembly and Provision of other Technical Services in connection with Reciprocal Deliveries of Machinery and Equipment between Foreign Trade Organizations of Member Countries of the Council for Mutual Economic Assistance, hereinafter referred to as GCA-CMEA;

(c) General Conditions for Technical Servicing of Machinery, Equipment and other Items Delivered between Foreign Trade Organizations of Member Countries of the Council for Mutual Economic Assistance, hereinafter referred to as GCTS-CMEA.

5. It may be noted that since the completion of Study I the UNIDO International Group of Experts has completed the work on the Model Form of Turnkey Lump Sum Contract for the construction of a fertilizer plant (UNIDO/PC.25), hereinafter referred to as UNIDO-TKL, and the Model Form of Cost Reimbursable Contract for the construction of a fertilizer plant (UNIDO/PC.26), hereinafter referred to as UNIDO-CRC. As the UNIDO Model Form of Semi-Turnkey Contract for the construction of a fertilizer plant is still in a draft form (ID/WG.318/2) and its final form may be adapted in future to the provisions of UNIDO-TKL and UNIDO-CRC, reference to this draft is limited only to issues connected with its semi-turnkey character.

Part Two

[A/CN.9/WG.V/WP.7/Add.1*]

I. FEASIBILITY STUDIES

1. The term "feasibility studies" as commonly used refers to pre-project analyses designed to assist the purchaser in determining whether a contemplated project would be technically and economically viable.¹

2. Contracts for the supply and construction of large industrial works usually do not provide for feasibility studies in this sense. Normally, by the time a purchaser is ready to enter into such a contract these studies will already have been performed, either by the purchaser or by someone engaged to do it for him. In the latter event certain types of studies may be performed by an engineer or other consultant under a contract which is wholly separate from the works contract.

3. However, information obtained during feasibility studies will serve as a basis for the implementation of the supply and construction contract. Moreover, it is not uncommon for the purchaser to provide to the contractor certain data derived from these studies for use in the performance of his obligations. Such contracts often contain provisions allocating as between the parties responsibility for errors and inadequacies in this information, and establishing the extent to which the contractor must control or verify the information obtained or supplied by the purchaser. Some contracts require the contractor to obtain for himself whatever data and information he requires in order to perform the contract, even though this may duplicate some of the studies already performed by the purchaser.

4. The ECE Guide states, in paragraph (iv):

"If the initial studies which culminate in the planning of a project and in the survey and selection of the site are carried out by the *client himself* or by a *design bureau* or by a *consulting engineer*, the client assumes the

responsibility for this preliminary work *vis-à-vis* the supplier of the industrial plant and *vis-à-vis* the building or civil engineering contractor; the contract may also specify that the building or civil engineering contractor is obliged to check the project data concerning the site on his own responsibility."

5. Some contracts assume that, if the purchaser has obtained information during pre-contract feasibility studies, the purchaser must have provided such information to the contractor before the formation of the contract, and provide that the tender is deemed to be based on such information. They also provide that the contractor is deemed to have obtained all the necessary information which might influence his tender. For example, clause 11 of FIDIC-CEC provides:

"The Employer shall have made available to the Contractor with the Tender documents such data on hydrological and sub-surface conditions as shall have been obtained by or on behalf of the Employer from investigations undertaken relevant to the Works and the Tender shall be deemed to have been based on such data, but the Contractor shall be responsible for his own interpretation thereof.

"The Contractor shall also be deemed to have inspected and examined the Site and its surroundings and information available in connection therewith and to have satisfied himself, so far as is practicable, before submitting his Tender, as to the form and nature thereof, including the sub-surface conditions, the hydrological and climatic conditions, the extent and nature of work and materials necessary for the completion of the Works, the means of access to the Site and the accommodation he may require and, in general, shall be deemed to have obtained all necessary information, subject as above mentioned, as to risks, contingencies and all other circumstances which may influence or affect his Tender."

6. Clause 10.1 of FIDIC-EMW is identical to the first paragraph of clause 11 of FIDIC-CEC (quoted in paragraph 5, above). Clause 10.2 of FIDIC-EMW provides:

"The Contractor by tendering shall be deemed to have satisfied himself as to all the conditions and circumstances affecting the Contract Sum, as to the possibility of executing the Works as shown and described in the Contract, as to the general circumstances at the site of the Works, if access thereto has been made available to him, and as to the general labour position at the Site, and to have determined his prices accordingly. The Contractor shall be responsible for any misunderstanding or incorrect information however obtained except information given in writing by the Employer or the Engineer."

7. The UNIDO model contracts call upon the purchaser to supply certain information to the contractor,

* 12 February 1982.

¹ See United Nations Industrial Development Organization (UNIDO), *Manual for the Preparation of Industrial Feasibility Studies* (ID/206) (1978).

much of which might well have been obtained during the purchaser's feasibility studies. In any event the contractor is obliged to obtain all the information necessary to execute the contract. Article 4.4 of UNIDO-CRC provides:

"The PURCHASER shall provide the CONTRACTOR with information pertaining to the suitability of the Site, the applicable laws, rules and regulations, or import restrictions in (PURCHASER's country) that are [sic] available to the PURCHASER. The CONTRACTOR shall review all such information, and obtain such other information as he may consider necessary to carry out his work under the Contract, particularly those bearing on transportation, disposal, handling and storage of Equipment and Materials, availability of water and power for construction purposes, approach roads, physical condition of Site, uncertainty of weather and ground conditions. It shall be the responsibility of the CONTRACTOR in any event to obtain all information required for him to carry out his obligations under the Contract."

8. UNIDO-TKL contains two alternative formulations of a clause dealing with these issues. One of these (article 4.4, Text B) is substantially the same as article 4.4 of UNIDO-CRC. The other one (article 4.4, Text A) is as follows:

"The CONTRACTOR acknowledges that he has fully satisfied himself as to the nature and location and suitability of the Site, the applicable laws, agreements and regulations, the general and local conditions applicable to the CONTRACTOR's works, particularly those bearing upon transportation, disposal, handling and storage of materials, availability of labour, water, electrical power, approach roads and uncertainties of weather or similar physical conditions at Site, the conformation and conditions of the ground and the sub-surface, the character of the Equipment and facilities needed preliminary to, and during the progress of the work and all other matters which can in any way affect the CONTRACTOR's work, Services, obligations, or the costs thereof to the CONTRACTOR under this Contract. The CONTRACTOR further acknowledges that subject to the provisions of Article 4.4.2, he has satisfied himself as to and assumes all risks relating to the quantity and quality of all surface and sub-surface materials, including ground water to be encountered. The CONTRACTOR has reviewed all exploratory work done by or for the PURCHASER and information presented by the drawings and technical specifications and other documentation. Any failure of the Contractor to acquaint himself with all the necessary data and information will not relieve him from his ultimate responsibilities under the Contract, and in any event shall not be cause for any claims for increases in the payments pursuant to the Contract."

9. Under article 5.2 of UNIDO-CRC, the purchaser is to supply data for the "design basis" for the works: much

of this data might well come from information obtained from his prior feasibility studies. The contractor is obligated "to examine the information and data for the design basis so specified, and shall expeditiously advise the PURCHASER on the adequacy and relevance of the information and data provided"

10. In addition, article 4.4.1 of UNIDO-CRC requires the contractor to review the design basis after the conclusion of the contract, and if the review shows "differences in the design basis", then "the PURCHASER and CONTRACTOR shall meet to discuss changes in the Contract specifications and the changes in the CONTRACTOR's obligations or price, if any. These changes will be embodied in a change order . . ."

11. UNIDO-TKL contains two alternative clauses dealing with the provision of and responsibility for the design basis. Article 3.2.2, text A, contrasts with the approach adopted by UNIDO-CRC. This provision is as follows:

"Unless otherwise agreed the CONTRACTOR shall be responsible for the design basis . . . and the CONTRACTOR also agrees and acknowledges that he shall accept final responsibility for the accuracy, suitability and adequacy of the information supplied by the PURCHASER, and shall ensure that the operational characteristics of the Plant are secure and guaranteeable."

Text B of this article states merely that the contractor shall "review the design basis".

12. Other contracts reviewed for this discussion provide additional examples of how contracts may deal with the issue of responsibility for data contained in the purchaser's feasibility studies. As an example, a turnkey contract for the supply of a steel rolling mill by a consortium of companies from a developed country to a developing country holds the contractor responsible for information supplied by him. But he is not responsible for discrepancies, errors and omissions in drawings or other information supplied by him if they arose out of incorrect information or particulars furnished by the purchaser, unless the contractor "could have known or discovered the said discrepancies, errors and omissions". The contract adds that the contractor "shall verify and satisfy himself of any data/information submitted by the [purchaser] of which he has any doubts about its correctness".

II. FORMATION OF CONTRACT

A. General remarks

13. The rules relating to the formation of works contracts are not different from the rules relating to the formation of other types of contracts. Most rules governing the formation of contracts have a mandatory character, and cannot be altered by agreement of the parties. Accordingly, many issues relating to the formation of a works contract

will be determined by the applicable law. A comparative study of the laws relating to the formation of the contract is beyond the scope of this study. It may be noted, however, that parties are free to stipulate certain requirements which must be complied with before the operative part of the contract becomes effective. For example, UNIDO-CRC provides as follows in article 8:

"8.1. The Contract shall become valid upon the formal execution (signing) by duly authorized officers of the Purchaser and Contractor in accordance with the applicable law. The Effective Date of the Contract shall be the date on which the Purchaser's definitive advice to proceed is received by the Contractor which shall occur when the last of the following requirements has been fulfilled:

"8.1.1. Approval of the Contract by the Government of () where the plant is to be located, such approval to be obtained by the Purchaser, if required.

"8.1.2. Approval of the Government of () where the Contractor resides and has his principal place of business, such approval to be obtained by the Contractor, if required.

"...

"8.2. In case the conditions of Article 8.1 hereabove are not fulfilled within () days following the date of signature of the Contract, the Contract execution time and the Contract Price shall be reconsidered and modified by mutual agreement to take into account variations of economic conditions in Contractor's or Purchaser's countries during the delayed period."

A footnote to article 8.2 states that this provision can be used in specific cases.

14. Certain characteristics of works contracts influence the manner in which they are formed. Such contracts are complex, and cover a long-term undertaking. Accordingly, it is necessary to settle more issues than in other types of contracts if the legal position of the parties is not to be uncertain. Furthermore, such contracts are often financed by national or international lending institutions, and these institutions often set terms which affect the formation of the contract. Sometimes approval by a specified governmental authority in the country of construction has to be obtained.

15. As in other areas of international trade, general conditions and model forms have been developing to simplify the formation of works contracts. Because of the unique character of each contract, however, these conditions and models have to be adapted and supplemented by negotiation between the parties.

B. Procedures leading to formation

16. There are currently two procedures used in connection with the formation of works contracts. One consists

of inviting tenders from enterprises interested in contracting with the purchaser, and the other of negotiating the contract with potential contractors or their agents without previously requiring competitive bids from them. The contracts examined assume that a contract has been formed through one or other of these procedures, and also assume that legal issues relating to formation, if they arise, (e.g. when the offer may be revoked, how acceptance must take place) will be regulated by the applicable law.

17. As regards tender procedure, the first stage is usually the invitation to tender. The purchaser may choose the system of open bidding under which the invitation is addressed to all contractors interested in supplying and constructing the required works, or he may prefer a closed bidding system under which the invitation is addressed only to a limited number of potential contractors whom he considers eligible.

18. The tender invitation will describe the works to be supplied and constructed. Tenderers are often requested to include specifically drafted conditions of contract defining the contractual obligations which the contractor is prepared to assume. The invitation will also contain information relating to such matters as the date of opening tenders, the documents to be completed by the tenderers, and special arrangements for visiting and inspecting the site.

19. Tender procedures can give rise to several difficult legal issues. Since such procedures are pre-contractual, contract clauses rarely deal with these issues. Some of the important issues which may arise are:

The circumstances, if any, in which the contractor can withdraw his tender;

The point of time at which a tender is accepted so as to form a valid contract;

The length of time a tender remains open.

20. Only two of the forms examined contained clauses specifically dealing with tenders. Clause 12 of FIDIC-CEC provides:

"The Contractor shall be deemed to have satisfied himself before tendering as to the correctness and sufficiency of his Tender for the Works and of the rates and prices stated in the priced Bill of Quantities and the Schedule of Rates and Prices, if any, which tender rates and prices shall, except insofar as it is otherwise provided in the Contract, cover all his obligations under the Contract and all matters and things necessary for the proper execution and the maintenance of the Works..."

The article requires that the scope of the offer to construct the works made in the tender should be in conformity with the tender invitation.

21. Clause 2.2 of ECE 188A/574A deals with the period of time within which a tender must be accepted, and provides as follows:

"If the Contractor, in drawing up his tender, has fixed a time-limit for acceptance, the Contract shall be deemed to have been entered into when the Purchaser has sent an acceptance in writing before the expiration of such time-limit, provided that there shall be no binding contract unless the acceptance reaches the Contractor not later than one week after the expiration of such time-limit."

22. It may be recalled that, since contracts for the supply and construction of large industrial works are frequently concluded on the basis of public tenders, it had been suggested that the drafting of procurement regulations might be a useful and promising approach for UNCITRAL, and that as the work progressed to a mature stage, such an undertaking may also become a relatively easy task (A/CN.9/WG.V/WP.4, Introduction, paragraph 45, footnote 20).^{*} The legal issues involved in tender procedure may appropriately be considered at a later stage.

III. VARIATIONS

A. General remarks

23. Due to the complex nature of works contracts, and the fact that the time during which they are to be executed is usually long, it may become necessary to make variations more frequently than in respect of other types of contracts.

24. It is understandable that as the works progress the parties, and the engineer, may find that the original drawings need to be varied or modified in order to conform to the quality standards imposed by the contract.² Modifications or variations can also be required because of an error or an omission in the drawings or because the parties decide by mutual agreement that modifications or variations are appropriate in order to achieve the purpose of the project.

25. The applicable law provides under what conditions the contract may be varied. Some of the legal rules on this subject are of a mandatory nature in order to maintain a proper balance in the legal positions of both parties to the contract. Within the limits imposed by the law, the parties are free to agree in the contract on the conditions and the procedure concerning variations. Some of the forms under study contain provisions on these issues. Under most legal systems, a contract may be varied by mutual agreement of the parties. A party can vary the contract unilaterally only in cases permitted by the law.

B. Variation by mutual agreement

26. UNIDO-TKL deals with the case where the contract is varied by mutual agreement following a proposal for variation made by the contractor. Article 15.4 provides:

^{*} Yearbook . . . 1981, part two, IV, B, 1.

² See A/CN.9/WG.V/WP.4/Add.2, VII, *Quality* (Yearbook . . . 1981, part two, IV, B, 1).

"The CONTRACTOR may at any time during his performance of the Contract submit to the PURCHASER for his approval written proposals for a modification of the work to be performed under the Contract. The CONTRACTOR, in connection with any proposal he makes pursuant to this Article . . . , shall furnish the reasons for his proposal and a breakdown in sufficient details to permit an analysis of all material, labour, equipment, sub-contracts and the estimated project time schedule, overruns and design changes, and shall include in such proposal or report all work involved in the modification, whether such work was to be deleted, added or changed. Any request for time extension shall be supported by such justification as may be required."

27. In this case, the variation is effected only if the purchaser approves the contractor's proposal. In certain circumstances, UNIDO-TKL obliges the purchaser to approve. Article 15.6 provides as follows:

"If the PURCHASER approves the CONTRACTOR's proposal, . . . , the CONTRACTOR shall make the variation so approved. The PURCHASER shall not refuse to approve any variation which is necessary to correct any defect in the Works which has occurred or which would otherwise occur if the CONTRACTOR's proposal is not accepted, . . . In all other cases, the PURCHASER may give or refuse his approval as he thinks fit and his decision shall be final."

28. An agreement on variation should cover all the related terms of the contract involved in the variation (e.g. scope of work, time schedule, price).

C. Variation required by the engineer

1. Extent of engineer's authority

29. Under clause 34.1 of FIDIC-EMW the contractor cannot alter any of the works except as directed in writing by the engineer. The engineer is entitled from time to time during the execution of the contract to direct the contractor to alter, amend, omit, add to or otherwise vary the works. The contractor is obliged to carry out such variations and is bound by the same conditions, as far as applicable, as though the variations were stated in the specification attached to the contract. However, if such variations would involve a net addition to or deduction from the contract sum (less provisional sums) of more than 15 per cent thereof, the written consent of the contractor and the purchaser is needed.³

30. Under clause 51(1) of FIDIC-CEC the engineer has even greater authority. He is entitled to make any variation of the form, quality or quantity of the works or any part thereof that may, in his opinion, be necessary, and

³ See A/CN.9/WG.V/WP.4/Add.2, *Quality*, para. 69 (Yearbook . . . 1981, part two, IV, B, 1).

may increase or decrease the quantity of any work included in the contract, omit any such work, change the character or quality or kind of such work, and change the levels, lines, position and dimension of any part of the works. He may also order the contractor to execute additional work of any kind necessary for the completion of the works. The value, if any, of such variations must be taken into account in ascertaining the amount of the contract price.⁴

2. Procedure for variation

31. The procedure for variation to be followed under FIDIC-EMW is described in clause 34.2 which provides as follows:

"If the Engineer shall make any variation in any part of the Works such reasonable notice in writing shall be given to the Contractor as will enable him to make his arrangements accordingly. In cases where Plant is already manufactured or in the course of manufacture, or any work done or Drawings or patterns made require to be altered, a reasonable sum in respect thereof shall be allowed by the Engineer. If, in the opinion of the Contractor, any variation is likely to prevent or prejudice the Contractor from or in fulfilling any of his obligations under the Contract, he shall notify the Engineer thereof in writing and the Engineer shall decide forthwith whether or not the same shall be carried out. If the Engineer confirms his instructions in writing the said obligations shall be modified to such an extent as may be justified. Until the Engineer so confirms his instructions they shall be deemed not to have been given."

32. The procedure to be followed under FIDIC-CEC is provided for in clause 51(2):

"No such variations shall be made by the Contractor without an order in writing of the Engineer. Provided that no order in writing shall be required for increase or decrease in the quantity of any work where such increase or decrease is not the result of an order given under this Clause, but is the result of the quantities exceeding or being less than those stated in the Bill of Quantities. Provided also that if for any reason the Engineer shall consider it desirable to give any such order verbally, the Contractor shall comply with such order and any confirmation in writing of such verbal order given by the Engineer, whether before or after the carrying out of the order, shall be deemed to be an order in writing within the meaning of this Clause. Provided further that if the Contractor shall within seven days confirm in writing to the Engineer and such confirmation shall not be contradicted in writing within fourteen days by the Engineer, it shall be deemed to be an order in writing by the Engineer."

3. Effects of variation

33. Where the contractor disagrees with a decision by the engineer to vary the contract, under clause 49.1 of FIDIC-EMW the contractor has the right to refer such a decision to arbitration. However, the contractor is obliged to proceed in accordance with the decision until it is reversed or varied in arbitration proceedings. Under clause 67 of FIDIC-CEC, the contractor loses his right to refer the engineer's decision to arbitration if he does not communicate to the engineer his claim to arbitration within a period of ninety days after receipt of notice of the engineer's decision. The legal position of the parties in this respect is analysed in Part Two, XXI, *Settlement of disputes*.

34. The variation of the scope of the works may have consequences on the price of the contract. FIDIC-EMW at clauses 34.3 and 34.5 makes a distinction between modified payments resulting from variations which exceed 15% and which do not exceed 15% of the contract sum. If the modified payment does not exceed 15%, the engineer is entitled to authorize payment.

35. When the written consent of the contractor and the purchaser is required for a variation (see paragraph 26, above) the amount of the modified payment shall be agreed upon between the engineer and the contractor. If they cannot come to such an agreement, the engineer is entitled to fix the amount unilaterally (clause 34.5).

36. In FIDIC-CEC, the question of the valuation of the variations is dealt with in clause 52(1), which provides:

"All extra or additional work done or work omitted by order of the Engineer shall be valued at the rates and prices set out in the Contract if, in the opinion of the Engineer, the same shall be applicable. If the Contract does not contain any rates or prices applicable to the extra or additional work, then suitable rates or prices shall be agreed upon between the Engineer and the Contractor. In the event of disagreement the Engineer shall fix such rates or prices as shall, in his opinion, be reasonable and proper."

37. In the event the variations exceed 10% of the contract sum, the revision of the contract sum is dealt with by clause 52.3 of FIDIC-CEC which provides:

"If on certified completion of the whole of the Works it shall be found that a reduction or increase greater than ten per cent of the sum named in the Letter of Acceptance, excluding all fixed sums, provisional sums and allowance for dayworks, if any, results from:

- (a) The aggregate effect of all Variation Orders, and
- (b) All adjustments upon measurement of the estimated quantities set out in the Bill of Quantities, excluding all provisional sums, dayworks and adjustment of price made under Clause 70(1) hereof

⁴ *Ibid.*, para. 70.

but not from any other cause, the amount of the Contract Price shall be adjusted by such sum as may be agreed between the Contractor and the Engineer or, failing agreement, fixed by the Engineer having regard to all material and relevant factors, including the Contractor's Site and general overhead costs of the Contract."

D. *Variation required by the purchaser*

38. In UNIDO-TKL, article 15.1 entitles the purchaser to vary the scope of the works in the following manner:

"The PURCHASER shall have full powers, subject to this Article and other provisions of the Contract from time to time during the execution of the Contract by notice in writing to direct the CONTRACTOR to alter, amend, omit, change, modify, add to or otherwise vary any of the work under the Contract and the CONTRACTOR shall carry out such work and be bound by the same conditions, so far as applicable, as though the said variations were stated in the Contract."

39. Under article 15.2, when in the opinion of the contractor the variation involves a change in the contract price, he must notify the purchaser. The amount of the difference is to be agreed between the contractor and the purchaser, and in the event of a failure to reach agreement is to be settled in accordance with the procedure for the settlement of disputes (article 37).

40. A different procedure is adopted in UNIDO-CRC. Whenever the purchaser makes a request to the contractor for change in design, or where services are required to be performed by the contractor which in his opinion are in addition to services agreed upon or which in the contractor's opinion require additional payment, the contractor is obliged to advise promptly the purchaser of the costs of such services (article 15.1). If the purchaser agrees that such services are in addition to the contractor's obligation under the contract, the purchaser is obliged to pay for them (article 15.2). In addition, UNIDO-CRC specifies certain cases in which the contractor is entitled to claim for additional costs (article 15.3).

41. The contractor must furnish a breakdown in sufficient detail to permit an analysis of factors (e.g. material, labour) involved in the variations (article 15.4) and must also furnish a cost and execution time estimate of the modifications (article 15.5). The purchaser is obliged to agree or to disagree within a certain period of time on the adjustment proposed by the contractor (article 15.5). If the purchaser agrees on the costs, execution time and modified performance guarantees, the contract is considered to be modified accordingly. If the parties do not agree on any of these items, the purchaser has the right to request the contractor to proceed to execute the work pending settlement of the dispute. Article 15.6 of UNIDO-CRC provides a procedure for the settlement of such disputes by indepen-

dent experts without prejudice of the right of either party to submit the dispute to arbitration.

42. Any variation of the contract terms are to be incorporated in a written change order which is to be signed by the purchaser (article 15.7). However, if in the opinion of the contractor such variations are likely to prevent or prejudice the contractor from fulfilling any of his obligations under the contract, he is obliged to notify the purchaser thereto in writing and the purchaser must decide forthwith whether or not the variations are to be carried out. If the purchaser re-confirms in writing his intention to carry out the variations, then the contractual obligations of the contractor are modified to such an extent as may be justified.

E. *Variation required by the contractor*

43. The contractor is not entitled unilaterally to vary contract is not varied unless the purchaser agrees to the variation. However, under certain circumstances, the purchaser is obliged to agree (see paragraphs 26 and 27, above).

IV. INTERPRETATION OF CONTRACTS

A. *General rules on interpretation*

44. Although a contract has been concluded, there may be uncertainty as to the scope of the agreement between the parties. Rules for resolving such uncertainty are found in the applicable law and may be found in usages or in the contract itself.

45. The Sales Convention* provides in article 8 as follows:

"(1) For the purposes of this Convention statements made by and other conduct of a party are to be interpreted according to his intent where the other party knew or could not have been unaware what that intent was.

"(2) If the preceding paragraph is not applicable, statements made by and other conduct of a party are to be interpreted according to the understanding that a reasonable person of the same kind as the other party would have had in the same circumstances.

"(3) In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties."

46. This provision applies to any statement or other conduct which falls within the scope of the Sales Convention, including statements and conduct relevant to the con-

* Yearbook . . . 1980, part three, I, B.

clusion of a contract and its content. Under paragraph (3) of article 8 of the Sales Convention even statements made in the course of negotiations may be relevant to the interpretation of the contract.

47. GCD-CMEA has, however, a different approach, as it provides in article 4 as follows:

"From the moment the contract is concluded all previous correspondence and negotiations for the contract shall become null and void."

48. It might be argued from this stipulation that an exchange of views in correspondence in respect of the content of the contract effected before the conclusion of the contract may not be used for the interpretation of the contract.

49. A similar approach may be found in article 38.1 of UNIDO-TKL which states:

"This Contract supersedes all communications, negotiations, and agreements, either written or oral, relating to the Work and made prior to the date of this Contract."

50. UNIDO-TKL continues in article 38.2:

"The express covenants and agreements herein contained and made by the PURCHASER and the CONTRACTOR are and shall be the only covenants and agreements upon which any rights against the PURCHASER or the CONTRACTOR are to be founded."

Provisions with the same wording are contained in articles 38.1 and 38.2 of UNIDO-CRC and UNIDO-STC.

51. How the parties denominate the contract may be relevant to its interpretation. Certain types of contracts have been developed in the course of international trade. They are not defined by any particular rules but they may be characterized by certain features which they have in common.

52. For example, in determining the extent of responsibility in connection with the supply and construction of large industrial works it may be relevant that the parties denominate the contract as a "turnkey contract". In international trade practice this type of contract may be characterized by an obligation on the contractor to supply all equipment and construction works capable of operating in accordance with the contract terms. Thus, in article 2.1 of UNIDO-TKL the object of the turnkey contract is characterized as follows:

"The object of the Contract is to establish a modern, reliable, efficient and integrated Plant, suitable to the location, for the production of . . . The scope of the Contract covers a turnkey supply, which includes the grant of licence and know-how, to provide basic and detailed engineering to supply all the Plant and Equipment, to design and construct all Civil Works, to erect the Plant and Equipment, to commission and start-up the Plant and

to demonstrate the ability of the Plant to continuously produce . . ."

53. Accordingly, in the absence of a clear limitation of the contractor's responsibility, in a contract denominated as a turnkey contract the contractor is responsible for all documentation and for all persons employed for construction of the works and for co-ordination of activities. The contractor can avoid this responsibility only by proving that the failure to perform was due to a breach of obligation by the purchaser or to exonerating circumstances.⁵

54. In connection with the determination of the price to be paid a distinction may be drawn between "a lump-sum contract" and "cost-reimbursable contract". Normally a lump-sum contract provides that the price stipulated in the contract is to remain applicable under all circumstances regardless of the extent of the work and the costs connected therewith. In a cost-reimbursable contract the price is normally considered in substance to be determined on the basis of costs paid by the contractor. These principles, however, are often modified to a certain extent in both kinds of contracts. In the absence of such modifications, however, where a contract denominated as "lump-sum" or "cost-reimbursable" contains unclear provisions as to the price, such provisions will be interpreted as incorporating the price terms normal to such contracts.

B. Annexures and general conditions

55. The rights and duties of the parties may arise directly from contract provisions or from annexures attached to a contract or from general conditions referred to by a contract. Annexures attached to a contract as well as general conditions referred to in a contract would ordinarily be considered parts of the contract. Contract provisions, the provisions of annexures and general conditions are applied concurrently and are considered to be complementary to each other.

56. However, questions may arise as to the relevance and mutual relationship of contract provisions, annexures and general conditions, particularly in cases where there is a conflict between them.

57. If there is a conflict between contract provisions and the provisions of the annexures article 38.3 of UNIDO-TKL provides that the contract provisions prevail over the contents of annexures:

"The provisions of the Articles of this Contract and the contents of the Annexures shall be complementary to each other, but in the event of any conflict, the provisions of the Articles shall prevail."

The same rules are contained in article 38.3 of UNIDO-CRC and UNIDO-STC.

⁵ See ECE Guide, para. 25.

58. The prevalence of written contract provisions over general conditions in case of their conflict is provided for in clause 1 of ECE 188A/574A. A similar approach may be found to a certain extent in the CMEA General Conditions. The preamble to the General Conditions provides that, in those instances when the parties in making a contract come to the conclusion that because of the specific nature of the goods and/or special characteristics of their delivery a departure from particular provisions of the present General Conditions of Delivery is required, they may so agree in the contract.

C. *Relevance of headings for interpretation*

59. Some forms under study also contain rules on the relevance of the headings of contract provisions, chapters or parts for the interpretation of the contract. FIDIC-CEC in clause 1(3) states:

"The headings and marginal notes in these Conditions of Contract shall not be deemed to be part thereof or be taken into consideration in the interpretation or construction thereof or of the contract."

The same provision is contained in clause 1.4 of FIDIC-EMW.

60. A rule that the headings are not to be used for the interpretation of contract provisions is contained in article 38.5 of UNIDO-TKL which states:

"Article headings appearing herein are included for convenience only and shall not be deemed to be a part of this Contract."

D. *Definitions in contracts*

61. The meaning to be given to some terms used in works contracts is very important for the interpretation of such contracts. These terms are defined in the contract itself for various reasons e.g. because these terms are not defined in the applicable law, or because a special meaning is assigned to the term distinct from the meaning in ordinary usage. It may be useful to note some of the important definitions given in the forms under study.

1. "Contract"

62. In article 1.3 of UNIDO-CRC and UNIDO-TKL the term "contract" is defined as follows:

"'Contract' shall mean this Contract (together with the Annexures) entered into between the PURCHASER and the CONTRACTOR for the execution of the work howsoever made, together with all of the documents to which reference has been made in the Contract documents, including such amendments and/or changes properly made from time to time by mutual agreement between the parties) to the documents constituting this Contract."

63. The FIDIC Conditions introduce a definition of "contract" which is adapted to their nature and contents. FIDIC-EMW defines it in clause 1.1 as follows:

"(g) 'Contract' means the Conditions of Contract, Specification, Drawings, Schedules, Tender, the Letter of Acceptance and the Contract Agreement (if completed)."

64. A similar definition is contained in clause 1(1) of FIDIC-CEC:

"(f) 'Contract' means the Conditions of Contract, Specifications, Drawings, priced Bill of Quantities, Schedule of Rates and Prices, if any, Tender, Letter of Acceptance and the Contract Agreement, if completed."

65. The purpose of all these definitions is to determine what documents are to be taken into consideration in connection with the interpretation of the contractual rights and duties of the parties.

2. "Writing"⁶

66. Most general conditions require works contracts and some legal acts connected with their execution to be in writing. Most of them, however, do not contain a definition of the writing. Only FIDIC-EMW states in clause 1.1 (v):

"'Writing' means any manuscript type-written or printed statement."

67. The Sales Convention* states in article 13:

"For the purposes of this Convention 'writing' includes telegram and telex."

3. "Contractor"

68. In most forms under study the party who is to supply and construct works is called the "contractor". GCD-CMEA and GCTS-CMEA use the term "seller" and GCA-CMEA the term "supplier".

69. In article 1.2 of UNIDO-TKL and UNIDO-CRC the term "contractor" is defined as follows:

"'CONTRACTOR' shall mean the party named as such in this Contract or his successors or permitted assigns."

70. FIDIC-EMW and FIDIC-CEC define the term "contractor" in clause 1.1:

"b. 'Contractor' means the person or persons, firm or company, whose tender has been accepted by the Employer and includes the Contractor's personal representatives, successors and permitted assigns."

71. A significant result of the definitions is that they permit certain categories of persons other than the original contractor to take his place. Assignment must, however, be effected in accordance with the contract.

* Yearbook, . . . 1980, part three, I, B.

⁶ See Part Two, XX, *Notification*, B.

4. "Purchaser"

72. There is no uniformity in the denomination of the person for whom works are to be supplied and constructed. In most forms under study the term "purchaser" is used. The FIDIC Conditions, however, call this person the "employer". GCD-CMEA and GCTS-CMEA prefer the term "buyer" and GCA-CMEA the term "client".

73. UNIDO-TKL and UNIDO-CRC define the term "purchaser" in article 1.1 as follows:

"PURCHASER" shall mean the party named as such in this Contract or his successors or permitted assigns."

74. In FIDIC-EMW and FIDIC-CEC the definition of "employer" is contained in clause 1.1:

"a. 'Employer' means the party named in Part II who will employ the Contractor and the legal successors in title to the Employer, but not, except with the consent of the Contractor, any assignee of the Employer."

75. These definitions have the result mentioned in paragraph 71.

5. "Sub-contractor"

76. Under clause 1.1 of FIDIC-EMW the term "sub-contractor" is defined as follows:

"c. 'Sub-Contractor' means any Nominated Sub-Contractor (as defined in Clause 39.1) or any person firm or company (other than the Contractor) named in the Contract for any part of the Works or any person to whom any part of the Contract has been sub-let with the consent in writing of the Engineer, and the Sub-Contractor's legal personal representatives, successors and permitted assigns."

77. Clause 39.1 of FIDIC-EMW referred to in clause 1.1. includes persons employed by the contractor for execution of any work or supplying any goods, materials or services and who have been nominated, selected or approved by the employer or the engineer.⁸

78. The term "sub-contractor" is defined in article 1.32 of UNIDO-CRC and in article 1.34 of UNIDO-TKL as follows:

"Sub-Contractor" shall mean any person or firm to whom any part of the CONTRACTOR's Services or the execution of any part of the Contract is sub-contracted by the CONTRACTOR."

6. "Engineer"

79. The legal position of a consulting engineer is different in the various forms under study.⁹ Under article 1.17 of UNIDO-TKL the term "engineer" is defined as follows:

"Engineer" shall mean the person(s) or firm(s) appointed from time to time and designated by the PURCHASER as its representative with specified authority to review all work on the PURCHASER's behalf and to give such instructions and/or grant such approvals as may be necessary for the purposes of this Contract."

80. In UNIDO-CRC the technical advisor has a similar legal position as the engineer in UNIDO-TKL. Article 1.17 of UNIDO-CRC states:

"Technical Advisor" shall mean the person(s) or firm(s) appointed from time to time by the PURCHASER as his representative with the specified authority to review all work on the PURCHASER's behalf and give such instructions and/or grant such approvals as may be necessary for the purposes of this Contract."

81. FIDIC-EMW contains definitions of the terms "engineer" and "engineer's representative" in clause 1.1 which provides:

"d. 'Engineer' means the person firm or company appointed by the Employer to act as Engineer for the purposes of the Contract and designated as such in Part II.

"e. 'Engineer's Representative' means any resident engineer or assistant of the Engineer appointed from time to time by the Employer or the Engineer to perform the duties set forth in Clause 2 hereof whose authority shall be notified in writing to the Contractor by the Engineer."

82. A similar definition is contained in clause 1(1) of FIDIC-CEC:

"(c) 'Engineer' means the Engineer designated as such in Part II, or other the Engineer appointed from time to time by the Employer and notified in writing to the Contractor to act as Engineer for the purposes of the Contract in place of the Engineer so designated.

"(d) 'Engineer's Representative' means any resident engineer or assistant of the Engineer, or any clerk of works appointed from time to time by the Employer or the Engineer to perform the duties set forth in . . . whose authority shall be notified in writing to the Contractor by the Engineer."

83. Some functions of the engineer under the FIDIC Conditions are performed to a certain extent by a "neutral independent person" or an "independent consultant" under the UNIDO model contracts. The manner of their appointment, however, is different as the appointment must be agreed upon by both parties. A definition of these terms is contained in article 1.23 of UNIDO-CRC and article 1.23 of UNIDO-TKL:

"Neutral Independent Person" or "Independent Consultant" shall mean a third party selected by the CONTRACTOR and PURCHASER by mutual agreement to carry out functions in accordance with the Contract, . . ."

⁷ See Part Two, VI, *Sub-contracting*.

⁸ *Ibid.*, para. 18, for clause 39.1 of FIDIC-EMW.

⁹ See Part Two, VIII, *Engineer*.

7. "Works", "plant", and "equipment"

84. In connection with the interpretation of the provisions concerning the execution of the works contract, some forms under study contain definitions of the term "works", the term "plant", the term "equipment" and other terms connected with the scope of the contract.

85. In clause 3.2 containing the expression "construction or erection of the Works", ECE 188A/574A refer to a footnote in which definitions of the terms "plant" and "the works" are given. Under these definitions, the term "plant" means all machinery, apparatus, materials and articles to be supplied by the contractor under the contract and the term "the works" means all plant to be supplied and work to be done by the contractor under the contract.

86. Similar definitions of the terms "plant" and "works" are contained in clause 1.1 of FIDIC-EMW which states:

"e. 'Plant' means machinery, apparatus, materials, articles and things of all kinds to be provided under the Contract other than Contractor's equipment.

"f. 'Works' means all Plant to be provided and work to be done by the Contractor under the Contract."

87. Definition of the terms "works" and "plant" in FIDIC-CEC are adapted to the subject of these Conditions, i.e. civil engineering construction. Clause 1(1) contains the following definitions:

"(e) 'Works' shall include both Permanent Works and Temporary Works.

"...

"(h) 'Constructional Plant' means all appliances or things of whatsoever nature required in or about the execution or maintenance of the Works but does not include materials or other things intended to form or forming part of the Permanent Works.

"(i) 'Temporary Works' means all temporary works of every kind required in or about the execution or maintenance of the Works.

"(j) 'Permanent Works' means all the permanent works to be executed and maintained in accordance with the Contract."

88. Under UNIDO-TKL the term "works" is used as a broad notion which includes the term "plant". In article 1.38 the term "works" is defined as follows:

"Work(s) shall mean the whole of the Work(s) equipment, Plant (as defined in this Article) and matters and things to be done, furnished, performed, accomplished and provided by the CONTRACTOR (inclusive of his services under this Contract)."

89. Furthermore, article 1.28 of UNIDO-TKL, taking into consideration that this model contract is to be used only for construction of a fertilizer plant, defines "plant" as follows:

"'Plant' shall mean the Ammonia plant, the Urea plant, the Off-sites and the administrative, maintenance, laboratory and other facilities as defined in this Sub-article and in the Annexures, to be supplied by the CONTRACTOR under the terms of this Contract, to be constructed at the Site and in respect of which the CONTRACTOR's Services are provided.

"1.28.1 'Ammonia Plant' shall mean the facilities for the production of ammonia, as described in Annexure ...

"1.28.2 'Urea Plant' shall mean the facilities for the production of Urea as described in Annexure ..."

90. UNIDO-CRC does not use the term "works" in determining the object of the contract and defines only the term "plant" in article 1.27:

"'Plant' shall mean the Ammonia Plant, the Urea Plant and the Off-Sites, as defined in this Sub-Article and in the Annexures, to be constructed at the Site, and in respect of which the CONTRACTOR's Services are provided.

"1.27.1 'Ammonia Plant' shall mean the facilities for the production of ammonia, as described in Annexure ...

"1.27.2 'Urea Plant' shall mean the facilities for the production of urea as described in Annexure ...

"1.27.3 'Off-Sites' shall mean the facilities demarcated and indicated in the Annexures and the plot plan attached to Annexure ..."

91. In UNIDO-CRC there is a definition of the term "equipment". Article 1.18 states:

"'Equipment' shall mean all the equipment, machinery, instruments, commissioning equipment and spares, and all the other items required for incorporation in the Plant, or required to operate the Plant in order for the Plant to be built and operated in accordance with the Contract, and in respect of which the CONTRACTOR has provided procurement services."

92. Taking into account the obligation of the contractor to supply the equipment in a turnkey contract, article 1.18 of UNIDO-TKL provides:

"'Equipment' shall mean all the equipment, machinery, instruments, commissioning equipment and spares, and all the other items to be supplied by the CONTRACTOR for incorporation in the Plant, or

required to operate the Plant in order for the Plant to be built and operated in accordance with the Contract."

93. In connection with the work to be done by the contractor the UNIDO model contracts also contain definitions of the term "contractor's services" and the term "civil works". Under article 1.13 of UNIDO-TKL and UNIDO-CRC the term "contractor's services" is defined as follows:

"'CONTRACTOR's Services' shall mean the services to be provided and the work to be done by the CONTRACTOR in the execution of the works, as set out in the Contract."

94. The term "civil works" is defined in article 1.8 of UNIDO-TKL and UNIDO-CRC as follows:

"'Civil Works' shall mean all the buildings, roads, foundations and any other work requiring Civil Engineering."

8. "Contractor's equipment"

95. A distinction is drawn in the UNIDO model contracts and FIDIC-EMW between the term "equipment" and the term "contractor's equipment". The definition of "contractor's equipment" can be found in article 1.11 of UNIDO-CRC and UNIDO-TKL.¹⁰

96. A similar definition is contained in clause 1.1 of FIDIC-EMW which states:

"k. 'Contractor's Equipment' means all appliances or things of whatsoever nature required for the purpose of the Works but does not include plant, materials or other things intended to form or forming part of the Works."

9. "Site"

97. UNIDO-TKL and UNIDO-CRC define the term "site" as a land upon which the works are to be constructed and presuppose that a specification thereof is to be contained in an annexure to the contract.

98. FIDIC-EMW defines the term "site" in clause 1.1 as follows:

"q. 'Site' means the lands and other places on, under, in or through which the Works are to be executed or carried out, and any other lands and places provided by the Employer for the purposes of the Contract, with such other places as may be specifically designated in the Contract as forming part of the Site."

99. A similar definition is contained in clause 1(1) of FIDIC-CEC:

"(m) 'Site' means the land and other places on, under, in or through which the Permanent Works or

Temporary Works designed by the Engineer are to be executed and any other lands and places provided by the Employer for working space or any other purpose as may be specifically designated in the Contract as forming part of the Site."

E. Language

100. A works contract is sometimes concluded in several languages as its provisions and annexures are to be applied by personnel of more than one nationality. In this connection the parties may agree which language is to be authentic for the interpretation of the contract provisions.

101. Article 35.1 of UNIDO-TKL and UNIDO-CRC states:

"The governing language of the contract shall be (), and the definition in such language shall be final in the use and interpretation of the terms of the Contract."

102. Clause 4.1 of FIDIC-EMW states:

"The language or languages in which the Contract documents shall be drawn up shall be stated in Part II of these Conditions and if the said documents are written in more than one language the language according to which the Contract is to be construed and interpreted shall also be designated in Part II, being therein designated the 'Ruling Language'."

103. In particular annexures to the contract and the documentation attached thereto are used by personnel employed by each party and clarification may be needed as to the language to be used. UNIDO-TKL and UNIDO-CRC stipulate in article 35.2:

"All correspondence, information, literature, data, manuals etc. required under the Contract shall be in the () language."

104. The problem of languages also arises in connection with personnel used for co-ordinating the work and training the purchaser's personnel. Article 35.3 of UNIDO-TKL and UNIDO-CRC provides:

"All expatriates sent by the Contractor to the Site, and all personnel sent by the Purchaser for training shall be conversant in the () language."

[A/CN.9/WG.V/WP.7/Add.2*]

V. ASSIGNMENT OR TRANSFER OF CONTRACT

A. General remarks

1. Under most legal systems, a party to a contract may not, without the consent of the other party, validly assign the contract to a third party, substituting for himself the

¹⁰ See A/CN.9/WG.V/WP.4/Add.1, III, *Erection*, para. 75 (Yearbook ... 1981, part two, IV, B, 1).

* 12 February 1982.

third party as a party to the contract.¹ In addition, a party is usually not permitted to avoid specific obligations under the contract by unilaterally assigning them to a third party. On the other hand, many legal systems recognize the right of a party to assign his benefits under the contract. These general principles may be modified by the terms of the contract.

B. Assignment of contract

2. The UNIDO model contracts permit the parties to assign the contract under certain conditions. For an assignment by the contractor, the written consent of the purchaser is required (article 9.2 of both UNIDO-TKL and CRC). The purchaser may assign the contract without having to obtain the contractor's consent,

"provided that such assignment does not increase the CONTRACTOR's liabilities over what they would have been if such assignment or transfer had not been made, and provided that the obligations of the PURCHASER are binding upon the assignee, . . . with assured guarantees for payment(s) under the Contract." (Article 9.3 of both UNIDO-TKL and CRC).

3. In the event of an assignment of the contract either by the contractor or by the purchaser, the UNIDO model contracts expressly provide (in article 9.1. of both UNIDO-TKL and CRC) that:

"This Contract shall inure to the benefit of and be binding upon the parties hereto and each of their executors, administrators, curators, successors and assigns . . ."

4. The FIDIC Conditions also require the written consent of the purchaser for an assignment of the contract by the contractor, but stipulate that this consent "shall not be unreasonably withheld" (clause 3.1 of FIDIC-EMW and clause 3 of FIDIC-CEC). No provision is made for assignment by the purchaser.

C. Assignment of contractual benefits

5. The FIDIC Conditions require the purchaser's written consent ("which shall not be unreasonably withheld") for an assignment by the contractor of "the Contract or any part thereof or any benefit, or interest therein or thereunder" (clause 3 of FIDIC-CEC; clause 3.1 of FIDIC-EMW), with certain exceptions.

6. Under both FIDIC Conditions, the contractor may, without having to obtain the purchaser's consent, assign any monies due or to become due under the contract by a charge in favour of the contractor's bankers (clause 3 of FIDIC-CEC and clause 3.1 of FIDIC-EMW). It is normal for contractors to finance their execution of the works by way of bank loans given on the security of payments to

be received under the contract. The ability of the contractor to assign such payments is thus necessary in order to obtain such financing.

7. In addition, clause 3.1 of FIDIC-EMW permits the contractor to subrogate insurers to his rights under the contract, without having to obtain the consent of the purchaser. Such subrogation will ordinarily be required under the insurance policies covering the contractor and his work. This provision does not appear in FIDIC-CEC.

VI. SUB-CONTRACTING

A. General remarks

8. Generally, in the context of the supply and construction of large industrial works, a sub-contracting relationship exists when a party to the main contract engages a third party to perform certain of the former's obligations under the contract. Some of the forms under study include in their concept of sub-contracting the procurement of materials and equipment in connection with the contract.²

9. Although it is more common in industrial works projects for the contractor to perform his obligations vicariously through third parties, in some situations the purchaser may also do so (see paragraph 34, below). In this chapter, such vicarious performance by the purchaser will also be considered.

10. The liability of parties for the acts of sub-contractors, and persons employed by sub-contractors, is considered in IX, *Parties' Liabilities in Respect of Third Parties*.

B. Sub-contracting by contractor

1. Selection of sub-contractor

11. The selection of a sub-contractor is a matter of interest to both the contractor and to the purchaser. The contractor bears ultimate responsibility for the quality of the work to be performed under the contract, and is ordinarily liable to the purchaser for defective work of the sub-contractors. It is important to him that a sub-contractor be chosen who possesses the technical and financial capabilities to perform the work satisfactorily. The purchaser's interest in the capabilities of the sub-contractor are less concrete than that of the contractor. A major reason for a purchaser's employment of a main contractor, rather than himself letting out individual contracts to specialists, is to benefit from the contractor's expertise in investigating potential sub-contractors and soliciting and evaluating tenders from them and co-ordinating their work. The purchaser customarily relies to a large extent on the ability of

¹ Such an assignment may also be described as a transfer of the contract, though the forms under study do not use this term.

² See UNIDO-CRC, article 4.12, quoted in para. 35, below; for the definition of "sub-contractor" in the forms under study, see Part Two, IV, *Interpretation of Contract*, paras. 76-78.

the contractor to identify qualified sub-contractors. The purchaser's ability to hold the contractor responsible for faulty performance by the sub-contractor makes this reliance possible.

12. In the case of a cost-reimbursable contract, the interest of the purchaser in the selection of a sub-contractor arises more from his concern to secure a competitive price for the work to be performed by the sub-contractor. Often, when a main contractor submits a tender to the purchaser for the contractor, the sums contained in the tender price for work to be sub-contracted are only provisional. This is because a contractor will not usually have enough time during the tender period to investigate and evaluate tenders from potential sub-contractors. These provisional sums are subject to variation in accordance with the actual extent and cost of the work sub-contracted. The purchaser therefore has an interest in seeing that the sub-contractor ultimately selected is one who can perform the work at a competitive price.

13. In the forms under study, the interests of both parties in the selection of a sub-contractor are accommodated by having both parties participate in the selection process. The degree of each party's participation varies. In some contracts, the contractor is free to choose his own sub-contractors, being required merely to inform the purchaser of sub-contracting. In others, sub-contracts may be concluded by the contractor only with the approval of the purchaser or his engineer. Finally, some contracts allow the contractor to sub-contract only with sub-contractors designated by the purchaser or engineer. In such instances the contractor is normally able to object to such a designation, particularly if the sub-contractor will not or cannot assume the same obligations and give the same warranties to the contractor as the contractor must give to the purchaser.

14. It is emphasized that even though a purchaser may participate in selecting a sub-contractor, even to the extent of designating sub-contractors, the purchaser does not normally thereby assume liability for the performance or conduct of the sub-contractor. The sub-contracts are usually concluded by and in the name of the contractor, and no contractual obligations normally exist between the purchaser and the sub-contractor. The contractor remains liable for the work of the sub-contractor.

15. The FIDIC Conditions contain general provisions requiring the prior written consent of the engineer for most sub-contracting by the contractor, and confirming the liability of the contractor for the performance and conduct of the sub-contractor. Clause 3.2 of FIDIC-EMW and clause 4 of FIDIC-CEC contain the following language:

"The Contractor shall not sub-let the whole of the Works. Except where otherwise provided by the Contract, the Contractor shall not sub-let any part of the Works without the prior written consent, of the Engineer (which shall not be unreasonably withheld). Any

such consent, if given, shall not relieve the Contractor from any liability or obligation under the Contract and he shall be responsible for the acts, defaults and neglects of any Sub-Contractor, his agents, servants or workmen as fully as if they were acts defaults or neglects of the Contractor, his agents, servants or workmen . . ."

16. Clause 3.2 of FIDIC-EMW states, however, that the restrictions on sub-contracting do not apply to "sub-contracts for materials, for minor details or for any part of the Works of which the makers are named in the Contract." FIDIC-CEC does not contain this exception. Rather, it excludes from the operation of its clause 4 "the provision of labour on a piece-work basis".

17. In addition to the general requirement of the engineer's consent, the FIDIC Conditions grant to the engineer specific powers in respect of work or supplies for which a "provisional sum" is designated in the contract. As explained in paragraph 12 above, certain sums comprising the contractor's tender price are only provisional, and are subject to modification depending upon the extent to which the work is actually performed, and the price actually charged by the sub-contractor ultimately selected.

18. The sub-contractors who supply the materials or services for which provisional sums are included in the contract price are termed by the FIDIC Conditions "nominated sub-contractors". Specifically, "nominated sub-contractors" are defined as follows: (FIDIC-EMW, clause 39.1; FIDIC-CEC, clause 59.1):

"All specialists, merchants, tradesmen and others executing any work or supplying any goods, materials or services for which Provisional Sums are included in the Contract, who may have been or be nominated or selected or approved by the Employer or the Engineer, and all persons to whom by virtue of the provisions of the Contract the Contractor is required to sub-let any work shall, in the execution of such work or the supply of such goods, materials or services, be deemed to be Sub-Contractors employed by the Contractor and are referred to in this Contract as Nominated Sub-Contractors."

19. The FIDIC Conditions also provide that the contractor is not obligated to employ any nominated sub-contractor against whom he raises a reasonable objection, and who declines to undertake, and to indemnify the contractor with respect to, the same obligations and liabilities arising from the sub-contracted work as the contractor owes to the purchaser, and to indemnify the contractor against the negligence or misuse of the contractor's equipment or constructional plant or works by the sub-contractor. Clause 39.2 of FIDIC-EMW provides:

"The Contractor shall not be required by the Employer or the Engineer or be deemed to be under any obligation to employ any Nominated Sub-Contractors whose

performance warranties are not acceptable to the Contractor or against whom the Contractor may raise reasonable objection, or who shall decline to enter into a sub-contract with the Contractor containing provisions:

"(a) that in respect of the work, goods, materials or services the subject of the Sub-Contract the Nominated Sub-Contractor will undertake towards the Contractor the like obligations and liabilities as are imposed on the Contractor towards the Employer by the terms of the Contract and will save harmless and indemnify the Contractor from and against the same and from all claims, proceeding, damages, costs, charges and expenses whatsoever arising out of or in connection therewith, or arising out of or in connection with any failure to perform such obligations or to fulfil such liabilities. Provided that nothing in this paragraph shall entitle the Contractor to object to a Nominated Sub-Contractor who requires that the liabilities and indemnities to the Contractor shall be limited pro rata to the Sub-Contract price.³

"(b) that the Nominated Sub-Contractor will save harmless and indemnify the Contractor from and against any negligence by the Nominated Sub-Contractor, his servants or agents, and from and against any misuse by him or them of any Contractor's Equipment⁴ provided by the Contractor for the purposes of the Contract and from all claims as aforesaid."

20. Clause 59 (2) of FIDIC-CEC contains comparable provisions, the major differences being noted in the footnotes to the above paragraph.

21. UNIDO-TKL differentiates between types of work which may not be sub-contracted without the written consent of the purchaser, and work which may be sub-contracted merely by advising the purchaser of such sub-contracts.

22. With respect to sub-contracting requiring the purchaser's written consent, article 9.4 provides:

"The CONTRACTOR shall not sub-contract the whole or any part of the Work and/or services relating to the design of the Plant, procurement of the Equipment, start-up, operation or any tests of the Plant and the Equipment (as defined in the Contract) with respect to the Works, without the written consent of the PURCHASER..."

23. As to some of the equipment to be procured from sub-contractors subject to the purchaser's consent under article 9.4 (paragraph 22 above), the contract itself identifies the sub-contractors from whom this equipment is to be procured. Article 12.1.7 provides:

³ The last sentence is omitted from FIDIC-CEC (clause 59 (2) (a)).

⁴ For the words "Contractor's Equipment" FIDIC-CEC substitutes "Constructional Plant or Temporary Works" (clause 59 (2)(b)).

"The PURCHASER and CONTRACTOR agree that certain items of Equipment shall be obtained by the CONTRACTOR from selected Vendors only. The list of these items and the selected sub-contractors from whom they shall be procured are provided in Annexures ... The Contractor shall procure these items from such sub-contractors only, unless otherwise agreed in writing between the CONTRACTOR and PURCHASER."

As to these items, therefore, the specific vendors will have been selected by the agreement of the contractor and purchaser.

24. With respect to the procurement of equipment for which a specific vendor is not designated in the contract, articles 10.1.3 through 10.1.7 of UNIDO-TKL specify the bidding procedure to be followed. The contractor must prepare bid documents on the basis of the technical specifications prepared by him and submit them to the purchaser for his approval. They are then issued to prospective vendors who are listed in a "Vendor's list" which has been previously agreed to by the parties. The contractor must use his best endeavours to obtain a minimum of three competitive offers. The offers received from the vendors are evaluated by the contractor, who makes the final selection of the vendor.

25. UNIDO-TKL makes special provision for the procurement of spare parts by the contractor.⁵

26. Under UNIDO-TKL, the contractor need not obtain the consent of the purchaser in order to sub-contract for work other than that specified in article 9.4 (see paragraph 22, above). He must merely advise the purchaser of such sub-contracts. Article 9.5 provides:

"The CONTRACTOR may sub-contract any other work or services under the Contract, provided the PURCHASER is advised of all such sub-contracts. Where sub-contracts are to be awarded to firms or individuals in (PURCHASER's country), the PURCHASER shall have the right to pre-qualify all firms or persons bidding for such sub-contracts. If the CONTRACTOR so desires, the PURCHASER shall pre-qualify such firms or persons at the time of signing of the Contract."

2. *Compatibility of sub-contract with main contract*

27. Very often a contractor will cover his liabilities to the purchaser in respect of the sub-contractor by requiring the sub-contractor to indemnify him against these liabilities. This is done by including such indemnity provisions in the contract between the contractor and the sub-contractor. The FIDIC Conditions contain clauses concerning such provisions. Clause 39.3 of FIDIC-EMW provides:

"If in connection with any Provisional Sum the services to be provided include any matter of design or speci-

⁵ See Part Two, XI, *Maintenance and Spare Parts*, paras. 42-49.

fication of any part of the Works or Plant to be incorporated therein, such requirement shall be expressly stated in the Contract and shall be included in any Nominated Sub-Contract. The Nominated Sub-Contract shall specify that the Nominated Sub-Contractor providing such services will save harmless and indemnify the Contractor from and against the same and from all claims, proceedings, damages, costs, charges and expenses whatsoever arising out of or in connection with any failure to perform such obligations or to fulfil such liabilities, but not so as to impose upon the Sub-Contractor any greater liability to the Contractor than the Contractor has to the Employer under these Conditions."

FIDIC-CEC, clause 59(3), contains a comparable provision.

28. Such a provision in the main contract cannot itself create obligations for the sub-contractor, who is not a party to the main contract. Its purpose, however, is two-fold. First it is designed to incorporate within the main contract the specifications of the work to be performed by the sub-contractor and any warranties, guaranties and other obligations in respect of this work which the sub-contractor owes toward the contractor. This will ensure that for a failure by the sub-contractor in respect of a particular specification or obligation contained in the sub-contract, the purchaser will be able to claim against the contractor. In addition, the provision is designed to ensure that after incorporation of the specifications and the indemnity in the sub-contract if liabilities are enforced by the purchaser against the contractor in respect of work performed by a sub-contractor, the contractor will, in turn, be able to recover against the subcontractor. However, the sub-contractor is not to be subject to greater liabilities to the contractor than the contractor has to the purchaser.

3. *Payment for sub-contracted work*

29. As explained in paragraph 12 above the contract price under the FIDIC conditions includes "provisional sums" for work to be sub-contracted. These forms provide that the costs actually incurred by the contractor in respect of his sub-contracts shall be included in the price to be paid to him by the purchaser:

"For all work executed or goods, materials or services supplied by any Nominated Sub-Contractor or purchased by the Contractor . . . , there shall be included in the sums paid to the Contractor:

"(a) the actual price paid or due to be paid by the Contractor, on the direction of the Engineer, and in accordance with the Sub-Contract;

"(b) in respect of all other charges a sum being a percentage of the actual price paid or due to be paid calculated at the rates inserted by the Contractor in the Appendix to the Tender." (FIDIC-EMW, clause 39.4.)

FIDIC-CEC, clause 59(4), contains comparable provisions.

30. Under the FIDIC Conditions, as in most contracts, the purchaser does not normally pay the sub-contractor directly; he is paid by the contractor. There may be instances, however, in which the purchaser wishes to pay a sub-contractor directly, as when the contractor has failed to pay previous sums due to the sub-contractor and the smooth progress of the contract programme is threatened by a reluctance of the sub-contractor to continue to work. Unless the main contract expressly authorizes the purchaser to pay a sub-contractor directly and deduct the sums so paid from payments due to the contractor, a purchaser who does pay a sub-contractor directly places himself in peril, since he will remain liable to pay the same sum to the contractor:

31. The FIDIC Conditions deal with this situation by permitting the purchaser to pay a sub-contractor directly if the contractor without reasonable cause has failed to make payments previously due to the sub-contractor, and authorizing the purchaser to deduct such payments from amounts due to the contractor. Clause 39.5 of FIDIC-EMW provides:

"Before issuing any certificate, which includes any payment in respect of work done or goods, materials or services supplied by any Nominated Sub-Contractor, the Engineer shall be entitled to demand from the Contractor reasonable proof that all payments, less retentions, included in previous certificates in respect of the work or goods, materials or services of such Nominated Sub-Contractor have been paid or discharged by the Contractor, and unless the Contractor shall:

"(a) satisfy the Engineer in writing that he has reasonable cause for withholding or refusing to make payments and

"(b) produce to the Engineer reasonable proof that he has so informed such Nominated Sub-Contractor in writing;

"the Employer shall be entitled to pay such Nominated Sub-Contractor direct, upon the certificate of the Engineer, all payments, less retentions, provided for in the Sub-Contract, which the Contractor has failed to make to such Nominated Sub-Contractor and to deduct by way of set-off the amount so paid by the Employer from any sums due or which may become due from the Employer to the Contractor.

"Provided always that, where the Engineer has certified and the Employer has paid direct as aforesaid, the Engineer shall in issuing any further certificate in favour of the Contractor deduct from the amount thereof the amount so paid direct as aforesaid but shall not withhold or delay the issue of the certificate itself when due to be issued under the terms of the Contract."

Clause 59(5) of FIDIC-CEC contains comparable provisions.

C. *Sub-contracting by or on behalf of purchaser*

32. In many types of works projects, the purchaser

is responsible for the supply of certain materials or equipment or the performance of certain work. He does not always perform these obligations himself. In some cases, he directly engages third parties to perform certain of his contractual obligations; in others the contractor is obligated to procure supplies or services from third parties on behalf of the purchaser.⁶

33. The purchaser under UNIDO-CRC has substantial responsibilities in connection with the supply and construction of the works. This model contract contains provisions dealing with sub-contracting in respect of two of these responsibilities — erection of the plant, and supply of equipment and materials. The model contemplates that the purchaser will contract directly with third parties for services in connection with erection of the plant. Procurement of equipment and materials is to be done by the contractor on behalf of the purchaser.

1. *Direct sub-contracting by purchaser*

34. With respect to the purchaser's obligations regarding erection of the works, article 5.13 of UNIDO-CRC states that sub-contractors are to be appointed by the purchaser from a list of firms agreed to by the contractor and the purchaser:

"The Plant shall be erected by the PURCHASER or by such other party/parties appointed by the PURCHASER (from a list of pre-qualified parties mutually agreed between the CONTRACTOR and the PURCHASER), under the supervision of the CONTRACTOR's personnel."

2. *Procurement by contractor on behalf of purchaser⁷*

35. Unlike UNIDO-TKL, according to which the contractor is obliged to supply equipment and materials for the works, under UNIDO-CRC the contractor procures equipment and materials "on behalf of the PURCHASER" and "on the PURCHASER's account" (article 4.12). The full text of this article is as follows:

"The CONTRACTOR will procure all Equipment and Materials on behalf of the PURCHASER in accordance with the procurement provisions and procedures laid down in the Contract . . . Notwithstanding the fact that the purchase is ultimately to be made on the PURCHASER's account, the CONTRACTOR shall be obligated to ensure that all procurement is accomplished so as to enable the Plant to meet the [contract] objectives . . . subject to the PURCHASER carrying out his obligations. The CONTRACTOR shall also assist the PURCHASER

in obtaining remedial action from Vendors (where such is necessary) and the CONTRACTOR's Services for any required procurement and/or inspection shall be discharged free of additional costs to the PURCHASER. However, this Article shall not be construed as imposing a liability on the CONTRACTOR for non-fulfilment of the obligations of Vendors, except where such non-fulfilment is due to incorrect or inappropriate instructions issued by the CONTRACTOR, or to a defect in the purchase orders issued to Vendors by the CONTRACTOR, or issued with his approval."

36. Article 10.2 of UNIDO-CRC specifies the procedure to be followed for the procurement of equipment and materials:

(a) The purchaser and contractor pre-qualify vendors (a minimum of three and a maximum of eight, unless the parties agree otherwise) in the following manner. The contractor submits to the purchaser a list of companies pre-qualified by him, indicating his reasons for rejecting any prospective vendors. The purchaser may add to or subtract from this list.

(b) The contractor prepares the bid documents on the basis of the technical specifications prepared by him. If the purchaser's representatives are available at the contractor's offices, they shall approve such specifications. The contractor then submits the bid documents to the purchaser or engineer for approval.

(c) Once the bid documents have been approved, the contractor sends them to the vendors listed in the list of vendors. The contractor must use his best endeavours to obtain a minimum of three competitive offers, except for "critical items".

(d) The contractor evaluates the offers received and makes appropriate recommendations to the purchaser. It is the purchaser who makes the final selection of a vendor.

37. Article 10 also deals with the selection by the purchaser of a vendor who is not acceptable to the contractor:

"The PURCHASER shall endeavour to preclude the selection of Vendors who are unacceptable to the CONTRACTOR. The CONTRACTOR shall, however, substantiate the reasons for such unacceptability (if any) so as to enable the PURCHASER to re-evaluate the choice of such Vendor(s). The CONTRACTOR agrees and acknowledges that guarantee provisions and other criteria established by this Contract shall not be prejudiced as a result of any difference arising between the PURCHASER and the CONTRACTOR as regards the final selection of the Vendor(s), however, that the CONTRACTOR has the right to request for modifications to the Performance Guarantee requirements of the Contract reasonably commensurate with the circumstances." (Article 10.2.5)

⁶ The liabilities of the parties in respect of the purchaser's sub-contractors are discussed in Part Two, IX, *Parties' Liabilities in Respect of Third Parties*.

⁷ Procurement of equipment and materials is considered to constitute sub-contracting by some of the forms under study (see para. 8 above).

"In case the PURCHASER intends to select a Vendor who is not acceptable to the CONTRACTOR, the CONTRACTOR shall indicate the specific changes in his guarantee or other obligations, if any, which would result from such selection. The PURCHASER shall thereafter still have the choice of purchasing the equipment from the selected Vendor subject to the reservations of, and modifications of the obligations of the CONTRACTOR." (Article 10.2.6)

38. Under UNIDO-TKL, most procurement is to be done by the contractor in his own name. However, spare parts are to be procured by the contractor on behalf of the purchaser. These provisions are discussed in Part Two, XI, *Maintenance and Spare Parts*, paragraphs 42-47.

D. Joint and several liability of contractors

39. Distinct from the legal relationship described in the foregoing paragraphs is the situation in which the purchaser concludes works contracts with two or more contractors. If separate contracts are concluded with each contractor it is clear that each contractor is obliged to perform only what he undertook in his contract. If the purchaser concludes only one contract with two or more contractors questions would arise as to whether the contractors are jointly liable to the purchaser for the performance of all of the contractors' obligations, or whether each contractor is liable only in respect of his own obligations. In both cases, this question would depend upon the terms of the contracts concerned and the applicable law.

40. If due to the nature of the work to be performed under a contract it can be effected only through the joint action of the contractors, or if joint liability of contractors is stipulated in the contract, the contractors are jointly liable under most legal systems and the purchaser may demand the entire performance to be effected by any of them.

41. On the other hand, if each contractor is obliged to perform a distinct and separate portion of construction of the works then he is not responsible for the performance of other contractors even if they are all parties to the same contract.

VII. CO-ORDINATION AND LIAISON AGENTS

A. General remarks

42. On account of the complexity and long duration of works contracts, and the fact that they resemble a "joint-venture", co-ordination of the performances of the two parties to the contract is essential. To ensure this co-ordination both parties retain the services of different persons (herein called liaison agents) to act for them during the execution of the contract. The nomenclature and the role of these persons may vary. Some have full legal powers to

represent the party in whose name they are acting. Others have limited powers and functions, and are employed to ensure communication and co-operation between the parties in the execution of the contract.

B. Co-ordination procedures

43. Article 6.1 of UNIDO-TKL describes the duty to co-ordinate as follows:

"The parties to this Contract hereby agree to undertake all reasonable co-operation to implement the Works as stipulated in the Contract. The parties to the Contract through their designated representatives will meet periodically to take stock of the progress of the Work, and suggest ways and means to improve the operations and to expedite the Work and resolve outstanding issues between the parties. Minutes of meetings shall be recorded and circulated for confirmation and necessary action."

Article 6.1 of UNIDO-CRC has a similar content.

44. Co-ordination procedure is dealt with in article 6.5 and 6.6 of UNIDO-TKL which provides that:

"6.5 Within 30 days from the Effective Date of the Contract a meeting shall be held in (PURCHASER's country) between the CONTRACTOR and the PURCHASER and/or the Engineer to discuss all matters of common interest, including but not restricted to the finalization of co-ordination procedure ...

"6.6 The co-ordination procedure (which shall be prepared in accordance with accepted international practice) shall become part of the Contract by reference, following agreement and respective approval by the CONTRACTOR and the PURCHASER."

Article 6.5 of UNIDO-CRC has a similar content to article 6.5 of UNIDO-TKL quoted above.

45. Article 6.7 of UNIDO-TKL provides that the co-ordination procedure shall cover many matters incidental to execution of the contract (e.g. giving instructions; decisions and approvals; submission of documents; drawings and documents distribution; invoicing of payments).

C. Duties and powers of liaison agents

46. The general duty of a liaison agent is to be present on site during working hours, to establish contact with his counterpart appointed by the other party and in general to check performance of the contract and to ensure smooth progress. The exact scope of his authority to act for the party he represents will vary with the role assigned to him. Thus clause 13 of ECE 188A/574A only gives the liaison agent the function of communication:

"13.1 The Contractor and the Purchaser shall each designate in writing a competent representative to be his channel of communication with the other party on the day-to-day execution of the works on the site.

"13.2 Each such representative shall be present on or near the site during working hours."

47. In contrast, article 13.2 of UNIDO-TKL gives extensive powers to the contractor's representative:

"13.2 The CONTRACTOR (as represented by a duly authorized person on its behalf) shall be constantly on Site during working hours, until Provisional Acceptance of the Works has been issued and such person shall devote its (*sic*) entire time to the superintendence of this work. Such authorized person shall have appropriate authority to act for and bind the CONTRACTOR . . ."

48. Article 13.4 provides for representatives of the purchaser to be vested with similar powers.

49. Various provisions in the forms under study envisage the appointment of agents with limited powers for specific purposes:

(a) Representatives appointed by the employer for inspection of equipment and materials (UNIDO-TKL, article 14.11);

(b) Representatives of either the purchaser or the contractor authorized to sign a change order (UNIDO-TKL, article 15.12);

(c) Representatives of the purchaser appointed to review the civil works, and to assure themselves that the work is being conducted with suitable materials and in the approved manner (UNIDO-TKL, article 25.4);

(d) Engineers to represent the purchaser to examine and approve procurement procedures, and to be present during the detailed design of the plant, and the procurement of equipment and materials (UNIDO-CRC, article 6.10 and 6.13);

(e) Project managers appointed by each party to co-ordinate and monitor the work (UNIDO-TKL, article 6.2).

VIII. ENGINEER

A. General remarks

50. The complex character of a works contract and its execution makes the services of technical experts essential. Such services will be needed at the various stages of the project e.g. the design stage, the negotiating stage or the execution stage. The services needed may be of various kinds e.g. drawing up of project programmes, evaluation of tenders, supervision of erection and co-ordination of activities. The forms under study provide for the supply of these services by a consulting engineer.

51. Most forms under study provide that the engineer is to be employed by and is to represent the purchaser. Where, however, the contractor is under a duty to co-ordinate the supply of equipment and services, the services of

an engineer may be used by the contractor as well. Furthermore, under the FIDIC Conditions, the engineer is given, to some extent, the role of a person independent of the contracting parties and with authority to decide on certain questions which may involve a conflict of interests between the parties, and affect their rights and obligations.

B. Engineer as purchaser's representative⁸

52. Under UNIDO-TKL, the engineer is a representative of the purchaser. Thus article 1.17 defines "engineer" as a person or firm appointed and designated by the purchaser as his representative. The "technical advisor" envisaged in UNIDO-CRC has a similar role to the engineer under UNIDO-TKL. Article 1.17 of UNIDO-CRC provides that he is authorized to review all work on the purchaser's behalf and give instructions and grant approvals which may be necessary for the purposes of the contract.⁹

53. The FIDIC Conditions also contain a number of provisions under which the engineer acts as the purchaser's representative. Thus clause 2.1 of FIDIC-EMW states:

"The Engineer shall carry out such duties in issuing decisions, certificates and orders as are specified in the Contract. If the Engineer is required under the terms of his appointment by the Employer to obtain the specific approval of the Employer for the execution of any part of his duties under the Contract, this shall be set out in Part II of these Conditions."

54. Under FIDIC-EMW the engineer may to a limited extent delegate his functions to a representative (clause 2.2 and 2.3).

C. Engineer's functions as representative of purchaser

55. Several articles in UNIDO-TKL determine the engineer's functions and scope of authority. Thus he is entitled:

(a) To give technical approvals or instructions on behalf of the purchaser (article 6.3);

(b) To authorize third parties to check the work of the contractor under certain conditions (article 13.14);

(c) To have access to the works and to be provided with full information concerning the progress and execution of the work (article 13.6).

56. Some of the functions conferred on the engineer by FIDIC-EMW are the following:

(a) Documents and programme

Approval of drawings (clause 5.1)

Inspection of drawings (clause 5.3)

⁸ For the definition of "engineer" in the forms under study, see Part Two, IV, *Interpretation of Contracts*, paras. 79, 81-82.

⁹ See Part Two, IV, *Interpretation of Contracts*, para. 79.

Setting out of the works in relation to original points, lines and levels of reference (clause 7.2)

Approval of programme (clause 12.1)

Revision of programme (clause 12.3)

Verification of insurance policies covering loss or damage to the works (clause 17.1)

(b) *Execution of the works*

Power to object to the contractor employing any persons for the execution of the works who, in the opinion of the engineer, is negligent or incompetent (clause 13.2)¹⁰

Instructions and orders as to proceeding with the works (clause 11)

Authorization of deliveries of the plant and equipment to the site (clause 26.1)

Order to suspend and to resume works (clause 27.1 and 27.3)

Grant of an extension of time to complete (clause 30)

Consent to the removal of contractor's equipment (clause 36.1).

(c) *Inspection and tests*

Inspection and testing of material and workmanship (clause 25.1)¹¹

Attendance at tests on completion (clause 29)

Inspection of repairs (clause 15.1 (a))

(d) *Failure of performance by contractor*

Notify contractor of existence of defects or damage appearing during the defects liability period (clause 33.3)

Consent to the removal from the site of a defective or damaged portion of the works or plant (clause 33.6)

57. FIDIC-CEC contains provisions conferring on the engineer similar functions.

D. *Engineer's decisions as independent person*

58. The FIDIC Conditions empower the engineer to make decisions on certain issues affecting the parties as an independent person (see paragraph 51, above).

(a) *Variation and change in scope of work*

59. The engineer may authorize a variation of the works where such variation does not involve an addition to or deduction from the contract sum of more than 15% (clause 34.1).¹²

(b) *Authorization of payment*

60. Under clause 34.4, the engineer is entitled to authorize payment to the contractor for additional work. Under clause 34.5 he is entitled to fix the sum owed to or by the contractor where the variation made requires an additional payment, or a deduction in payment, of more than 15% of the contract sum.¹³ Under clause 38.1 and 38.2 he is entitled to decide how the provisional sum (a sum designated for the execution of work or the supply of goods, materials or services at the discretion of the engineer) is to be used. He also issues interim and final certificates of payment (clause 37.1, 37.3, 37.8 and 37.9).

61. The engineer is further entitled to determine the amount to be paid to the contractor for making good damage to the works caused by special risks (clause 47.2). If the cost of performance to the contractor is increased or decreased by a change in laws or regulations in the country of the manufacture of the plant or the country where the site is located, such increase or reduction may be added to or deducted from the contract sum on certification by the engineer (clause 52.2).

(c) *Certification of performance*

62. The engineer bears the responsibility of evaluating the performance of the contract, and issuing or withholding certain certificates relating thereto. Thus he may certify the existence of adverse physical conditions and artificial obstructions encountered by the contractor (clause 24), or that the contractor is defaulting in performance (clause 44.1).

63. FIDIC-CEC contains similar provisions empowering the engineer to make decisions on certain issues as an independent person.

64. The role of the engineer in adjudicating on actual disputes between the parties is considered in Part Two, XXI, *Settlement of Disputes*.

E. *Engineer's obligations when making decisions*

65. Under the FIDIC Conditions, whenever the engineer is required to exercise a discretion he is required to observe certain standards in reaching his decision. Thus clause 2.4 of FIDIC-EMW provides:

"Whenever by these Conditions the Engineer is required to exercise his discretion, by the giving of a decision, opinion, consent or to express satisfaction or approval, or to determine value or otherwise take action which may affect the rights and obligations of either the Employer or the Contractor the Engineer shall exercise such discretion fairly within the terms of the Contract and having regard to all the circumstances. If either party disagrees with the action taken by the Engineer he shall

¹⁰ See A/CN.9/WG.V/WP.4/Add.1, III, *Erection*, para. 92 (Yearbook... 1981, part two, IV, B, 1).

¹¹ *Ibid.*, VIII, *Inspection and Tests*, para. 10.

¹² See Part Two, III, *Variation*, paras. 29-30.

¹³ *Ibid.*, para. 35.

be at liberty to refer the matter to Arbitration in accordance with these Conditions."

66. The FIDIC Conditions do not deal with the consequences of a failure by the engineer to perform his duties, either as the representative of the purchaser, or when acting as an independent person.

IX. PARTIES' LIABILITIES IN RESPECT OF THIRD PARTIES

A. General remarks

67. It is common in contracts for the supply and construction of large industrial works for the parties to perform many of their contractual obligations through the use of third parties. Due to the complexity and specialized nature of large industrial works projects, the parties often engage sub-contractors to perform much of the work.¹⁴ Moreover, materials, equipment and supplies required in the performance of the contract are usually procured from third-party vendors.

B. Contractor's liabilities to purchaser in respect of performance by third parties

68. Work performed by all third parties engaged by a contractor, whether categorized as employees, sub-contractors, or vendors, is usually deemed to be performed by the contractor himself, and the contractor is fully liable to the purchaser in respect of this work.

69. Conceptually, sub-contracting by the contractor constitutes the vicarious performance of the contractor's obligations under the contract. As a general proposition, therefore, the contractor is liable to the purchaser for work performed by the sub-contractor, as he would have been had he performed this work himself.

70. The UNIDO model contracts confirm this general principle:

"The CONTRACTOR shall ensure that every sub-contracting by the CONTRACTOR shall comply with all terms and conditions of this Contract." (UNIDO-TKL, article 9.6, UNIDO-CRC, article 9.5.)

71. The liabilities imposed by the contract upon the contractor towards the purchaser for quality and guarantees as to equipment and materials apply irrespective of whether the equipment and materials are supplied by the contractor himself or by vendors engaged on his behalf.¹⁵

C. Contractor's indemnities to purchaser for damage to other persons and their property

72. In addition to holding the contractor liable for the performance of his employees and sub-contractors, some of the forms under study require the contractor to indemnify the purchaser against liability for damage caused in connection with the execution of the contract by them to others for which the purchaser must pay compensation.

73. In some forms this indemnity is limited to damage caused by negligence. Article 22.1 of UNIDO-CRC provides:

"The CONTRACTOR shall indemnify and hold harmless the PURCHASER and anyone employed by him from and against all claims, demands, losses, costs, damages, actions, suits, expenses (including legal fees) or proceedings by whomsoever made for personal injuries, death or third party property damage, brought or prosecuted in any manner based upon, arising out of, related to, or occasioned by the negligent act or omission of the CONTRACTOR or his Sub-Contractors and their employees in connection with this Contract."

74. FIDIC-EMW also imposes on the contractor liabilities for personal injury or property damage caused in connection with the execution of the contract by the negligence of his sub-contractors. The relevant clauses are as follows:

"The Contractor shall . . . indemnify the Employer in respect of death or injury to any person and of all damages to any property (other than property forming part of the Works not yet taken over) occurring before all the Works shall have been taken over and against all actions, suits, claims, demands, costs, charges and expenses arising in connection therewith that shall be occasioned by the negligence of the Contractor or any Sub-Contractor or by defective design . . . materials or workmanship but not otherwise. Provided that the Contractor shall not be liable by virtue of this Sub-Clause in respect of damage or injury attributable to defects in any Section or Portion of the Works taken over." (Clause 15.3.)

"If there shall occur any loss of or damage or injury to any property (other than property forming part of the Works not yet taken over) or person while the Contractor is on the Site for the purpose of making good a defect in any Section or Portion of the Works . . . or for the purpose of carrying out Tests on Completion of any such Section during the Defects Liability Period . . . the Contractor shall be liable . . . as follows:

" . . .

"(b) In respect of damage or injury to any other property or to any person and of any actions, claims, demands, costs, charges and expenses arising in connection therewith the Contractor shall be liable to the ex-

¹⁴ See Part Two, VI, *Sub-contracting*.

¹⁵ This is also the approach adopted in article 79 of the Sales Convention (Yearbook . . . 1980, part three, I, B). These relevant provisions are quoted in A/CN.9/WG.V/WP.4/Add.5, XIII, *Exoneration*, paras. 19-21 (Yearbook . . . 1981, part two, IV, B, 1). See also A/CN.9/WG.V/WP.4/Add.2, VII, *Quality*, para. 46 (Yearbook . . . 1981, part two, IV, B, 1).

tent that such damage or injury was caused by the negligence of the Contractor or a Sub-Contractor while on the Site as aforesaid or by defective materials or workmanship used in making good the said defect but not otherwise..." (Clause 15.4.)

"If there shall occur, after the commencement of the Defects Liability Period in respect of any Section or Portion of the Works, any loss of or damage or injury to any property (other than property forming part of the Works not yet taken over) or person as a result of a cause occurring prior to the commencement of the Defects Liability Period the Contractor's liability... shall be as follows:

"...

"(b) In respect of damage or injury to any property or to any person and of any actions, claims, demands, costs, charges and expenses arising in connection therewith the Contractor shall be liable to the extent that such damage or injury was caused by the negligence of the Contractor or a Sub-Contractor or by defective design... materials or workmanship but not otherwise." (Clause 15.5)

75. In UNIDO-TKL negligence is not mentioned. Article 22.1 of that form provides:

"The CONTRACTOR shall indemnify and hold harmless the PURCHASER and anyone employed by him from and against all claims, demands, losses, costs, damages, actions, suits, expenses (including legal fees) or proceedings by whomsoever made, brought or prosecuted in any manner based upon, arising out of, related to, occasioned by or attributable to the activities of the CONTRACTOR under or in connection with this Contract.

"22.1.1 For the purpose of Article 22.1 above, 'activities' includes an act improperly carried out, an omission to carry out an act and a delay in carrying out an act."

D. Contractor's responsibility for safety

76. UNIDO-TKL imposes on the contractor responsibility for compliance with safety regulations by third parties engaged by him, and for the safety of persons employed by him and by his sub-contractors. Article 4.33 provides:

"Throughout the execution of the Work(s), the CONTRACTOR shall ensure that he, his employees, agents and invitees and his Sub-Contractors, their employees, agents and invitees while upon the Site comply with all applicable safety laws, rules and regulations. The conduct and safety of all persons employed by the CONTRACTOR and his Sub-Contractors on the PURCHASER's premises for reasons relating to this Contract, shall be the sole responsibility of the CONTRACTOR."

Article 4.24 of UNIDO-CRC contains comparable provisions.

E. Contractor's responsibility for sub-contracting on behalf of purchaser

77. Under UNIDO-CRC the contractor procures equipment and materials from third party vendors on behalf of the purchaser.¹⁶ In this situation there exists a contractual relationship between the vendor and the purchaser, and the vendor is directly responsible to the purchaser for the quality and performance of the equipment and materials. The contractor's responsibility to the purchaser in this regard is limited to endeavouring to obtain adequate warranties from the vendor, and assisting the purchaser in obtaining remedial action from the vendor. Unless there is an error or defect on his part, the contractor is not liable to the purchaser for non-fulfilment of the obligations of the vendor. This is confirmed by articles 4.12¹⁷ and 28.1. The latter article provides:

"In inviting bids for the Equipment and Materials, the CONTRACTOR shall use his best endeavours to ensure that adequate warranties for mechanical soundness and guarantees for performance are given to the PURCHASER by the successful Vendor. The PURCHASER acknowledges that the Equipment purchased from the Vendors is not warranted by the CONTRACTOR. However, the CONTRACTOR shall assist the PURCHASER in obtaining and enforcing warranties and guarantees to ensure satisfactory performance of the Equipment supplied by the Vendors, if (*sic*) when (a) issuing the purchase order(s), (b) during inspection of the Equipment, (c) on completion and during test running in Vendor's shops (if any), (d) at the time of taking delivery of the Equipment and (e) operating the Plant; provided the deficiency, inadequacy or defects are noticed within the period of warranty."

78. Similarly, article 29.9 of UNIDO-CRC provides, with respect to equipment, materials and parts obtained on behalf of the purchaser:

"If any defect is found during inspection (before despatch) of Equipment or Materials of Vendor, or during erection or pre-commissioning tests at the Site of the Plant, the CONTRACTOR shall immediately advise the PURCHASER as to what action should be taken to have the Vendors replace defective equipment, defective parts, or inadequate Material in the shortest possible time. The CONTRACTOR shall assist the PURCHASER in facilitating any action which may be necessary in such circumstances. If any defect is found in the Vendor's equipment, machinery, spare parts or Materials within the period when the guarantee is valid, the CON-

¹⁶ See Part Two, VI, *Sub-Contracting*, paras. 35-38.

¹⁷ Quoted in Part Two, VI, *Sub-Contracting*, para. 35.

TRACTOR shall assist the PURCHASER in immediately undertaking the necessary measures to have the Vendor(s) replace the defective Equipment, Material, machinery or spare parts within the shortest possible time, including the air freighting of the equipment or parts etc. at Vendor's cost."

F. Purchaser's indemnities to contractor against liabilities to others

79. Under UNIDO-CRC the purchaser must indemnify the contractor with respect to liabilities arising out of his and his sub-contractor's negligence, and that of their employees. Article 22.2 provides:

"The PURCHASER shall indemnify and hold harmless the CONTRACTOR, his employees and agents from and against all claims, demands, losses, costs, damages, actions, suits or proceedings arising out of the CONTRACTOR's activities under this Contract for personal injuries, death (other than to CONTRACTOR's personnel) and property damage (other than to the Plant) arising out of the PURCHASER's and his Sub-Contractors' and their employees' negligence."

[A/CN.9/WG.V/WP.7/Add.3*]

X. TECHNICAL ASSISTANCE

A. General remarks

1. The expression "technical assistance" is not a term of art and is used to cover different types of services rendered in the field of works contracts. In its narrow connotation it involves the training of personnel and management. In a broader context, it covers assistance in not only commercial but also general matters pertaining to the efficient organization of the works.¹

2. Because of the skills and knowledge that are invariably needed to ensure the proper functioning and maintenance of a large industrial plant, provision is often made for technical assistance. Indeed, such assistance is vital to the fulfilment of the objectives of works contracts. The degree of technical assistance required depends on the type of industry and the state of technological services available in the purchaser's country.

B. Technical assistance

3. The types of technical assistance to be rendered pursuant to the objectives of a works contract vary in detail in each particular contract. However, there are two aspects of technical assistance which are commonly found in works contracts, i.e. training and management.

1. Training

4. The crucial period to begin training should be before the start-up of production as the purchaser's personnel should be familiar with all the operational and technical aspects of production.

5. Both UNIDO-TKL and UNIDO-CRC contain only a general provision on training. The training of the purchaser's personnel by the contractor must be of a standard which is adequate for operating and maintaining the plant (UNIDO-TKL, articles 4.30 and 16.4; UNIDO-CRC, articles 4.19 and 16.4). It is the responsibility of the contractor to prepare a plan for technical training (UNIDO-TKL, annexure XVIII; UNIDO-CRC annexure XVIII) and also arrange for overseas training of the purchaser's personnel (UNIDO-TKL, article 16.3, annexure XVIII; UNIDO-CRC, article 16.3, annexure XVIII). The details of such training, however, are to be agreed upon at a future date. Article 16.4 of UNIDO-TKL reads:²

"The PURCHASER and the CONTRACTOR shall agree at the first co-ordination meeting contemplated under Article 6.8, the time, place and details to be established for the training of the PURCHASER's personnel and final details for training shall be forwarded to the PURCHASER within () months following the Effective Date."

6. According to the UNIDO model contracts the purchaser is to provide personnel to be trained, with qualifications and experience recommended by the contractor and agreed to by the purchaser (UNIDO-TKL, article 16.5; UNIDO-CRC, article 16.5). Provision is also made for the specific type and duration of training (UNIDO-TKL, article 16.2, annexure XVIII; UNIDO-CRC, article 12.3 and 16.2, annexure XVIII).³

2. Management services

7. To fulfil the objectives of the contract, provision is usually made for management services. The kind and extent of such services would again depend on the particular type of contract.

8. UNIDO-TKL provides an example of management services for a particular type of turnkey works contract. Two stages of management services are envisaged. In the first stage the contractor manages the operations of the plant following the mechanical completion stage. This management ceases upon the successful completion of the performance guarantee tests and provisional acceptances of the works by the purchaser (UNIDO-TKL, article 17.1).

9. At the second stage, i.e. from provisional acceptance until final acceptance of the works, the type of

* 12 February 1982.

¹ See A/CN.9/191, para. 79 (Yearbook . . . 1980, part two, V, B); Trade/GE.1/R.22/Rev.1, paras. 8-9.

² A similar provision is contained in article 16.4 of UNIDO-CRC.

³ The cost of training is dealt with in Part Two, XIII, Price.

management services provided by the contractor is called "management assistance services" (UNIDO-TKL, article 17.2).

10. In contrast to the first stage, during the second stage the contractor does not manage the operations himself but only assists the purchaser and provides such personnel as is necessary. Article 17.3 provides for the number and type of staff required and stipulates that the number and type of the contractor's personnel to be maintained at site for the purposes of management assistance must, as far as practicable, be selected by the contractor and the purchaser from the category of personnel who have been responsible for the actual start-up and operation of the plant up to and including the performance guarantee tests.

11. As this is a period (before final acceptance) during which the plant must reach a certain standard before it will be finally accepted, certain obligations are imposed on the contractor in regard to management assistance. Article 17.4 UNIDO-TKL provides:

"The CONTRACTOR's obligations pursuant to the requirements of Article 17.2 shall be as follows:

"17.4.1 Provide Management Assistance to the PURCHASER to ensure maintenance of production levels at optimum capacity, and with maximum efficiency.

"17.4.2 Provide Management Assistance to the PURCHASER to assure maintenance of the Plant and the Equipment to enable operations to be kept at design levels of production, and efficiency ratios.

"17.4.3 Provide Management Assistance to the PURCHASER through in-plant training of PURCHASER's personnel."

12. Provision is also made for the purchaser to retain part or all of the personnel covered by article 17.3 (paragraph 10, above) for an extended period on terms and conditions to be mutually agreed in advance and upon the payment of additional fees to the contractor (UNIDO-TKL, article 17.6).

13. UNIDO-CRC contains a similar management services provision. However, it is an optional clause at the instance of the purchaser. The purchaser is given the option to obtain management assistance following provisional acceptance of the plant until final acceptance (UNIDO-CRC, articles 3.1.31 and 17).

3. Other technical assistance

14. Since technical assistance must be tailored to each individual contract it is beyond the scope of this study to consider the particular kinds of technical assistance required for each contract.

15. It is important that even after final acceptance the efficiency of the operations of the plant be maintained and

that any improvements that could subsequently be made to the plant be implemented.

16. In UNIDO-TKL the purchaser has the option, after final acceptance, of entering into a separate agreement with the contractor for the provision of technical advisory services "upon mutually agreed terms" including the following matters: provision of senior advisory personnel to conduct half-yearly review of plant and efficiency of its operations; recommendations as to improvement of plant operations; and provision of answers to technical queries related to plant operations (UNIDO-TKL, article 17.7, 17.7.1, 17.7.2, and 17.7.3; UNIDO-CRC, articles 4.28 and 17.3).

17. Questions may arise as to the legal validity of such an option on the ground of certainty of terms. The option is to be "upon mutually agreed terms" and this may be too vague under some legal systems.

18. The technical advisory services agreement is to become effective immediately following final acceptance of the plant if the option is exercised (UNIDO-TKL, article 17.7; UNIDO-CRC, article 17.3). The purchaser may exercise the option not later than one month following provisional acceptance (UNIDO-TKL, article 17.7). In UNIDO-CRC, the option must be exercised not later than the expiry of one month before final acceptance (UNIDO-CRC, article 17.3).

19. The rights and obligations envisaged in such an agreement for technical advisory services are to be considered wholly separate and distinct from the liabilities and responsibilities contained in the main contract (UNIDO-TKL, article 17.7; UNIDO-CRC, article 17.4).

C. Confidential information

20. The nature of a technical assistance contract may be such that technical information of a confidential nature may be communicated to the purchaser. Where this is envisaged, there is usually a clause against the disclosure of such information to a third party without the written consent of the contractor not only during the term of the agreement but also thereafter. Problems connected therewith are similar to those concerning transfer of technology, which has been dealt with in Study I.⁴

21. There is usually a provision that all inventions and technical information communicated by the contractor to the purchaser will remain the property of the contractor and that the purchaser is to use such inventions and technical information in accordance with the contract provisions.

XI. MAINTENANCE AND SPARE PARTS

A. Maintenance and repairs

22. The proper maintenance of a plant will ensure its effective operation and optimum life. Maintenance con-

⁴ See A/CN.9/WG.V/WP.4/Add.2, VI, *Transfer of Technology*, paras. 19-26 (Yearbook . . . 1981, part two, IV, B, 1).

siderations include repairs and an adequate support for spare parts. We are here concerned with maintenance repairs which the contractor undertakes although not in breach of any of his obligations.

23. Thus clause 49(2) of FIDIC-CEC provides that, during the period of maintenance or within fourteen days after its expiration, the contractor can be required to rectify defects. As these defects do not result from a breach of obligation by the contractor, clause 49(3) of FIDIC-CEC provides that the value of the repair work is to be ascertained and paid for as if it were additional work. Furthermore, clause 50 of FIDIC-CEC provides that the contractor can be required to search for the cause of any defect appearing during the period of maintenance, and if the defect is one for which the contractor is not liable under the contract, the cost of search is to be borne by the employer.⁵

24. The maintenance of a plant after taking over may be problematical, particularly where there is a scarcity of skilled personnel and spare parts. Also, if many large items of equipment are obtained from a number of different sources, the problem may be further aggravated.

B. Spare parts

1. General remarks

25. The question of spare parts requires careful consideration by parties to a works contract as the operation of a plant is expected to last over a period of time, and replacements may be necessary.

26. Not every works contract contains a provision on spare parts (hereinafter referred to as "spares provision"). Even where such a provision exists, it would appear that the types of problems that may arise have not always been fully explored or provided for by the parties. In recent years, however, there seems to be a growing realization of the importance of a spares provision. At least three documents published by UNIDO raise this question.⁶ It is also noteworthy that in a recent publication by FIDIC entitled *Notes on Documents for Electrical and Mechanical Works Contracts* (1980),⁷ which "have been produced during the process of reviewing the Conditions of Contract (International) for Electrical and Mechanical Works"⁸ (FIDIC-EMW) it was recommended that the subject "[s]pecification" should deal with the provision of spare parts for the Plant.⁹

⁵ See Part Two, XIV, *Revision of Price*, para. 49.

⁶ *Contract Planning and Organization* (United Nations publication, Sales No. E.74.II.B.4), pp. 38-40; *A Guide to Industrial Purchasing* (United Nations publication, Sales No. E.72.II.B.19), p. 42; *Guidelines for Contracting for Industrial Projects in Developing Countries* (United Nations publication, Sales No. E.75.II.B.3), pp. 27-28, 161-163.

⁷ Published by the International Federation of Consulting Engineers, The Hague, Netherlands.

⁸ *Notes on Documents for Electrical and Mechanical Works Contracts*, note 7 above, Foreword.

⁹ *Ibid.*, p. 40.

2. Some problem areas

27. Some of the problems that may be encountered in regard to the question of spare parts are:¹⁰

Long delivery periods for spare parts;

Non-availability of spare parts from the contractor during the anticipated working life of the plant;

Changes in design which might lead to uncertainty of obtaining identical components at some future date, after initial purchase of the plant;

Methods of ensuring that the contractor would undertake to provide spare parts that are compatible with the equipment originally provided and that the spare parts will not downgrade the system or equipment performance;

Assurance of early information to the purchaser regarding future development of component parts which would render certain parts of the plant obsolete;

Whether spare parts can or should be obtained from a third source;

Whether the contractor should object to the purchaser buying spare parts directly from, say, the manufacturer instead of through the contractor;

Determination of the cost of spare parts over a period of time;

Determination of "spares scaling" i.e. what scales of spare parts should be ordered initially and at a given period;

Possibility that the owner of the proprietary rights might licence the production and sale of the plant or equipment to another supplier;

Position where large items of plant or equipment are obtained from a number of different sources;

"Non-standard" spare parts — the need to procure production drawings to enable the local manufacturer to produce such non-standard spare parts;

Restriction on obtaining spares from others;

Allied problem of maintenance and training programmes.

28. Apart from the UNIDO model contracts, none of the forms under study contains spares provisions. Of the works contracts in the Secretariat's collection only a few were found to contain spares provisions. It may be noted that the spares provisions under study do not deal with all the problems stated in paragraph 27. This is not to say that these problems exist in every contract. However, it is not clear from the provisions examined whether the parties have considered the whole gamut of problems that may arise in their particular contract.

29. The spares provisions under study, however, reveal a number of areas which appear to merit some attention.

30. It may be desirable to classify various types of spare parts since special provisions may be made in regard

¹⁰ Some of these problems are mentioned in some UNIDO publications. See note 6 above.

to certain types of spares. For example, a contractor may be asked to guarantee the availability of certain important spare parts or a special procedure may be required for the procurement of certain critical items.

31. Broadly, spares may be divided into those of normal wear and tear; those of extra wear and tear; those which have no or little wear but should be kept on stock because of their vital function; those which are critical and subject to wear and tear.

32. Special provision is made in UNIDO-TKL and UNIDO-CRC for the purchase of spare parts which are "critical items" (UNIDO-TKL, annexures VIII and X; UNIDO-CRC annexures VIII and X). "Critical items" are defined in article 1 of UNIDO-TKL to mean all the equipment specifically designated as such in annexure VIII, which include synthesis reactor, boilers and turbo-generators (see UNIDO-CRC, article 1 and annexure VIII). These items are so classified because they tend to change technologically due to process and market developments.

33. Special provision is made in UNIDO-TKL and UNIDO-CRC for procuring these critical items. These items are to be purchased only from a list of prequalified vendors (UNIDO-TKL, annexures VIII and XII; UNIDO-CRC, annexures VIII and XII). Pre-qualified vendors are intended to be those manufacturers of equipment who are dependable and have sufficient experience of those items (see paragraphs 47 and 49, below).

34. The supply of spares may constitute one of the important sources of income for the contractor who may be the manufacturer himself. The contractor may phase the technology transfer in such a way as to ensure a purchaser's dependence on him for spares for as long as possible.

35. It is not uncommon for a contractor to insist on a tie-in clause providing that the purchaser shall obtain some or all spares from the contractor. To avoid allowing the contractor to enjoy a monopolistic position in the supply of spares, it is desirable for the purchaser to ensure that provision is made for obtaining some spares from a third source. Where spares are to be obtained from a third source, the contractor could obtain them as agent for the purchaser, i.e. on behalf and on the account of the purchaser.

3. Other aspects of spares provisions

36. Brief mention may be made of some of the more common types of spares provisions found in works contracts.

37. The contractor is generally required to supply a list of spare parts for the purchaser within a certain period after the effective date of the contract together with an estimate of cost. The details to be included depend on the availability of information and the types of spare parts. The purpose of obtaining early information regarding spares is to ensure delivery before, say, the start of commissioning of the plant.

38. A contractor may be required under a works contract to supply spare parts for a certain period. The cost of spare parts may be borne by the contractor. This is usually the case where spare parts are needed until completion of the guarantee tests. The cost is then included in the contract price. Annexure X, section 6 of UNIDO-TKL provides such an example:

"The CONTRACTOR is required to ensure that the quantity of spare parts used by him until he completes his guarantee tests are replaced by him at his own cost . . ."

39. Sometimes a works contract may contain a provision requiring the contractor to guarantee the supply of spare parts to the purchaser for a certain period.

4. Procurement procedures

40. Both UNIDO-TKL and UNIDO-CRC contain substantially similar procedures for the procurement of certain types of spare parts by the contractor on behalf of the purchaser. These procedures are designed to enable the purchaser to obtain from reliable vendors competitive offers of spare parts in an expeditious manner.

41. In both the UNIDO model contracts the services of the contractor are required for the procurement of spare parts. Depending on the types of spare parts, certain procedures have to be followed by the contractor.

42. Article 10.1.2 of UNIDO-TKL provides that in the case of spare parts of a proprietary nature, the contractor is to obtain from the suppliers directly in the name of, and for, the purchaser a list of two-years supply of spare parts as recommended by the supplier, for approval of the purchaser. Annexure XXVI, section 11 provides:

"Purchase of spare parts for proprietary items of equipment for which quotations shall be obtained by the CONTRACTOR at the time of purchase by him of the equipment shall be in accordance with a separate protocol between the PURCHASER and the CONTRACTOR, (but in all cases where procedures of the financing agency are required these shall be followed)."

43. In respect of spare parts which are not of a proprietary nature the contractor is to prepare bid documents on the basis of the technical specifications prepared by him and submit the same to the purchaser for approval. On approval the list is sent by the contractor on behalf of the purchaser to the respective vendors which have been previously agreed to by both the contractor and the purchaser (UNIDO-TKL, article 10.1.3, 10.1.4 and 10.1.5).

44. The contractor is to obtain from the vendors a minimum of three competitive offers (UNIDO-TKL, article 10.1.5). This will assist in obtaining lower cost supplies. The offers received from the vendors are to be evaluated by the contractor who is to submit the bid evaluation with appropriate recommendations to the purchaser for the relevant

final selection. The purchaser's final selection of the vendor will be communicated to the contractor within twenty days from the date of the contractor's submission of the bid tabulation (UNIDO-TKL, article 10.1.6). The contractor is to purchase the spare parts or other equipment, after the selection of the vendors by the purchaser (UNIDO-TKL, article 10.1.7).

45. Further details regarding the mode of procurement relating to bidding are set out in an annexure of UNIDO-TKL. These include the issue of tender specifications and bid tabulations.

46. Some purchasers¹¹ may require a list of "pre-qualified" vendors. Special procedure is made in an annexure of UNIDO-TKL for the purchase of spare parts from vendors who are to be "pre-qualified". The contractor is to issue pre-qualifying notices for all groups of spare parts (other than proprietary equipment spare parts) inviting potential vendors for pre-qualification. The contractor is responsible for submitting to the purchaser a list of companies pre-qualified by him for the purchase of different types of spare parts, indicating reasons for rejection of any vendor. The purchaser has the right to add to or subtract from such list of pre-qualified vendors. The contractor has to bear the cost of satisfying himself on the competence of any bidders (UNIDO-TKL, annexure XXVI).

47. Spare parts of critical items are to be procured only from a list of pre-qualified vendors for critical items to be listed in an annexure of UNIDO-TKL.

48. In UNIDO-CRC, spare parts are to be procured in accordance with the procedures for the procurement of equipment and materials generally as set out in article 10 and annexures.¹²

49. As in UNIDO-TKL, the purchase of spares which are critical items are to be purchased from a list of pre-qualified vendors for critical equipment to be listed in an annexure. In addition, annexure XXVI, section 11 of UNIDO-CRC provides:

"For purchase of critical items of equipment quotations shall be obtained promptly after the effective date by the CONTRACTOR and purchase shall be in accordance with a separate protocol between the PURCHASER and the CONTRACTOR. Separate protocols between the PURCHASER and the CONTRACTOR may also be made for specialised proprietary equipment, but in all cases where procedures of the financing agency are required these shall be followed."

XII. STORAGE ON SITE

A. General remarks

50. It is essential for the efficient implementation of

¹¹ See UNIDO-TKL, annexure XXVI, note 1 where it is stated that some governments and agencies require prequalification.

¹² See Part Two, VI, *Sub-contracting*, paras. 35-37.

an industrial works contract that the required materials and equipment be available at the site when the construction schedule calls for their incorporation in the works. They must therefore be procured and delivered to the site in advance of the time when they are due to be used. At the site, facilities are needed to store these items and to protect them against loss and damage.

51. Some of the issues which arise in connection with storage on site concern the provision of storage facilities, the security and safety of the facilities, the obligations to arrange for storage of materials and equipment as they are delivered to the site and responsibility for the stored items. These issues are dealt with in many works contracts.

B. Responsibility for storage

52. The UNIDO model contracts contain clauses assigning general responsibility for the storage of equipment and materials to one of the parties. Under UNIDO-TKL, the contractor is "responsible for storage at Site" (article 4.2.1). UNIDO-CRC on the other hand, states that it is the purchaser who must "arrange for storage of Equipment and Materials" (article 5.8).

53. Both UNIDO model contracts obligate the contractor to investigate and familiarize himself with circumstances bearing on the storage of equipment and/or materials. UNIDO-TKL contains two alternative texts of article 4.4. Under Text A the contractor acknowledges that he has fully satisfied himself as to the general and local conditions applicable to the contractor's work, particularly those bearing upon the handling and storage of materials.

54. Text B of UNIDO-TKL, article 4.4, requires the contractor to obtain such information as he may consider necessary to carry out his work under the contract, particularly that bearing on the handling and storage of materials.

55. Article 4.4 of UNIDO-CRC contains language similar to that in Text B of UNIDO-TKL, article 4.4, but refers to the handling and storage of both equipment and materials.

56. Under both UNIDO model contracts, the overall responsibilities of the respective parties for storage include the obligation to provide suitable storage facilities. Article 12.4.1 of UNIDO-TKL states:

"The CONTRACTOR shall be obliged to arrange for and have ready adequate warehouse facilities at the Site to receive packages. In the event that permanent facilities are not ready or available, the CONTRACTOR shall provide adequate temporary facilities at his cost in good time at the Site."

57. However, the purchaser must provide the land on which these facilities are to be located. Article 5.3 provides:

"The PURCHASER shall secure and make available to the CONTRACTOR not later than the Effective Date of

the Contract: the land indicated on the lay-out and plot plan for construction of the Works, free of all encumbrances, including the necessary right of way. The PURCHASER shall also make available adequate space for storage depots at or near the Site."

58. On the other hand, according to the provisions of UNIDO-CRC, under which the purchaser is responsible for storage (see paragraph 52, above) the obligations of the contractor for the provision of land and storage facilities are limited. He must merely (through his appointed "site representative") "advise the PURCHASER on storage at Site" (article 4.15). The land and facilities for storage must, presumably, be provided by the purchaser.

59. Under ECE 188A/574A, although the contractor is apparently responsible for storing materials and equipment, the purchaser must provide the storage facilities. According to clause 6.1(d) the purchaser must provide the contractor (free of charge, unless otherwise agreed) with closed or guarded premises on or near the site as a protection against theft and deterioration of the plant to be erected, of the tools and equipment required therefor, and of the clothing of the contractor's employees.

60. With limited exceptions, FIDIC-EMW does not deal expressly with issues of storage on site. It does, however, impose general responsibilities upon the contractor with respect to fencing, lighting and guarding the works. Clause 14.2 states that:

"Unless otherwise agreed the Contractor shall be responsible for the proper fencing, lighting, guarding and watching of all the Works on the Site until taken over. . ."

Under this form, "Works" is defined to include "all Plant to be provided . . . by the Contractor under the Contract" (clause 1.1(f)); and "Plant" means "machinery, apparatus, materials, articles and things of all kinds to be provided under the Contract other than Contractor's Equipment" (clause 1.1(c)).¹³ Accordingly, the contractor's obligations with respect to fencing, lighting, guarding and watching the works extend to materials and equipment stored on site.

61. Some of the forms under study contain special provisions dealing with the storage of materials or equipment, the delivery, acceptance or use of which, in the works, is delayed. FIDIC-EMW applies these provisions to "delayed Plant", which is defined as follows:

"For the purposes of this Clause only: 'delayed Plant' means either (a) Plant which by delay or failure on the part of the Engineer to give such authorisation as is mentioned in Sub-Clause I of this Clause¹⁴ or from any cause for which the Employer or some other contractor

employed by him is responsible the Contractor is prevented from delivering to the Site at the time specified for the delivery thereof or, if no time is specified, at the time when it is reasonable for it to be delivered having regard to the date by which the Works ought to be completed; or (b) Plant which has been delivered to the Site but which by delay or failure on the part of the Engineer or from any cause for which the Contractor is not responsible the Contractor is for the time being prevented from erecting . . ." (Clause 26.2)

62. Under certain circumstances, the Contractor must store, protect and preserve the "delayed Plant", and provide insurance coverage for it. First, the contractor must under clause 26.3 notify the purchaser and the engineer of readiness for delivery. Thereafter, clause 26.4(a) provides as follows:

"There shall be included in the Contract Price a sum . . . for storing and taking reasonable measures to protect and preserve the delayed Plant from and insuring it (to the extent that it can be insured) against loss, deterioration and damage however caused from the date of the said notice or the normal delivery date if this shall be later until the Contractor shall no longer be prevented from delivering the delayed Plant or (as the case may be) erecting it . . ."

63. However, after receipt of the notice referred to in clause 26.3 (see paragraph 62, above) the purchaser may assume responsibility for storing, protecting and preserving the "delayed plant". And the purchaser must assume this responsibility after receiving further notices from the contractor:

"The Employer may at any time after receipt of the notice referred to in Sub-Clause 3 of this Clause assume responsibility for storing, protecting and preserving the delayed Plant. If at any time after the expiration of 12 months from the date of the said notice or at any time after the delayed Plant has been delivered to the Site the Employer shall not have assumed such responsibility the Contractor may by a further notice in writing expiring 30 days after receipt thereof by the Employer require the Employer to assume the responsibility aforesaid and upon the expiration of the last mentioned notice the Employer shall assume such responsibility provided always that, if notice to proceed¹⁵ shall be given within 30 days after receipt by the Employer of the last mentioned notice given by the Contractor, this paragraph of this Sub-Clause shall not operate." (Clause 26.5)

64. It is clear from further provisions in FIDIC-EMW that storage and protection of the "delayed Plant" by the contractor is obligatory, and not optional. After receiving notice to proceed, clause 26.6 requires the contractor to

¹³ For the definition of "works" and "plant" in the forms under study, see Part Two, IV, *Interpretation of Contracts*, paras. 84-94.

¹⁴ Sub-clause 1 provides, *inter alia*, that "Plant or Contractor's Equipment shall be delivered to the Site only upon an authorisation in writing applied for and obtained by the Contractor from the Engineer."

¹⁵ "Notice to proceed" means notice in writing from the engineer to the contractor that delayed plant may forthwith be delivered or erected (clause 26.2).

examine the "delayed Plant", and remedy any deterioration and defects:

"After receipt of notice to proceed the Contractor shall after due notice in writing to the Engineer and if required by the Engineer, in his presence, examine the delayed Plant, . . . and make good any deterioration or defect therein that may have developed or loss thereof that may have occurred after the normal delivery date or (if later) the date when the Contractor was by such delay, failure or other cause as before-mentioned first prevented from erecting the delayed Plant."

65. The next provision (clause 26.7) states that the costs of this examination and repair work is to be included in the contract price to be paid by the purchaser to the contractor, unless the loss was caused, *inter alia*, by a failure of the contractor to store and preserve the "delayed Plant":

"There shall be included in the Contract Price a reasonable sum for making the examination referred to in Sub-Clause 6 of this Clause and in making good any deterioration, defect or loss as therein mentioned except insofar as the same was caused by faulty workmanship or materials or by the Contractor's failure to take the measures referred to in paragraph (a) of Sub-Clause 4 of this Clause or in Clause 15.1(a) (Care of the Works) . . ."

66. Thus, if the contractor fails to take appropriate measures to store and protect the "delayed Plant", he must remedy at his own expense any deterioration or defects caused to the "delayed Plant" by such failure.

67. Under ECE 188A/574A the contractor must arrange for the storage of equipment of which the purchaser fails to accept delivery on the due date, "at the risk and cost of the Purchaser". Clause 10.1 provides:

"If the Purchaser fails to accept delivery of the Plant on due date, he shall nevertheless make any payment conditional on delivery as if the Plant had been delivered. The Contractor shall arrange for the storage of the Plant at the risk and cost of the Purchaser. If required by the Purchaser, the Contractor shall insure the Plant at the cost of the Purchaser. Provided that if the delay in accepting delivery is due to one of the circumstances mentioned in Clause 25 and the Contractor is in a position to store it in his premises without prejudice to his business, the cost of storing the Plant shall not be borne by the Purchaser."

C. Access to storage facilities

68. In the course of implementing the contract, the contractor will require access to the storage facilities. The UNIDO model contracts contain provisions specifically authorizing such access. Article 13.6 of UNIDO-CRC provides:

"The CONTRACTOR and his authorized personnel shall have free access to the Site, storage yards, fabrica-

tion shops, facilities for the supply of utilities and laboratories, which are set up or intended for use for establishing the Plant."

69. UNIDO-TKL contains a comparable provision (article 13.11)

[A/CN.9/WG.V/WP.7/Add.4*]

XIII. PRICE

A. General remarks

1. The determination of the price to be paid by the purchaser in a works contract is important for both parties. The purchaser must know at the conclusion of the contract how much the project will cost him, and the financial resources he must obtain. The contractor must be able to estimate his profits. Both parties are interested in minimizing the possibility of later disputes on this issue.

2. The price in a works contract covers not only the supply of plant and machinery, but also the provision of different services connected with the works and the transfer of technology. A considerable period of time may elapse between the drawing up of plans and specifications, and the supply and erection of the plant, and accordingly there is a risk of price increases of the materials and services to be supplied. The quantity of the work to be done and the quality of the material to be supplied cannot be exactly determined at the time of conclusion of the contract. Accordingly, determination of the price is more difficult than in simpler types of contracts.

3. In view of the fact that the price in a works contract will consist of a large sum of money, parties will normally agree on the price of most items at the conclusion of the contract. As regards the supply of services, if the price is not fixed at the time of concluding the contract, it may under most legal systems be determined later on the basis of trade usage or price lists approved by public authorities. Under some legal systems, however, it is essential that as regards goods to be supplied the price, or a method for determining it, is agreed at the time of concluding the contract. It may be noted, however, that article 55 of the Sales Convention provides:

"Where a contract has been validly concluded but does not expressly or implicitly fix or make provision for determining the price, the parties are considered, in the absence of any indication to the contrary, to have impliedly made reference to the price generally charged at the time of the conclusion of the contract for such goods sold under comparable circumstances in the trade concerned."

* 22 February 1982.

4. In international trade three methods of pricing a works contract have been developed:

(a) The price may be a lump-sum. The price thus stipulated is, in general, to remain constant even though the cost of performance by the contractor turns out to be higher than anticipated;

(b) The price may be determined on the basis of schedules or tariffs of cost for work or time units, taken together with an estimate made of the anticipated extent of work. The final price to be paid will be definitely known only at the conclusion of performance;

(c) Parties may agree on a cost reimbursable price. In this case the purchaser is to pay all costs incurred by the contractor in connection with the anticipated work, together with a fee for the procurement of supplies and services effected by third parties, and for co-ordination and inspection of the work.

5. While most contracts will reflect preponderantly one of the above-mentioned approaches to pricing, it is unlikely that one approach will be adopted for all items under the contract. For in every contract it will be more convenient to price a few items on other bases other than the main one that is adopted. Techniques may also be adopted to offset the disadvantages of each method of pricing, e.g. the uncertainty created by pricing on the basis of schedules and tariffs may be mitigated by fixing a ceiling price of the contract.

6. Under most legal systems the principle of "nominalism" is applied to currency questions, i.e. the price to be paid is not automatically increased or decreased in case the value of the money has changed between the time of the conclusion of the contract and the time of payment in terms of its exchange rate in relation to other currencies or in its purchasing power. In works contracts, there may, therefore, be clauses aimed at the protection of the parties against the effects of currency fluctuations, and dealing with the rate of exchange to be applied. In the forms under study only the FIDIC Conditions deal with these problems. Clause 72 of FIDIC-CEC provides in this respect as follows:

"(1) Where the Contract provides for payment in whole or in part to be made to the Contractor in foreign currency or currencies, such payment shall not be subject to variations in the rate or rates of exchange between such specified foreign currency or currencies and the currency of the country in which the Works are to be executed.

"(2) Where the Employer shall have required the Tender to be expressed in a single currency but with payment to be made in more than one currency and the Contractor has stated the proportions or amounts of other currency or currencies in which he requires payment to be made, the rate or rates of exchange applicable for calculating the payment of such proportions or

amounts shall be those prevailing, as determined by the Central Bank of the country in which the Works are to be executed, on the date thirty days prior to the latest date for the submission of tenders for the Works, as shall have been notified to the Contractor by the Employer prior to the submission of tenders or as provided for in the tender documents.

"(3) Where the Contract provides for payment in more than one currency, the proportions or amounts to be paid in foreign currencies in respect of Provisional Sums items shall be determined in accordance with the principles set forth in sub-clause (1) and (2) of this Clause as and when these sums are utilised in whole or in part in accordance with the provisions of Clause 58 and 59¹ hereof."

A similar provision is contained in clause 43 of FIDIC-EMW.

B. Methods of pricing work

1. Lump-sum price

7. A significant factor in determining the most appropriate method of fixing the price is the nature of the contract. A lump-sum price is usually provided in projects where significant changes in the extent and design of the work are not envisaged. Thus a lump-sum price is likely to be stipulated in a turnkey contract, where the contractor bears the total responsibility for carrying out and completing a clearly identified project. However, a lump-sum price may be used in other types of works contracts as well, in particular in fixing the price of plant and machinery to be supplied.

8. UNIDO-TKL provides for a fixed price for the plant and machinery and for most of the services connected with the execution of a works contract. Under article 20.1² of UNIDO-TKL a fixed price is stipulated for the following items:

(a) The supply of plant, equipment, and materials ex-site (inclusive of the complete engineering and related services);

(b) The granting of the licences and know-how for the plant;

(c) The detailed civil engineering design work, and completion of all civil works, including road, (rail) and telephone connections and related services;

(d) The complete erection of plant and equipment including the supply of erection materials and hire of erection equipment and related services;

(e) Services related to management, operation and supervision, and

¹ See Part Two, VI, *Sub-contracting*, paras. 18-19.

² For the reimbursable price element in this model contract, see para. 21 below.

(f) The provision of training facilities for the purchaser's personnel.

9. UNIDO-CRC provides for a combination of a fixed and reimbursable price, but the categorization of the items of the contract are different from that under UNIDO-TKL. Under article 20.1³ of UNIDO-CRC a fixed lump-sum price is stipulated for the following items:

- (a) The granting of the licences and know-how for the plant;
- (b) The supply of basic and detailed engineering;
- (c) The supply of procurement, inspection and expediting services; and
- (d) The provision of training and training facilities.

10. Under article 20.1 of UNIDO-STC a fixed lump-sum price is stipulated for the following items:

- (a) The supply of the equipment (FOB or FOR);
- (b) The transport of the equipment (optional only);
- (c) The procurement of spare parts and the purchase of specialized equipment, such as erection equipment, or other materials;
- (d) The granting of the licences, know-how and the supply of basic and detailed engineering for the plant; and
- (e) The provision of training and training facilities.

11. A footnote to article 20.4 of UNIDO-CRC states that the price for the supply of the plant, equipment and materials could be partly in the form of a firm price and partly in the form of reimbursable price.

12. Clause 7.2 of ECE 188A/574A provides that the price for the erection may be partly in the form of a lump-sum and partly in the form of a reimbursable price.

2. Pricing on basis of time incurred and work done

13. If the extent of the work cannot be determined accurately in advance, a practicable method for pricing is to record the hours spent on work by the contractor and his personnel, the quantities of any materials supplied, and the extent of work done, and to pay the contractor in accordance with the record.

14. ECE 188A/574A makes provision for pricing on a daywork basis in respect of the erection of a plant. Clause 7.1 states that when erection is carried out on a time basis certain items shall be separately charged: the living expenses of the contractor's employees; the time worked, which is to be calculated by reference to the number of hours certified as worked in the time-sheets signed by the purchaser; and time necessarily spent on preparation for journeys; journeys themselves; daily travel between lodgings and site; and waiting when work is prevented by circumstances for which the contractor is not responsible.

³ *Ibid.*

15. Under FIDIC-CEC the engineer has the power to order additional or substituted work to be done. Such work is to be priced on a time basis. Clause 52.4 provides:

"The Engineer may, if, in his opinion it is necessary or desirable, order in writing that any additional or substituted work shall be executed on a daywork basis. The Contractor shall then be paid for such work under the conditions set out in the Daywork Schedule included in the Contract and at the rates and prices affixed thereto by him in his Tender."

16. Pricing on the basis of time spent on the work, and measurement of the work done, requires agreement on procedures for the computation of time and the measurement of work. Thus, clause 52.4 of FIDIC-CEC (see paragraph 15, above) provides that the contractor must deliver each day to the engineer's representative a statement of the names, occupation and time of all workmen employed, and of the description and quantity of all materials used, while clause 56 provides a procedure for the measurement of work.

17. It may not be possible to make an exact advance assessment of the duration of the work required of certain categories of personnel, and pricing their services on a time basis may be convenient. Thus, in regard to payment of expatriate personnel, article 20.7 of UNIDO-CRC provides:

"The PURCHASER will pay to the CONTRACTOR daily rates in accordance with the schedule of charges . . . for each Day of absence from the (respective) normal place of work in (country) of the specified expatriate personnel supplied by the CONTRACTOR."

18. Article 20.8 of UNIDO-CRC deals with overtime of expatriate personnel and states:

"The daily rates . . . shall be related to a normal working week of (48) hours, with, at least, one Day included as a holiday. In the event of any overtime for expatriate staff (excluding engineers, and any other staff who would not normally be paid overtime in their home country), or for work on weekly holidays or public holidays in (PURCHASER's country) the expatriate personnel shall be paid overtime charges at the rates contained in Annexure . . ."

3. Reimbursable price

19. Like pricing on the basis of time incurred and work done, pricing on a reimbursable basis will be convenient when the extent of the work cannot be accurately determined in advance. In addition, the fixing of schedules or tariffs of cost may be difficult e.g. where a major part of the work is to be done by sub-contractors, and the rates to be charged by them are unknown at the time of the conclusion of the contract. Again, the contractor may require the high degree of protection from loss which a reimbursable contract affords.

20. FIDIC-CEC provides that the contract price shall include the price paid by the contractor to nominated sub-contractors.⁴ Clause 59(4) provides:

"For all work executed or goods, materials, or services supplied by any nominated Sub-Contractor, there shall be included in the Contract Price:

"(a) the actual price paid or due to be paid by the Contractor, on the direction of the Engineer, and in accordance with the Sub-Contract;

"(b) the sum, if any, entered in the Bill of Quantities for labour supplied by the Contractor in connection therewith, or if ordered by the Engineer . . . ;

"(c) in respect of all other charges and profit, a sum being a percentage rate of the actual price paid or due to be paid calculated (at a specified rate) . . ."

FIDIC-EMW contains a comparable provision in clause 39.4.

21. In article 20.1, UNIDO-TKL expressly stipulates a reimbursable price for the supply of spare parts, and in article 10 provides a procedure for their purchase. Under article 20.6 of UNIDO-CRC, services related to management and supervision are priced on a reimbursable basis.

22. The uncertainty as to amount inherent in a reimbursable price may be mitigated by the parties agreeing on an estimate of cost without any undertaking by the contractor to guarantee the correctness of the estimate. Article 2.5 of UNIDO-CRC, for example, provides for estimated costs of supplies and services connected with the project, including know-how and basic engineering, procurement, inspection and expediting, training, site supervision, and materials and equipment, and provides that the parties acknowledge that the estimate shall not constitute a guarantee of project cost. Article 2.6 of UNIDO-CRC states:

"It is acknowledged that the estimate of the cost of all Equipment and Materials, FOB/FOR . . . is an estimated amount . . . The CONTRACTOR shall submit to the PURCHASER within four (4) months of the Effective Date of the Contract a revised estimate of the FOB/FOR cost of all Equipment and Materials to be procured under this Contract. The estimates shall be broken up by Plants and by sections thereof, to the extent practicable."

23. Like a contract priced on a time and measurement basis, a cost reimbursable contract necessitates an extensive record keeping which may place a special responsibility on the contractor. Article 23.1 of UNIDO-CRC provides:

"The CONTRACTOR shall keep adequate books of accounts and time-logs in accordance with the form and procedure required by the PURCHASER with regard to charges incurred and purchases made/payments effected

on behalf of the PURCHASER up to a period of two years following Final Acceptance of the Plant, if:

"23.1.1 any price or part of a price under provisions of Article 20 is based on time charges;

"23.1.2 provision has been made in the Contract for the CONTRACTOR to make purchases/effect payments up to a prescribed value on behalf of the PURCHASER."

4. Price currency

24. The contract price must be fixed in a currency. In principle it must be paid in that currency unless otherwise provided by the parties or the applicable law. The purchasers from a country which does not have a freely convertible currency, in particular, from developing countries or countries which have imposed currency restrictions, may have an interest in ensuring that a part of the price should be paid in the currency of their country. In practice such a contract provision may be stipulated for performance of work the cost of which the contractor must bear in local currency. Article 20.9 of UNIDO-TKL, for example, provides that payment for management and training, which is to be on site, shall be made partly in local currency.

XIV. REVISION OF PRICE

A. General remarks

25. Even if the price is fixed and firm, the parties may agree that it be revised in specific circumstances. Such a revision may increase or reduce the price.

26. Provisions on price revision are agreed upon by the parties because of the complex nature of a works contract and the long-term character of its execution. There are a number of such provisions in the forms under study. They provide for revision mainly in the following circumstances: changes in the extent and scope of the contract, furnishing of additional supplies and services, and incurring of additional costs in performance.

27. Under some provisions in the forms under study, the contractor is entitled in certain circumstances to claim payment of costs incurred by him. Such provisions of a cost reimbursable nature can be found even in contracts with a lump-sum price. In some cases where the purchaser is obliged to pay costs connected with his failure to perform an obligation, it may, however, not be quite clear whether such costs are to be considered as damages or an additional price. The provisions are regarded as relating to price revision, and are considered in this chapter, where it appears that the obligation to pay costs is not dependent on absence of exonerating circumstances or fault on the part of the purchaser.

⁴ As to the meaning of "nominated sub-contractor", see Part Two, VI, *Sub-contracting*, para. 18.

B. *Changes in extent and scope of work*

28. During performance, the contractor or the purchaser may find that due to certain factors it is impossible to carry out the work exactly as planned. In the forms under study, it is noted that the following factors may require a deviation from strict performance in accordance with the contract and thereby necessitate a proportionate adjustment of the price.

1. *Incorrect data supplied by engineer or by purchaser*

29. Clause 6.3 of FIDIC-EMW states that the purchaser has to pay the contractor for alterations of the work necessitated by reason of incorrect drawings or information in writing supplied by the purchaser or engineer.⁵

30. Under clause 17 of FIDIC-CEC incorrect data supplied in writing by the engineer or his representative can obligate the purchaser to pay costs connected with the rectification of errors based on such data.⁶

2. *Uncertainty in contract documents*

31. Where the documents forming the contract contain ambiguities or discrepancies which are resolved through instructions issued by the engineer, and compliance with such instructions involves costs for the contractor which he could not reasonably have foreseen, clause 5(2) of FIDIC-CEC requires the purchaser to pay the contractor additional sums.

3. *Change in physical conditions*

32. Clause 12 of FIDIC-CEC provides that additional costs are to be paid if the contractor encounters on the site physical conditions (other than climatic conditions) or artificial obstructions which an experienced contractor could not reasonably have foreseen. The engineer decides whether the physical conditions could not reasonably have been foreseen by an experienced contractor and certifies the additional cost to be paid by the purchaser. FIDIC-EMW contains a similar provision in clause 24.

4. *Changes in local laws*

33. Subsequent changes in administrative legislation of the country where the works are to be constructed can substantially affect the scope and cost of works contracts.⁷ Most of the forms under study contain provisions designed to safeguard the contractor, to a certain extent, against unforeseen contingencies of this kind.

34. Thus under clause 70(2) of FIDIC-CEC, if after the date thirty days prior to the latest date for submission

of the tenders there occur in the country where the works are to be executed changes in local laws which cause additional or reduced cost to the contractor, such cost is to be certified by the engineer and paid by or credited to the purchaser. FIDIC-EMW contains a similar provision in clause 52.2.⁸

35. UNIDO-TKL deals with the adverse impact on the parties' obligations due to changes in local laws in article 36.2, which provides:

"... In the event that any code, law or regulations are enacted after the Effective Date of the Contract (which are proven to the satisfaction of the PURCHASER), to have adverse effect on the CONTRACTOR's obligations, scope of work, prices and/or time schedule under this Contract, the PURCHASER shall either:

"36.2.1 obtain appropriate exemption(s) from the relevant authorities on the CONTRACTOR's behalf; or

"36.2.2 negotiate with the CONTRACTOR for commensurate change(s) in the scope of the work to be performed under the Contract, together with such changes in price as properly reflect the actual increased costs that are anticipated. The increased amount shall be subject to full audit by the PURCHASER..."

36. Article 15.3 of UNIDO-CRC specifies the circumstances in which the contractor is entitled to claim additional payment in the event that observance of local laws results in additional costs. This article provides:

"The CONTRACTOR shall be entitled to claim for additional costs... when a modification, change or variation occurs in the event of any one of the following:

"1. ...

"2. Any additional engineering/re-engineering required for compliance with applicable laws and in conformity with local statutes consequent on changes in such laws/statutes enacted after the signing of the Contract.

"3. Any additional engineering/re-engineering required for compliance with local statutes consequent on changes in environmental protection standards..."

5. *Variation of work*

37. Revision of the price required by variation of the work by the parties is dealt with in Part Two, III, *Variation*.

6. *Technological innovations*

38. A works contract may provide that the contractor is to carry out the mechanical work in accordance with additional superior standards which become known to him after the conclusion of the contract. In that event one of

⁵ See A/CN.9/WG.V/WP.4/Add.1, I, *Drawings and Descriptive Documents*, para. 23 (Yearbook... 1981, part two, IV, B, 1).

⁶ See A/CN.9/WG.V/WP.4/Add.2, VII, *Quality*, para. 55 (Yearbook... 1981, part two, IV, B, 1).

⁷ See A/CN.9/WG.V/WP.4/Add.7, XVIII, *Applicable Law*, paras. 95-100 (Yearbook... 1981, part two, IV, B, 1).

⁸ *Ibid.*, para. 107.

the questions that arises is which party will pay for the use of the new superior standards which become known to the contractor.

39. Under UNIDO-TKL and UNIDO-CRC the contractor is obliged to make available to the purchaser new improved standards that may become available. Article 7.3 provides:

"The CONTRACTOR shall ensure that the Process Licensors and the CONTRACTOR shall make available to the PURCHASER . . .

"7.3.1 . . .

"7.3.2 On payment, at a reasonable cost, and on agreed terms, including extension of secrecy agreements, rights to use proprietary processes developed or acquired by the CONTRACTOR including patented processes which could result in significant improvements in the capacity, reliability and efficiency of the Plant, and quality of the Products."

40. Under UNIDO-TKL and UNIDO-CRC the purchaser and the contractor are, however, obliged under certain conditions to exchange at no extra charge information on any new and improved operating techniques and preventive maintenance. Article 7.3.1 states:

"The CONTRACTOR shall ensure that the Process Licensors and the CONTRACTOR shall make available to the PURCHASER. . .

"7.3.1 Free of charge, developments and improvements in operating techniques, preventive maintenance and safety measures applicable to the Plant, and other relevant technical data and information which is made available free of cost by the Process Licensors to other licencees within the same period. The PURCHASER will also make available to the Process Licensor and CONTRACTOR, free of charge, any improvements in operating techniques which the PURCHASER shall have made in the same period."

C. *Furnishing of additional supplies and services*

41. In some cases although there may be no change in the extent and scope of the work itself, certain factors may necessitate the furnishing of additional supplies and services in connection with the work. Under certain conditions the contractor is entitled in such cases to claim payment of costs connected therewith. In the forms under study the following categories of cases are found in which the contractor is entitled to claim additional payment.

1. *Protection of highways and bridges*

42. Clause 30(2) of FIDIC-CEC states:

"Should it be found necessary for the Contractor to move one or more loads of Constructional Plant, machinery or pre-constructed units . . . over part of a

highway or bridge, the moving whereof is likely to damage any highway or bridge unless special protection or strengthening is carried out, then the Contractor shall before moving the load on to such highway or bridge give notice to the Engineer . . . of . . . his proposals for protection or strengthening the said highway or bridge. Unless within fourteen days of the receipt of such notice the Engineer shall by counter-notice direct that such protection or strengthening is unnecessary, then the Contractor will carry out such proposals . . . and, unless there is an item . . . in the Bill of Quantities for pricing by the Contractor of the necessary works for the protection or strengthening aforesaid, the costs thereof shall be paid by the Employer to the Contractor."

2. *Additional tests*

43. Under some works contracts the purchaser or a person authorized by him may check the quality of the equipment or the plant even during its production and erection. In such cases clause 36(4) of FIDIC-CEC provides that the costs connected with quality tests that are not provided for by the contract are to be paid by the purchaser unless the tests show lack of conformity with the contract:

"If any test is ordered by the Engineer which is either

"(a) not so intended⁹ by or provided for, or

"(b) (in the cases above mentioned) is not so particularised, or

"(c) though so intended or provided for is ordered by the Engineer to be carried out by an independent person at any place other than the Site or the place of manufacture or fabrication of the materials tested,

"then the cost of such test shall be borne by the Contractor, if the test shows the workmanship or materials not to be in accordance with the provisions of the Contract or the Engineer's instructions, but otherwise by the Employer."

3. *Inspection during erection*

44. The engineer or purchaser may find it advisable to send a representative or technical consultant during the erection to enter the site to check the contractor's compliance with his obligations. Such inspection may, however, entail the provision of additional services by the contractor. Under UNIDO-TKL the contractor shall be entitled to additional payment for such services unless the inspection arose from a non-fulfilment of the contractor's obligations. Article 13.15 states:

"If the sending on the Work and/or the Site of a third party under article 13.14 does not arise from any

⁹ Under the contract.

non-fulfilment of the CONTRACTOR's obligations and, in addition, could not have been reasonably foreseen or anticipated by the CONTRACTOR when entering into this CONTRACT, and, if proven to the reasonable satisfaction of the PURCHASER, the CONTRACTOR has incurred expense in complying with article 13.14 in respect of such third party, the PURCHASER . . . shall pay to the CONTRACTOR the necessary cost of any services provided by the CONTRACTOR."

45. Article 13.8.1 of UNIDO-CRC provides:

"If the sending of such a technical consultant under Article 13.8 above involves delays and/or entails expenses incurred by the CONTRACTOR, the PURCHASER shall pay to the CONTRACTOR these expenses and the contractual time schedule shall be adjusted accordingly."

4. *Samples*

46. Clause 36(2) of FIDIC-CEC states that all samples shall be supplied by the contractor at his own cost if the supply thereof is clearly intended by or provided for in the contract, but if not, then at the cost of the purchaser.

5. *Uncovering works and making openings*

47. Clause 38(2) of FIDIC-CEC deals with the uncovering of the civil engineering work. If this work is uncovered at the request of the engineer, costs connected therewith must be borne by the purchaser provided that the covering up was done with the approval of the engineer and the parts covered up are found to be properly executed.¹⁰

6. *Repairs during maintenance period*

48. With regard to the execution of repairs to the work during the maintenance period, clause 49(3) of FIDIC-CEC stipulates that the purchaser is obliged to pay for repairs which do not result from a breach of obligation by the contractor.¹¹

7. *Detection of defects*

49. Clause 50 of FIDIC-CEC states:

"The Contractor shall, if required by the Engineer . . . search . . . for the cause of any defect . . . appearing during the progress of the Works or in the Period of Maintenance. Unless such defect . . . shall be one for which the Contractor is liable under the Contract, the cost of the work carried out by the Contractor in searching . . . shall be borne by the Employer."

8. *Services or facilities to other contractors employed by purchaser, or to workmen of purchaser*

50. Where the contractor, on the request of the engineer, provides any facilities, services or plant to other contractors employed by the purchaser or to workmen employed by the purchaser, under clause 31 of FIDIC-CEC the purchaser must pay the contractor a reasonable sum for the provision of such facilities, services or plant.

9. *Exploratory excavations*

51. Clause 18 of FIDIC-CEC provides:

"If, at any time during the execution of the Works, the Engineer shall require the Contractor . . . to carry out exploratory excavations, such requirement . . . shall be deemed to be an addition . . . unless a provisional sum in respect of such anticipated work shall have been included in the Bill of Quantities."

D. *Additional costs*

52. Even if the contractor is not called upon to provide additional supplies and services there are certain factors such as delay or disruption of the contractor's arrangements or methods of work which may cause additional expenses to him in performing the contract. Some provisions of the forms analysed deal with the increase of price in such cases.

1. *Prolongation or suspension of work*

53. The ECE General Conditions contain express provision for revising the contract price in cases where the erection is delayed for a cause for which the purchaser or engineer is responsible. Clause 7.2 of ECE 188A/574A provides:

"When erection is carried out for a lump sum, the quoted price includes all the items above mentioned. Provided that if the erection is prolonged for any cause for which the Purchaser or any of his contractors other than the Contractor is responsible and if as a result the work of the Contractor's employees is suspended or added to, a charge will be made for any idle time, any extra work, any extra living expenses of the Contractor's employees and the cost of any extra journey."

54. The purchaser or engineer is sometimes entitled to suspend the performance of the work when, in his opinion, it is necessary to do so, even in the absence of breach of contract by the contractor. In such cases the contractor is entitled to payment of additional costs caused by the suspension. Article 32.4 of UNIDO-CRC provides that the contractor, upon the expiration of the period of suspension, shall be reimbursed for his reasonably justified additional costs evidenced by necessary documentation. Clause 40(1) of FIDIC-CEC stipulates that the contractor is entitled to payment of extra cost connected with the suspension of the

¹⁰ See A/CN.9/WG.V/WP.4/Add.3, VIII, *Inspection and Tests*, para. 47 (Yearbook . . . 1981, part two, IV, B, 1).

¹¹ See A/CN.9/WG.V/WP.4/Add.6, XVI, *Rectification of Defects*, para. 97 (Yearbook . . . 1981, part two, IV, B, 1).

work ordered by the engineer, unless the suspension is necessary by reason of some default on the part of the contractor, or due to climatic conditions on the site or necessary for the proper execution or the safety of the works insofar as such necessity does not arise from any act or default by the engineer or the purchaser or from any of the excepted risks.¹²

2. Circumstances beyond control

55. According to the UNIDO model contracts the contractor is entitled, *inter alia*, to compensation for additional costs arising out of specified occurrences (e.g. vandalism) beyond his control which damage or delay the work required to be undertaken under the contract. (UNIDO-TKL, article 19.1, Text B, and UNIDO-CRC, article 19.1, Text B.)

56. Under clause 65(4) of FIDIC-CEC, the contractor is entitled to any increased cost of execution of the work resulting from special risks. Special risks are defined in clause 65(5) to include rebellion, revolution, insurrection, civil war, and commotion or disorder not solely restricted to the employees of the contractor or sub-contractor.

3. Delay in giving possession of site

57. If the contractor incurs costs from failure on the part of the purchaser to give possession of the site in accordance with the contract, the engineer is, under clause 42(1) of FIDIC-CEC, to certify the sum to be paid by the purchaser to the contractor to cover the costs incurred.

4. Delay in issuing drawings or orders

58. Under clause 6(4) of FIDIC-CEC the contractor is entitled to be paid the reasonable amount of costs incurred due to any failure of the engineer to issue within a reasonable time any drawing or order requested by the contractor in accordance with the contract terms.

5. Failure to issue interim certificates or make payment

59. Clause 41.2 of FIDIC-EMW provides:

"If the Engineer fails to issue an interim certificate ... or if the Employer fails to make any payment ... the Contractor shall be entitled to stop the Works after giving 14 days' notice in writing to the Employer and the Engineer of his intention so to do, until the said certificate be issued or payment be made as the case may be, in which case the expenses of the Contractor occasioned by the stoppage and the subsequent resumption of work shall be included in the Contract Price."

6. Delayed delivery caused by engineer or purchaser

60. Under clause 26.1 of FIDIC-EMW a written authorization by the engineer is required before the plant or the

contractor's equipment can be delivered to the site. If the engineer fails to give such authorization in time for reasons for which he or some other contractor employed by him is responsible and the contractor is prevented from delivering in accordance with the contract terms, the contract price is to include certain resulting costs incurred by the contractor (clauses 26.2, 26.3 and 26.4).

7. Purchaser elects to use higher cost materials

61. In a works contract, the purchaser, particularly in a developing country, may have a right to decide that materials and equipment of a local origin shall be used when available. A problem can arise in the event of an increase in the cost of local materials subsequent to the conclusion of the contract. In a cost reimbursable contract the contractor would be reimbursed the cost of the higher priced local materials. In respect of a lump-sum contract, a question that arises is which party will bear the additional cost of local materials. Article 12.6.2 of UNIDO-TKL provides:

"... The PURCHASER shall have the right to decide whether materials of local (indigenous) origin shall be used when available provided that they are in conformity with the specification ... and in conformity with the time schedules. In the event that the use of local materials result in higher delivery costs at Site (even though imported materials are freely available), the CONTRACTOR shall so advise the PURCHASER together with an estimate of the increased costs. The PURCHASER at his discretion may decide to use the higher-cost local materials, in which event an adjustment of price shall be made as necessary."

E. Currency fluctuations

62. The parties may agree on a currency fluctuation clause (a monetary clause or a purchasing value maintenance clause) to be included in the contract.¹³ In the forms under study only the FIDIC Conditions deal with this problem. Clause 70(1) of FIDIC-CEC contains a provision which may be considered as an index clause. Under this provision adjustment of the price is to be made in respect of the rise or fall in some costs of the execution of the works. Clause 70 of Part II of FIDIC-CEC, to which clause 70(1) refers, provides:

"This clause should cover such matters as: Adjustment of Contract Price, in both local and foreign currency expenditure, by reason of alteration in rates of wages and allowances payable to labour and local staff, changes in cost of materials for permanent or temporary works, or in consumable stores, fuel and power, variation in freight and insurance-rates, Customs or other import duties, the operation of any law, statute, etc; price adjustment formula to be used, if any."

A similar provision is contained in clause 52.1 of FIDIC-EMW.

¹² See A/CN.9/WG.V/WP.4/Add.6, XVI, *Rectification of Defects*, para. 83 (Yearbook ... 1981, part two, IV, B, 1).

¹³ See Part Two, XIII, *Price*, para. 6.

XV. PAYMENT CONDITIONS

A. General remarks

63. Payment conditions express, in time sequence, the relationship of the obligations to be performed by the parties, i.e. the supply and construction of the works by the contractor and payment of the price by the purchaser. Thus payment of the price may precede performance by the contractor (advance payment) or may be made during performance, or may be made immediately after or within a certain period of time after the completion of the works or after the expiration of the guarantee period. Payment conditions will also usually stipulate the modalities of payment (e.g. the documents against which payment is to be effected). Each party understandably prefers payment conditions which require his performance after performance by the other party; in addition to financial advantages the risk connected with failure to perform the contract by the other party is reduced in such cases as the party required to perform subsequently may suspend his performance if the other party fails to perform. Some legal systems even permit a party to suspend performance or to avoid the contract in cases of anticipatory breach of contract. Article 71 of the Sales Convention* in this connection provides:

"(1) A party may suspend the performance of his obligations if, after the conclusion of the contract, it becomes apparent that the other party will not perform a substantial part of his obligations as a result of:

"(a) a serious deficiency in his ability to perform or in his creditworthiness; or

"(b) his conduct in preparing to perform or in performing the contract.

"(2) If the seller has already dispatched the goods before the grounds described in the preceding paragraph become evident, he may prevent the handing over of the goods to the buyer even though the buyer holds a document which entitles him to obtain them. The present paragraph relates only to the rights in the goods as between the buyer and the seller.

"(3) A party suspending performance, whether before or after dispatch of the goods, must immediately give notice of the suspension to the other party and must continue with performance if the other party provides adequate assurance of his performance."

64. If there are no payment conditions in a contract, the applicable law determines when the price is to be paid. Article 58 of the Sales Convention* in this connection provides:

"(1) If the buyer is not bound to pay the price at any other specific time, he must pay it when the seller places either the goods or documents controlling their

disposition at the buyer's disposal in accordance with the contract and this Convention. The seller may make such payment a condition for handing over the goods or documents.

"(2) If the contract involves carriage of the goods, the seller may dispatch the goods on terms whereby the goods, or documents controlling their disposition, will not be handed over to the buyer except against payment of the price.

"(3) The buyer is not bound to pay the price until he has had an opportunity to examine the goods, unless the procedures for delivery or payment agreed upon by the parties are inconsistent with his having such an opportunity."

65. Payment conditions in works contracts are usually drafted with great care, and in most cases the types of payment terms mentioned above are combined. Whether and to what extent advance and credit payment conditions are required will depend upon the kind of commercial operation, the nature of the work and the amount of the price.

66. As noted in Part Two, XIII, *Price*, a single price may not have been fixed for the total performance to be made under the contract; the price may be divided into several parts and each part allocated against a different item of performance (such as supply of equipment, granting of licence and know-how, erection of the equipment, training, management). The payment conditions may be different in respect of each of these items.

67. In some works contracts the price is not fixed as a lump-sum at the time of the conclusion of the contract but is determined at a later stage on the basis of the extent of the work executed and costs connected therewith.¹⁴ The payment conditions must be adapted to the method of pricing used in the contract.

68. The place of payment is another aspect of payment conditions which has important implications for the parties' legal positions and it may also be important in the event of currency restrictions. FIDIC-EMW deals with currency restrictions in clause 42 which provides:

"If, after the date thirty days prior to the latest date for submission of tenders for the Works, the Government or authorised agency of the Government of a country from which any payments under the Contract are to be made imposes currency restrictions and/or transfer of currency restrictions in relation to the currency or currencies in which the Contractor is to be paid, the Employer shall reimburse any loss or damage to the Contractor arising therefrom, without prejudice to the right of the Contractor to exercise any other rights or remedies to which he is entitled in such event."

* Yearbook . . . 1980, part three, I, B.

¹⁴ See Part Two, XIII, *Price*, para. 4.

A similar provision is contained in clause 71 of FIDIC-CEC.

B. Time of payment

1. Advance payment

69. Provisions for advance payment are usually inserted in a works contract to cover the contractor's working capital and other expenses in the initial stages of the project, and to provide some protection in the event of premature termination of the contract by the purchaser.

70. FIDIC-EMW contains a provision on advance payment before or during manufacture of the plant at the contractor's works. Clause 37.6 states:

"If the Contract provides for progress payments or other payments in advance, before or during manufacture . . . details shall be given in Part . . . and any amounts becoming due to the Contractor in respect thereof shall be included in interim certificates. The making of payments pursuant to this Sub-Clause shall be subject to the Contractor procuring financial assurance by means of the bond or guarantee of an insurance company or bank or other securities approved by the Employer, the details and terms of which shall be stated in Part . . ."

71. The UNIDO model contracts stipulate for advance payment in respect of various items of the work. Under UNIDO-TKL advance payment is stipulated in respect of the following items:

- (a) For the granting of licences and know-how, in the amount of 25% of the contract price¹⁵ (article 20.10);
- (b) For the supply of plant, equipment, materials ex-site (inclusive of the complete engineering and related services), in the amount of 10% (article 20.11). Another 10% is to be paid under certain conditions at the end of six months from the effective date of the contract;
- (c) For the detailed civil engineering design work, and completion of all civil works and other services connected therewith, in the amount of 10% (article 20.12); and
- (d) For complete erection of the plant and equipment including the supply of erection materials and hire of erection equipment and related services, in the amount of 10% (article 20.13).

72. UNIDO-CRC provides for the following amounts of advance payment in respect of various items of the work:

- (a) The granting of the licences and know-how for the plant, in the amount of 25% (article 20.10.1);
- (b) The supply of basic and detailed engineering and the supply of procurement, inspection and expediting services, in the amount of 15% (article 20.11.1); and

(c) The provision of training and training facilities, in the amount of 15%, upon agreement of the programme of training (article 20.13).

73. UNIDO-STC contains the following provisions for advance payment:

(a) The granting of licences, know-how and the supply of basic and detailed engineering for the plant, in the amount of 50% (article 20.13.1); and

(b) The supply of equipment, in the amount of 15% (article 20.14.1).

74. Article 20.17 of UNIDO-TKL provides that advance payment in respect of the items mentioned in paragraph 71 above, shall be made upon the provision of the performance bond or bank guarantee by the contractor as provided for in the contract. Article 20.14 of UNIDO-CRC contains an identical provision.

2. Payment during execution of work

75. Works contracts normally provide for payments to be made during the course of the work at specified stages of the work. Such payments may be based on the value of the work done and equipment supplied at the date of payment, or they may be fixed periodical payments representing a percentage of the price.

76. FIDIC-EMW provides for payment against certificates issued by the engineer. Clause 40 provides that the purchaser shall, during the progress of the work, pay to the contractor within one month from the issue of each interim certificate a sum equal to 50 per cent of the amount certified therein. Under clause 60(1) of FIDIC-CEC payments are to be made, unless otherwise provided, at monthly intervals.

77. The UNIDO model contracts contain detailed provisions setting forth the events in which payment is to be due and the amounts of such payments. UNIDO-TKL contains the following provisions for payments during the execution of the work:

(a) For the granting of licences and know-how, in the amount of 50% of the price on receipt by the purchaser of all the documents concerning know-how and basic engineering (article 20.10);

(b) For the supply of plant, equipment, materials ex-site (inclusive of the complete engineering and related services), 60% of the price to be paid *pro rata* on shipments of the equipment and materials (article 20.11);

(c) For the detailed civil engineering design work, and completion of all civil works and other services connected therewith, 10% of the price to be paid on completion of the design work for the main buildings and structures of the plant, and 65% of the price to be paid as progressive payments in monthly instalments against actual progress of work on site as reported and approved by the engineer (article 20.12);

¹⁵ The percentage is of the contract price for the items in question.

(d) For complete erection of the plant and equipment including the supply of erection materials and hire of erection equipment and related services, 15% of the price to be paid on the arrival of an agreed quantity of the contractor's erection equipment at the site. An additional 50% of the price is to be paid progressively in monthly instalments against actual progress of erection work on site as reported in the contractor's monthly progress report and certified by the engineer (article 20.13);

(e) For services related to management operations and supervision, 25% of the price to be paid on the mechanical completion of the plant, 25% on the first input of feedstock and 25% on commercial production of specification grade urea (article 20.14);

(f) For providing training and training facilities for the purchaser's personnel, 15% of the price to be paid upon agreement of the programme of training and 60% during the training stipulated in the contract. It is further provided that 25% is to be paid on completion of the overseas training of the purchaser's personnel as provided for in the contract (article 20.15); and

(g) For procurement and supply of spare parts, and services related thereto, 15% of the price to be paid on approval by the purchaser of the list of spare parts, and 75% *pro rata* on shipment of the spare parts (article 20.16).

78. UNIDO-CRC also specifies when payments are to be made during the execution of the work. UNIDO-CRC provides as follows:

(a) For the granting of the licences and know-how, in the amount of 50% of the price on receipt by the purchaser of all the documents concerning know-how and basic engineering (article 20.10);

(b) For the supply of basic and detailed engineering and the supply of procurement, inspection and expediting services, the payment is to be made as follows:

- (i) Upon the completion of the meetings stipulated in the contract and upon the issue of purchase orders for all critical items, 10% of the price;
- (ii) On the issue of bid specifications for all process equipment (excluding certain items), 15% of the price;
- (iii) On the issue of purchase orders for all process equipment, 10% of the price;
- (iv) On the issue of purchase orders for 95% (by value) of the equipment, 10% of the price;
- (v) On the issue of inspection certificates for 50% (by value) of the equipment, 5% of the price;
- (vi) On the shipment FOB of 50% (by value) of the equipment, 5% of the price;
- (vii) On the issue of inspection certificates for 95%

(by value) of the equipment, 5% of the price; and;

(viii) On the shipment FOB of 95% (by value) of the equipment, 5% of the price (article 20.11);

(c) For the provision of training and training facilities, 15% of the price to be paid upon agreement of the programme of training, 65% *pro rata* during the training as stipulated in the contract and 25% on completion of the overseas training of the purchaser's personnel (article 20.13).

79. UNIDO-STC contains the following provisions for payment during execution of the work:

(a) For granting of licences, know-how and the supply of basic and detailed engineering for the plant, 25% of the price to be paid on receipt of all the documents (article 20.13);

(b) For the supply of the equipment together with other goods, 75% of the price to be paid on *pro rata* shipment of goods FOB (port) or FOR (rail) as the case may be, subject to the deduction of liquidated damages for late deliveries (article 20.14);

(c) For the procurement of spare parts, 90% of the CIF price to be paid *pro rata* shipment to site (article 20.16); and

(d) For the provision of training and training facilities the price to be paid on completion of the overseas training of the purchaser's personnel (article 20.17).

3. Payment after completion of works

80. Payment after completion is usually dependent on the issue of a certificate of proper performance. Under UNIDO-TKL the following provisions are made for payment after completion of the work:

(a) For the granting of licences and know-how, 25% of the price is to be paid on completion of the performance guarantee tests of the plant and issuance of the provisional acceptance certificate by the purchaser (article 20.10.3);

(b) For the supply of plant, equipment, materials *ex-site* (inclusive of the complete engineering and related services), 10% of the price is to be paid on completion of the performance guarantee test of the plant and issuance of the provisional acceptance certificate by the purchaser, and 10% on the issuance of the final acceptance certificate by the purchaser (article 20.11);

(c) For the detailed civil engineering design work, and completion of all civil works and other services connected therewith, 15% of the price is to be paid on completion of the performance guarantee tests of the plant and issuance of the provisional acceptance certificate by the purchaser (article 20.11);

(d) For complete erection of the plant and equipment including the supply of erection materials and hire of

erection equipment and related services, 15% of the price is to be paid on mechanical completion of the plant and issuance of a mechanical completion certificate, and 10% of the price on completion of the performance guarantee tests of the plant and issuance of the provisional acceptance certificate by the purchaser;

(e) For services related to management operations and supervision, 25% of the price is to be paid on completion of the performance guarantee tests of the plant and issuance of the provisional acceptance certificate by the purchaser (article 20.14.14); and

(f) For procurement and supply of spare parts and services related thereto, 10% of the price is to be paid on the successful completion of the performance guarantee tests of the plant and issuance of a provisional acceptance certificate by the purchaser after deducting the value of the spare parts consumed by the plant before the guarantee tests have been completed, unless such spare parts have been fully replaced by the contractor (article 20.16.3).

81. UNIDO-CRC contains the following provisions for payment after completion of the work:

(a) For the granting of the licences and know-how, 25% of the price is to be paid on completion of the performance guarantee tests of the plant, and issuance of a provisional acceptance certificate by the purchaser (article 20.10.3); and

(b) For the supply of basic and detailed engineering and the supply of procurement, inspection and expediting services, 7% of the price is to be paid on the mechanical completion of the plant, 10% on the issue of the provisional acceptance certificate of the plant, and 3% on the final acceptance of the plant (article 20.11).

82. UNIDO-STC also contains similar provisions on payment after the completion of the work in article 20.13.3, 20.14.3 and 20.16.2.

83. FIDIC-EMW contains provisions for the payment of a large part of the contract price on the taking over of the work. Clause 40 states that unless otherwise agreed the purchaser shall pay to the contractor 95 per cent of the contract sum adjusted within one month from the date certified in the taking over certificate.

4. Bonus payment

84. Sometimes it is in the interest of both parties to advance the completion of the work. As an inducement to the contractor to speed up the work, a bonus payment may be made for saved time. Article 20.29 of UNIDO-TKL and article 20.26 of UNIDO-CRC provide for such bonus payments.

5. Payment after expiration of guarantee period

85. Works contracts usually provide for payment of a percentage of the price after the expiration of the guarantee

period. The purpose is to guarantee rectification of defects which may appear during the guarantee period.

86. Article 40 (c) of FIDIC-EMW provides for the payment of the balance of the price within one month after the issue of the final certificate.

87. Clause 60 of Part II of FIDIC-CEC provides as follows:

"Not later than . . . months after the issue of the Maintenance Certificate the Contractor shall submit to the Engineer a statement of final account . . . showing . . . the value of the work done in accordance with the contract together with all further sums which the Contractor considers to be due to him under the Contract. Within . . . months after receipt to this final account . . . the Engineer shall issue a final certificate stating

"(a) the amount which in his opinion is finally due under the Contract . . .

"(b) the balance, if any, due from the Employer to the Contractor or from the Contractor to the Employer as the case may be. Such balance shall . . . be paid to or by the Contractor as the case may require within twenty-eight days of the Certificate."

C. Payment documents

88. Payment conditions normally also stipulate what documents are required in connection with payments. Most payments are to be effected on the basis of an invoice, which is required usually by banks in connection with payment arrangements. There are often provisions in works contracts requiring approval or certification of the invoice by the purchaser's site representative or by the engineer as a precondition to payment. In addition to the invoice other documents may be required by works contracts in connection with payment procedure, such as certificates of performance, bills of lading, certificates of origin, inspection certificates, packing lists.

89. The UNIDO model contracts contain detailed provisions stating the documents that are required for payment. Article 20.26 of UNIDO-TKL provides that any payment due under the contract not being secured by a letter of credit shall be made to the contractor within 8 weeks of receipt by the purchaser of invoices duly certified by the purchaser's site representative. For instalment payments for the detailed civil engineering design work and other civil work, article 20.19.5 of UNIDO-TKL requires a monthly invoice from the contractor indicating the percentages of civil work completed. Article 20.20.2 of UNIDO-CRC provides that payments for daily rates and overtime of the contractor's expatriate personnel shall be effected upon presentation to the purchaser of monthly invoices supported by time-logs of each of the contractor's expatriate personnel, duly countersigned by the purchaser's representative at the site. Under 20.19.7 of UNIDO-TKL an invoice

for payment for the erection of plant and equipment must indicate that the percentage of progress in the erection of equipment as indicated in the monthly progress reports has not been previously compensated and the invoice must be duly certified by the purchaser or his representative.

90. Under FIDIC-EMW payments are effected after the issue of interim certificates by the engineer (clause 40). Applications for interim certificates may be made by the contractor in respect of each shipment of plant and from time to time as work on the site progresses. Each such application in respect of shipment shall identify the plant shipped, state the amount claimed and must be accompanied by such evidence of shipment and of payment of freight and insurance and such other documents as the engineer may reasonably require. Application for interim certificates other than in respect of shipment must set forth in detail particulars of the work executed on site and the plant delivered to the site (clause 37.2).

D. Letters of credit

91. Some payments are secured and payable on the basis of letters of credit. UNIDO-TKL required the purchaser to establish a letter of credit for the purpose of making all payments required during the execution of the work. Article 20.18 provides as follows:

"For the purpose of making payments . . . other than the advance payments . . . and final payments . . . the PURCHASER shall establish in favour of the contractor at a specified Bank in *(the CONTRACTOR's country or as agreed otherwise)* an irrevocable transferable and divisible Letter of Credit providing for payments, in accordance with the scope and schedule laid down . . . in conjunction with the documents-supply specified . . ."

Article 20.15 of UNIDO-CRC contains similar provisions with regard to the form of the letter of credit.

92. For payment of costs connected with the provision of expatriate personnel for management assistance and supervisory services, article 20.20.1 of UNIDO-CRC provides that the purchaser shall establish with a specified bank irrevocable letters of credit in favour of the contractor for an amount to be mutually negotiated between the parties. These letters of credit are to be established one month before the commencement of services by the contractor. UNIDO-STC contains a similar provision in article 20.26.

XVI. PERFORMANCE GUARANTEES

A. General remarks

93. A purchaser planning a large-scale industrial project will want to be assured that the project will be completed in accordance with the specifications and within the time period to be set forth in the contract. Accordingly,

the purchaser will seek a contractor who possesses the financial as well as the technical and operational resources needed to complete the work. Often, however, a purchaser will not have sufficiently thorough information concerning a prospective contractor's finances, the extent of his other work commitments (which could interfere with his performance or completion of the project), his prior performance record, or other factors bearing on the contractor's ability to see the project through to completion. Performance guarantees¹⁶ are therefore often required in works contracts as a means of ensuring that funds will be available to complete the work if the contractor fails to do so. In essence, a performance guarantee is an undertaking given to the purchaser, at the request of the contractor, by a third party — the guarantor — in which the guarantor undertakes to make payment to the purchaser, or arrange for performance of the contract.¹⁷

B. Necessity for performance guarantees

94. Not all works contracts require a performance guarantee. In some cases the purchaser may have full confidence in the contractor and the likelihood that he will complete the work in accordance with the terms of the contract. In addition, the purchaser may not expect the project to present difficult technical problems or other unusual factors, and he may be satisfied that any work left defective or unfinished by the contractor can be completed with a minimum of delay and expense. In such situation, the purchaser might conclude that the risks associated with the project do not justify the expense of requiring a performance guarantee. It should be noted that where a guarantee is required, even if the contractor initially pays the cost of the guarantee, he will in many cases pass this cost on to the purchaser by including it in his price.

95. UNIDO-TKL requires a performance bond in article 21.1 as follows:

"Upon the execution of the Contract, the CONTRACTOR shall provide to the PURCHASER a Performance Bond guaranteed by a First Class Bank in the form given in Annexure XXII A or approved Bonding Institution in the form given in Annexure XXII B for the amount of *(amount)* in favour of the PURCHASER. The PERFORMANCE Bond shall be valid for the period required under the Contract and such extensions thereof, and the CONTRACTOR shall take any and all actions including renewals at the appropriate time to keep the said Bond current and valid for the said period. Fifty per cent of the Performance Bond shall be released upon Mechanical Completion of the Plant, and the balance on Provisional Acceptance of the Plant."¹⁸

¹⁶ Performance guarantees are sometimes called performance bonds.

¹⁷ See para. 110 below.

¹⁸ Under the UNIDO form of bank guarantee, the obligation of the bank is to pay money up to a specified limit. Under the bond,

Article 21.1 of UNIDO-CRC contains a comparable provision, and the bank guarantee and bond required under that article and set forth in Annexures XXII A and XXII B to UNIDO-CRC are in identical terms to those required in UNIDO-TKL, article 21.1.

96. FIDIC-CEC deals with performance guarantees in clause 10 which states:

"If, for the due performance of the Contract, the Tender shall contain an undertaking by the Contractor to obtain, when required, a bond or guarantee of an insurance company or bank, or other approved sureties to be jointly and severally bound with the Contractor to the Employer, in a sum not exceeding that stated in the Letter of Acceptance for such bond or guarantee, the said insurance company or bank or sureties and the terms of the said bond or guarantee shall be such as shall be approved by the Employer. The obtaining of such bond or guarantee or the provision of such sureties and the cost of the bond or guarantee to be so entered into shall be at the expense in all respects of the Contractor, unless the Contract otherwise provides."

FIDIC-EMW contains substantially similar provisions (clause 9.1).

C. Time for submitting guarantee

97. Clause 21.1 of UNIDO-TKL and UNIDO-CRC specify that the contractor shall obtain the bond "[u]pon the execution of the Contract." This provision is to be interpreted in conjunction with article 8.1 of the UNIDO model contracts, according to which "the Contract shall become valid upon the formal execution (signing) by the duly authorized officer of the PURCHASER and CONTRACTOR in accordance with the applicable law."¹⁹ The FIDIC Conditions leave the time for submitting the performance guarantee to the agreement of the parties.

D. Relationship between performance guarantee and contract

1. Character of guarantor's obligation

98. The treatment of many issues which arise in connection with performance guarantees reflects differing approaches to the relationship between the guarantee and the contract in connection with which it is issued. While the contract between the contractor and the purchaser can prescribe the nature and terms of the guarantee which the contractor is obligated to provide, it is the guarantee itself which establishes the juridical link between the guarantor and the purchaser. Therefore, the rights and obligations of

the purchaser and guarantor *inter se* are governed in the first instance by the provisions of the guarantee and its applicable law, which may be different from the law applicable to the contract.

99. In form, a performance guarantee is closely connected with a works contract i.e. the guarantor has to pay upon failure of performance by the contractor under the works contract. The terms of the guarantee, however, may make the guarantee independent of the works contract, or accessory to it.

100. The guarantee would be independent when the obligation of the guarantor to pay, or arrange for performance, is independent of the liability of the contractor under the works contract for failure to perform. An example of an independent guarantee would be a so-called first demand guarantee, under which the guarantor has to make payment on demand by the purchaser. The contractor's failure to perform is proved by the bare assertion to that effect of the purchaser. Whether in fact there is a failure in terms of the works contract, or whether there is liability for such failure on the part of the contractor, is irrelevant to the guarantor's liability.

101. The guarantee would be accessory when the obligation of the guarantor is linked to liability under the works contract for failure of performance by the contractor. The nature of the link may vary under different guarantees e.g. the purchaser may have to establish the contractor's liability, or the guarantor may be entitled to establish the contractor's absence of liability, or entitled to rely on certain defences which the contractor may have in respect of his failure of performance.

102. Guarantees may be so drafted that their categorization into independent and accessory assumes lesser importance. Thus an accessory guarantee, under which the guarantor can only resist a claim to payment on the basis of one or two restricted defences to failure of performance available under the works contract to the contractor, may in practice operate as an independent guarantee.

103. Both independent and accessory guarantees may be either subsidiary or not subsidiary. Where a bond is subsidiary, the purchaser must notify the contractor and give him an opportunity to remedy his failure before claiming under the guarantee. The nature of the notification, and the extent of the opportunity given to remedy the failure may differ under various guarantees. An example is contained in clause 9.2 of FIDIC-EMW:

"If the Employer shall consider himself entitled to any claim under the bond or guarantee he shall forthwith so inform the Contractor specifying the default of the Contractor upon which he relies. Should the Contractor fail to remedy such default within 40 days after the receipt of such notice the Employer shall be entitled to require the bond or surety to be forfeit to the extent of the loss or damage incurred by reason of the default."

the obligation of the bonding institution is either to remedy the contractor's default, or to complete the contract, or to arrange for its completion.

¹⁹ See Part Two, II, *Formation*, para. 13.

104. The UNIDO form of performance bank guarantee has a non-subsidary character, as the bank must undertake to pay to the purchaser "on demand by the PURCHASER and without prior recourse to the CONTRACTOR" such sum, not exceeding a specified amount, "as may be demanded by the PURCHASER simply stating that the CONTRACTOR has failed to fulfil his obligations." (UNIDO model contracts, Annexure XXII A.)

105. Where an accessory guarantee requires the purchaser to establish the contractor's failure of performance, it will prescribe the method to be used. Some guarantees only require certification of failure by the engineer or a third party, while others require the purchaser to obtain a judicial decree or arbitral award establishing the contractor's failure to perform.

106. A contract between an international organization and a contractor from an industrialized country for the supply of iron plant in a developing country requires a guarantee which is conditioned on the contractor's non-performance of his obligations. Proof of the contractor's non-performance would be established either by

(a) A protocol signed by both the international organization and the purchaser stating the amount to be paid by the guarantor; or

(b) A copy of a judgment of an arbitral tribunal.

107. Article 9 of the ICC Rules for Contract Guarantees,²⁰ if incorporated in a guarantee, would require (unless the guarantee otherwise specified),

"... either a court decision or an arbitral award justifying the claim, or the approval of the [contractor] in writing to the claim and the amount to be paid."

2. Reduction in amount of guarantee

108. The liability of the guarantor under a performance guarantee is limited to an amount specified therein. Some contracts enable the contractor to perform the works by portions, or are otherwise divided into distinct stages of completion.²¹ The amount of the guarantee may be reduced as portions of the work are completed by the contractor and accepted or taken over by the purchaser. An example of a provision to that effect is provided by FIDIC-EMW, which under clause 32.2 enables the purchaser to take over the work in stages. This form requires that as each section of the works is taken over the guarantee shall be reduced proportionately (clause 9.3).

109. The guarantee required in a contract between an international organization and a contractor from an industrialized country for the supply of iron plant in a developing country provides that:

"... the amount of this guarantee shall decrease automatically according to the value of supplies provided and/or services performed by the contractor upon submission to the international organization by the contractor of sufficient documentary evidence, such as progress reports and invoices."

3. Nature of guarantor's obligations

110. In most cases, whether the guarantee or bond is accessory to or independent of the works contract, the obligation of the guarantor is simply to pay a sum of money to the purchaser under the circumstances provided in the guarantee. Some bonds, however, may impose additional obligations, including the obligation to take certain measures toward the completion or remedy of the contractor's failure to perform. The bond required by the UNIDO model contracts²² contains such obligations:

"Whenever Contractor shall be, and declared by Owner to be in default under the Contract, the Owner having performed Owner's obligations thereunder, the Surety may promptly remedy the default, or shall promptly

"1. Complete the Contract in accordance with its terms and conditions, or

"2. Obtain a bid or bids for completing the Contract in accordance with its terms and conditions, and upon determination by Surety of the lowest responsible bidder, or, if the Owner elects, upon determination by the Owner and the Surety jointly of the lowest responsible bidder, arrange for a contract between such bidder and Owner, and make available as work progresses (even though there should be default or a succession of defaults under the contract or contracts of completion arranged under this paragraph) sufficient funds to pay the cost of completion less the balance of the contract price; but not exceeding, including other costs and damages for which the Surety may be liable hereunder, the amount set forth in the first paragraph hereof. The term 'balance of the contract price', as used in this paragraph, shall mean the total amount payable by Owner to Contractor under the Contract and any amendments thereto, less amount properly paid by Owner to Contractor."

4. Period covered by guarantee

111. The period of validity of a guarantee is normally stipulated therein and in most cases is linked to the duration of the contractor's obligations. UNIDO-TKL and UNIDO-CRC in article 21.1 express this requirement in general terms:

"The Performance Bond shall be valid for the period required under the Contract and such extensions thereof..."

²⁰ See Uniform Rules for Contract Guarantees, ICC Publication No. 325.

²¹ See A/CN.9/WG.V/WP.4/Add.3, IX, Completion; X, Take-over and Acceptance (Yearbook... 1981, part two, IV, B, 1).

²² See para. 95, above.

Under the FIDIC Conditions this issue is a matter for agreement of the parties. (See paragraph 96 above; FIDIC-EMW, clause 9.1.)

112. A guarantee may specify a time limit for the submission of claims by the purchaser against the guarantor and this limit will often be related to the time of final completion of the contract. For example, in a guarantee incorporating the ICC Rules for Contract Guarantees, unless some other date is specified in the guarantee, a claim would have to be "received by the guarantor . . . six months from the date specified in the contract for delivery or completion or any extension thereof, or one month after expiry of any maintenance period (guarantee period) provided for in the contract if such maintenance period is expressly covered by the performance guarantee . . ." (Article 4(b)).

5. *Effect of variation of contract*

113. A significant issue in connection with guarantees is the effect of a variation or extension of the contract on the obligations of the guarantor under the guarantee. It is not uncommon in large scale industrial projects for the contract specifications or the completion date to be modified as the work progresses.²³ Since these variations will change the contractor's obligations under the contract, they will be of concern to the guarantor, particularly if the guarantor's obligations are linked to those of the contractor. A substantial extension or increase of the contractor's responsibilities will increase the risk to which the guarantor is exposed. In some legal systems, unless otherwise provided in the guarantee, an alteration of the underlying contract could operate to release the guarantor; or the guarantor may be obligated only to the extent of the contractor's obligations at the date of issuance of the guarantee.

114. For these reasons, guarantees frequently contain provisions stipulating that the guarantee will not cover variations increasing the contractor's responsibility, or that it will cover such variations only upon approval of the guarantor, or that the guarantor will automatically cover such variations. Guarantees may also deal with the issue of whether the amount of the guarantee is to be increased or the period covered by it extended as a result of variations in the contract.

115. An example of such provision is contained in article 7.2 of the ICC Rules on Contract Guarantees which would apply to a guarantee to which the Rules apply:

"A performance guarantee . . . may stipulate that it shall not be valid in respect of any amendment to the contract, or that the guarantor be notified of any such amendment for his approval. Failing such a stipulation, the guarantee is valid in respect of the obligations of

the principal as expressed in the contract and any amendment thereto. However the guarantee shall not be valid in excess of the amount or beyond the expiry date specified in the guarantee or provided for by these Rules, unless the guarantor has given notice in writing or by cable or telegram or telex to the beneficiary that the amount has been increased to a stated figure or that the expiry date has been extended . . ."

116. The performance guarantee required by the UNIDO model contracts states:

"The surety hereby waives notice of any alteration or extension of the time made by the Owner."

[A/CN.9/WG.V/WP.7/Add.5*]

XVII. INSURANCE

A. *General remarks*

1. A project as complex as the supply and construction of large industrial works has numerous risks associated with it. Due to the potential loss from these risks, it is common for the parties to the contract to require that many of them be covered by insurance.

2. Both parties to the contract have an interest in providing for protection against risks connected with the execution of the contract. Accordingly works contracts usually include provisions relating to

(a) *Property insurance* which insures the works and other types of property against loss or damage from specified events;

(b) *Liability insurance* which covers the liability of a party for a failure to perform his obligations under the contract and for injury or damage caused in connection with his execution of the contract.

3. It should be noted that the fact that a party has provided insurance covering certain risks – even if the contract requires him to insure those risks – will not normally constitute a limitation on obligations under that contract.

4. Indeed, most of the forms under study contain express provisions to this effect. FIDIC-CEC stipulates that fulfilment of the insurance requirement does not limit the contractor's obligations and responsibilities for the care of the works (clause 21). FIDIC-EMW provides that receipt by the purchaser of insurance proceeds "shall not affect the Contractor's liabilities under the Contract" (clause 17.1). The UNIDO model contracts contain the provision that the contractor's obligation to provide insurance shall not restrict "the generality of any other provision of the Contract, and in particular any such provision as pertaining to the liability or responsibility of the CONTRACTOR . . ." (article 24.1 of UNIDO-TKL and CRC).

²³ See Part Two, III, *Variation*.

* 19 April 1982.

B. General insurance clauses

5. In addition to special provisions dealing with particular risks, contracts typically contain general clauses covering both property and liability insurance. FIDIC-CEC provides in clause 21:

"Without limiting his obligations and responsibilities under Clause 20¹ hereof, the Contractor shall insure in the joint names of the Employer and the Contractor against all loss or damage from whatever cause arising, other than the excepted risks, for which he is responsible under the terms of the Contract and in such manner that the Employer and Contractor are covered for the period stipulated in Clause 20(1) hereof and are also covered during the Period of Maintenance for loss or damage arising from a cause, occurring prior to the commencement of the Period of Maintenance, and for any loss or damage occasioned by the Contractor in the course of any operations carried out by him for the purpose of complying with his obligations under Clauses 49² and 50³ hereof:

"(a) The Works for the time being executed to the estimated current contract value thereof, or such additional sum as may be specified . . . together with the materials for incorporation in the Works at their replacement value.

"(b) The Constructional Plant and other things brought on to the Site by the Contractor to the replacement value of such Constructional Plant and other things.

"Such insurance shall be effected with an insurer and in terms approved by the Employer, which approval shall not be unreasonably withheld, and the Contractor shall, whenever required, produce to the Engineer or the Engineer's Representative the policy or policies of insurance and the receipts for payment of the current premiums."

6. Clause 17.1 of FIDIC-EMW provides:

"Unless the Employer shall have approved in writing other arrangements the Contractor shall, in the joint names of the Contractor and the Employer, insure so far as reasonably practicable the Works and keep each part thereof insured for the Contract Sum or such other value as may be mutually agreed between the Employer and the Contractor against all loss or damage from whatever cause arising, other than the excepted risks, from the date of shipment or the date on which it becomes the property of the Employer, whichever is the earlier,

¹ I.e. the obligation to care for the works. See A/CN.9/WG.V/WP.4/Add.1, IV, *Passing of Risk*, paras. 121-122 and 127 (Yearbook . . . 1981, part two, IV, B. 1).

² I.e. the execution of repairs to the work during the maintenance period. See Part Two, XIV, *Revision of Price*, para. 48.

³ I.e. searching for the cause of any defect appearing during the progress of the works or in the maintenance period. See *ibid.*, para. 49.

until it is taken over by the Employer. The Contractor shall so far as reasonably practicable insure against the Contractor's liability in respect of any loss or damage occurring whilst the Contractor is on Site for the purpose of making good a defect or carrying out the Tests . . ."

7. Article 24.4 of UNIDO-TKL provides:

"The Insurance Policies . . . required to be taken out by the CONTRACTOR shall be as follows:

"24.4.1 'Construction All Risks' (C.A.R.) liability or 'Erection All Risks' (E.A.R.) policy (inclusive of third party cover) in the name of the PURCHASER and the CONTRACTOR to insure the Plant, while at the Site from the start of work until Provisional Acceptance of the Plant. Endorsements to the policy shall include coverage for E.A.R., 'faults in design', requiring the replacement and repair of damaged equipment due to faults in design, faulty workmanship and faulty material, up to the Performance Guarantee tests. Specific insurances for bodily injury and personal liability insurance, (excluding that to third parties) and endorsements for such items as elevator and hoist liability, shoring, blasting, excavating shall also be included.

"24.4.2 'Loss of Advanced Profits Insurance' (otherwise called 'Machinery Consequential Loss (Interruption) Insurance') to cover consequential loss amounting up to (amount) to the PURCHASER, which may arise following any damage to the Plant during testing and maintenance periods for a total period of (months) providing extended cover to that already provided by the C.A.R./E.A.R. policy.

"24.4.3 'Machinery Breakdown Policy' (if not included in 24.4.1) to cover the breakdown of machinery during testing, Initial Operation and operation of the Plant, including boilers, pressure vessels, turbines, etc., and explosion risks incidental thereto."

UNIDO-CRC (article 24.5) contains substantially similar provisions. One exception is that the limitation in article 24.4.1 of UNIDO-TKL, requiring coverage of the plant "while at the Site", does not appear in UNIDO-CRC.

C. Property insurance

8. Several types of property will be involved in a large works project, including the erected works themselves, equipment and materials to be incorporated in the works, and construction machinery and equipment. Most of the contracts considered for this study distinguish among various types of property in their treatment of issues dealt with by insurance clauses.

1. Insurance of materials and equipment to be incorporated in works

9. In a typical situation, materials and equipment which will become part of the works are shipped to the site

(often through different carriers and modes of transportation) and stored at the site until they are incorporated in the works. The materials and equipment are subject to risks of loss or damage throughout this period. If they do suffer loss or damage, it may be impossible to determine at which stage the loss or damage occurred. Because of this, some contracts require the contractor to provide insurance for materials and equipment covering the period as a whole, without distinguishing among the various stages. This approach is adopted by clause 17.1 of FIDIC-EMW (see paragraph 6, above) which requires the contractor to keep the machinery, apparatus and materials insured "from the date of shipment or the date on which it becomes the property of the Employer, whichever is the earlier, until it is taken over by the Employer." Providing insurance coverage for the period as a whole avoids the necessity of identifying the point at which the loss occurred.

10. Under article 24.1 of UNIDO-TKL the contractor is obligated to take out and keep in force, *inter alia*, transport insurance. This is required by article 24.4.4 to include "Marine Insurance" or "Cargo Insurance" to cover the transit of equipment and materials from the shops to the site. Under article 24.7 of UNIDO-CRC the purchaser is obliged to take out this insurance.

2. Insurance of works

(a) Works covered by insurance

11. Some forms specify that the works to be covered by the insurance include both permanent and temporary works (e.g. FIDIC-CEC, clause 1(1)(e)), and structures ancillary to the main works, such as off-sites and administrative, maintenance, laboratory and other facilities (e.g. UNIDO-TKL, article 1.29).

(b) Risks covered

12. According to FIDIC-EMW, the insurance for the project is to cover "all loss or damage from whatever cause arising, other than the excepted risks" (clause 17.1 (paragraph 6, above)). The excepted risks are defined in clause 15.1 (b) as follows:

"(i) (Insofar as they relate to the country where the Works are to be erected) war, hostilities (whether war be declared or not), invasions, act of foreign enemies, rebellion, revolution, insurrection or military or usurped power, civil war, or unless solely restricted to employees of the Contractor or of his Sub-Contractors and arising from the conduct of the Works, riot, commotion or disorder, or use or occupation by the Employer of any part of the Works; or

"(ii) A cause due to a design furnished or specified by the Employer or the Engineer for which the Contractor has disclaimed responsibility in writing within a

reasonable time after the receipt of the Employer's or Engineer's instructions; or

"(iii) Ionising radiations or contamination by radio-activity from any nuclear fuel or from any nuclear waste from the combustion of nuclear fuel, radio-active toxic explosive, or other hazardous properties of any explosive, nuclear assembly or nuclear component thereof; or

"(iv) Pressure waves caused by aircraft or other aerial devices travelling at sonic or supersonic speeds; or

"(v) Any occurrences that an experienced contractor could not foresee, or if foreseeable could not reasonably make provision for or insure against."

13. The UNIDO model contracts, as seen in paragraph 7 above are specific as to the types of insurance required. The precise scope of coverage provided by "construction all risks" and "erection all risks" policies may vary depending upon the particular insurer and policy. However, the fundamental purpose of such policies is to pay the cost of repairing or replacing any physical loss or damage to the works, including materials for incorporation in them.

14. According to the FIDIC Conditions, the contractor must provide insurance covering the works from the commencement of the works until the date(s) specified in the Certificate(s) of Completion in respect of work covered by the certificates. In addition, the FIDIC Conditions specify that the insurance must cover the post-completion maintenance period for loss or damage arising from a cause occurring prior to completion or take-over (FIDIC-CEC, clauses 20(1) and 21; FIDIC-EMW, clause 17.1).⁴

15. In the UNIDO model contracts, the basic "C.A.R./E.A.R." (see paragraph 7 above) insurance is to cover the period from the start of the work until provisional acceptance by the purchaser (UNIDO-TKL, article 24.4.1 and UNIDO-CRC article 24.5.1).

3. Insurance of contractor's equipment

16. FIDIC-CEC requires insurance coverage for "[t]he Constructional Plant and other things brought on to the Site by the Contractor to the replacement value of such Constructional Plant and other things" (clause 21). This insurance is to be provided by the contractor and is to insure the same risks and cover the same period as the insurance of the works themselves (see paragraph 5 above).

D. Liability insurance

1. General liability insurance

17. FIDIC-CEC contains a very broad clause requiring the contractor to insure against his liabilities toward the

⁴ See para. 6 above.

purchaser and toward third parties arising out of the execution of the works under the contract. Clause 23 provides as follows:

"(1) Before commencing the execution of the Works the Contractor, but without limiting his obligations and responsibilities under Clause 22 hereof, shall insure against his liability for any material or physical damage, loss or injury which may occur to any property, including that of the Employer, or to any person, including any employee of the Employer, by or arising out of the execution of the Works or in the carrying out of the Contract, otherwise than due to the matters referred to in the proviso to Clause 22 (1) hereof.⁵

"(2) Such insurance shall be effected with an insurer and in terms approved by the Employer, which approval shall not be unreasonably withheld, and for at least the amount stated in the Appendix in the Tender. The Contractor shall, whenever required, produce to the Engineer or the Engineer's Representative the policy or policies of insurance and the receipts for payment of the current premiums.

"(3) The terms shall include a provision whereby, in the event of any claim in respect of which the Contractor would be entitled to receive indemnity under the policy being brought or made against the Employer, the insurer will indemnify the Employer against such claims and any costs, charges and expenses in respect thereof."

18. The general liability insurance provision in FIDIC-EMW is somewhat more specific as far as the period of coverage is concerned. FIDIC-EMW requires the contractor to "insure against his liability for damage or injury occurring before all the Works have been taken over", and against his liability for any loss or damage while he is on the site after take-over to remedy a defect or carry out tests during the Defects Liability Period, or for the purpose of completing outstanding work (clause 17.2). FIDIC-EMW excludes from the liability insurance liability for damage to property forming part of the works (clause 17.2) as damage to the works is to be covered by the property insurance concerning the works (see paragraph 6 above).

19. Article 24.5.1 of UNIDO-CRC and article 24.4.1 of UNIDO-TKL provide that "endorsements to the policy shall include coverage for E.A.R., 'faults in design', requiring the replacement and repair of damaged equipment due to faults in design, faulty workmanship and faulty materials, up to the Performance Guarantee Tests. Specific insurances for bodily injury and personal liability insurance (excluding that to third parties) and endorsements for such items as elevator and hoist liability, shoring, blasting, excavating may

also be included": Article 24.5.3 of UNIDO-CRC and article 24.4.3 of UNIDO-TKL require "machinery breakdown policy" to cover the breakdown of machinery during testing, initial operation and operation of the plant, including boilers, pressure turbines etc. and explosion risks incidental thereto.

2. *Liability arising from use of transport vehicles*

20. The UNIDO model contracts require liability for the use of "automobiles, trucks, aircraft, launches, tugs, barges etc." (UNIDO-TKL, article 24.4.5 and UNIDO-CRC, article 24.5.5). Under article 24.6 of UNIDO-TKL the contractor is responsible for taking out this insurance except for vehicles of which the purchaser is owner. Under article 24.7 of UNIDO-CRC the purchaser is responsible for it except vehicles of which he is owner.

3. *Liability for injury to workmen*

21. Workmen on the site and other employees of the parties run the risk of injury in the course of employment. Many legal systems have statutory schemes to provide compensation for such injuries to workers, some requiring employers to compensate employees directly for work-related injuries and others requiring employers to provide and pay for insurance covering these risks. In other legal systems, workers may be left to their remedies under general legal principles governing injury and damages. Contracts for industrial projects frequently contain provisions requiring insurance to cover these risks.

22. UNIDO-TKL (article 24.4.6) requires the contractor to take out, in the joint names of the contractor and the purchaser (article 24.7), liability insurance for payments under workmen's compensation acts, as required under legislation in the purchaser's country. The purchaser is to be the beneficiary of this policy (article 24.7). The purchaser is also obligated to carry accident insurance for his own personnel at the site (article 24.6.1).

23. The situation is reversed in UNIDO-CRC. There, the workmen's compensation insurance is to be taken out by the purchaser (article 24.5.6), and the contractor must carry accident insurance for his personnel at the site unless otherwise agreed by the parties (article 24.7.2). This presumably reflects the fact that under UNIDO-CRC, the erection of the plant is to be done by the purchaser under the supervision of the contractor's personnel (article 5.13), while under UNIDO-TKL the contractor performs the construction and erection himself (article 4.9).

24. The subject of insurance for workers is treated somewhat differently in the FIDIC Conditions. In these forms, the contractor is obligated to indemnify the employer against claims and damages arising from injuries to employees of the contractor or any sub-contractor, other than injuries arising from an act or default of the employer, his agents or servants (clause 24.1 of FIDIC-CEC and clause 15.7 of FIDIC-EMW). The FIDIC Conditions require the contractor

⁵ See A/CN.9/WG.V/WP.4/Add.4, XII, *Damages and Limitation of Liability*, para. 52 (Yearbook . . . 1981, part two, IV, B, 1).

to provide insurance to cover this obligation of indemnity (clause 24.2 of FIDIC-EMW and clause 17.3 of FIDIC-EMW).

E. Proof of insurance

25. The FIDIC Conditions obligate the contractor to produce to the engineer, when required to do so, the insurance policies and the receipts for payment of the premiums (FIDIC-EMW adds the words "or satisfactory evidence of insurance cover") (clauses 21, 23(2), 24(2) of FIDIC-CEC and clauses 17.1, 17.2, 17.3 of FIDIC-EMW).

26. UNIDO-TKL requires that within thirty days after obtaining each policy, the contractor must deposit an authenticated copy of the policy with the purchaser (this requirement does not apply to the general corporate and professional indemnity insurance). The purchaser is entitled to ask for up-to-date proof that the policies are in force (article 24.2).

27. To avoid any unintended implication arising from the purchaser's receipt of the copies, article 24.2 further provides that "receipt by the PURCHASER of any such copy shall not be construed as an acknowledgement by the PURCHASER that the insurance is adequate in nature, amount and/or scope."

28. The requirements in UNIDO-CRC are more general than those of UNIDO-TKL. Furthermore, unlike UNIDO-TKL, UNIDO-CRC imposes obligations on both parties:

"Whenever required from time to time, the CONTRACTOR and the PURCHASER shall submit to the other party adequate proof that the insurance(s) . . . to be in his responsibility has been taken and remains in force. The parties hereto shall also provide each other with certified documentation with regard to the coverage and value of the policies." (article 24.2)

F. Consequences of failure to provide insurance

29. The FIDIC Conditions provide that if the contractor fails to provide and keep in force any required insurance, the purchaser may do so, and deduct the amounts paid from any sums due to the contractor. Alternatively, the purchaser may recover such amounts paid as a debt due to the contractor (clause 25 of FIDIC-CEC and clause 17.4 of FIDIC-EMW).

30. The UNIDO model contracts would permit the purchaser to "take out insurance(s) considered appropriate and necessary in the circumstances". The premiums paid by the purchaser would constitute a debt due from the contractor to the purchaser which the latter could deduct from sums due to the contractor (article 24.3 of UNIDO-TKL and UNIDO-CRC).

31. UNIDO-CRC contains an additional provision permitting the contractor to take out "appropriate and necessary" insurance if the purchaser fails to comply with his insurance obligation. The premium paid by the contractor

would constitute a debt due from the purchaser (article 24.4).

XVIII. CUSTOMS DUTIES AND TAXES

A. General remarks

32. The economic aspect of works contracts covers, *inter alia*, customs duties and taxes. Problems relating to customs duties are analogous to those in the context of sales of goods. However, questions relating to taxes on items such as erection of equipment or other services, and transfer of technology raise special problems. The question of double taxation and the resulting question of who should ultimately bear the financial burden of taxation may become acute, particularly when the amount involved is substantial.

B. Customs duties

33. Generally, customs duties are imposed on imported goods. However, in some countries, some goods exported are also subject to such duties. Moreover, in some countries even goods in transit may be liable to customs duties. The question then arises which party is to pay such customs duties. This question may be solved by special contract provisions or by applying international trade terms (e.g. INCOTERMS).

34. Clause 53.1 of FIDIC-EMW contemplates that the obligations of the contractor and the purchaser concerning customs and import duties are to be settled by the parties. Clause 53.2 of FIDIC-EMW only stipulates that the purchaser is to assist the contractor where required in obtaining clearance through the customs of all plant and contractor's equipment and in procuring any necessary Government consent to the re-export of contractor's equipment upon removal from the site.

35. UNIDO-TKL states in clause 4.13:

" . . . The CONTRACTOR shall be responsible for clearance of Equipment and Materials at the port of entry, but the PURCHASER will provide all necessary import permits and authorizations required for this purpose and shall be responsible for demurrage and charges arising out of his failure to provide such permits. The PURCHASER shall be responsible for the payment of customs duties at port of entry."

36. This provision takes into consideration the nature of the performance by the contractor under a turnkey contract and provides for the duty of the purchaser to pay customs duties at the port of entry.

37. Clause 5.6 of UNIDO-CRC provides for the duties of parties in a different way:

"The PURCHASER shall be responsible (unless otherwise agreed) for the transportation of Equipment and

Materials from the port of dispatch (FOB) to the entry port (CIF/FOR) in the PURCHASER's country, for clearance at the entry port and for transportation of the Equipment to the Site."

38. It follows from this provision that in case of doubt the purchaser is to arrange clearance of the equipment and materials at the entry port. Such clearance may include payment of import customs duties.

39. Export and transit customs are dealt with indirectly in clause 31.1 of UNIDO-TKL which provides that the price quoted or contemplated by the contract includes, *inter alia*, customs duties outside the purchaser's country.⁶ Clause 31.1 of UNIDO-CRC contains an identical provision.

C. Taxes and levies

40. Under the tax regulations of most countries, the economic activity connected with the execution of works contracts, in particular income arising from such activity, is liable to taxes or levies. Under some legislation the payer is obliged to reduce payment effected in this connection by the extent of taxes due and to pay such taxes on the account of the foreign tax-payer. Parties therefore would usually agree upon all questions concerning the taxes and levies to be paid in connection with the execution of the works.

41. Clause 26(1) of FIDIC-CEC provides that the contractor has to give all notices and to pay all fees "required to be given or paid by any National or State Statute, Ordinance, or other Law, or any regulation, or by-law of any local or other duly constituted authority in relation to the execution of the Works and by the rules and regulations of all public bodies and companies whose property or rights are affected or may be affected in any way by the Works."

42. Under clause 26(2) of FIDIC-CEC the contractor is obliged to conform in all respects with the provisions mentioned in clause 26(1) and to keep the purchaser indemnified against all penalties and liabilities for breach of such provision.

43. Article 31 of UNIDO-TKL provides:

"31.1 Except as otherwise specified in this Contract, each and every price cited in or contemplated by this Contract . . . includes and covers all patent royalties, and all taxes, rates, charges and assessments of any kind whatsoever (whether Federal, State or Municipal, and whether or not in the nature of excise taxes/duties, customs tariffs, sales taxes, land taxes, license fees or otherwise) outside the PURCHASER's country pertinent to the equipment and material and CONTRACTOR's services provided with respect to the Works pursuant to this Contract, and/or to the performance of the

work, and all other costs and charges whatsoever relevant to such equipment, material, services and/or to such performance of the work by the CONTRACTOR."

An identical provision is included in clause 31.1 of UNIDO-CRC.

44. This provision should not be interpreted as providing that all taxes and levies imposed on the contractor in the purchaser's country are to be paid by the purchaser in all cases. A footnote to clause 31.2, which is left blank, states that parties should agree, according to the circumstances of each case, on a clause as to the payment of income tax, other taxes, imports and levies imposed on the contractor, his sub-contractors or on their employees in the purchaser's country. In determining the payment of such taxes and levies the law of the purchaser's country, including any relevant agreements for the avoidance of double taxation, is to be taken into consideration. The agreed clause may enable the contractor to receive payments from the purchaser free of the above taxes and levies or to have them considered when fixing the amounts to be received by the contractor. Under the agreed clause the contractor may be obliged in case of any of his taxes having been assumed by the purchaser to co-operate with him to minimize the tax burden and to reimburse him with any tax savings which the contractor may have from tax payments effected by the purchaser.

XIX. BANKRUPTCY

A. General remarks

45. The bankruptcy of a party to a contract may affect contractual obligations. This issue is of particular importance with respect to works contracts, taking into consideration their long term character and the considerable amount of money to be paid during their execution.

46. Under most legal systems, the main effect of bankruptcy is to bring the property of the bankrupt, including both the rights and the obligations under the contracts to which he is a party (except some contracts of a personal character), into the custody and control of the trustee in bankruptcy.

47. The bankruptcy of one of the parties to a contract may not, in itself, have the effect of terminating the contract or constituting a breach of it, since the trustee may, to a certain extent, have the power to carry on the business of the debtor so far as it may be necessary for the purpose of the bankruptcy proceedings. Under some legal systems, bankruptcy may, however, constitute an anticipatory breach of the contract entitling the party who is not bankrupt to suspend the performance of his obligations or even to declare the contract avoided. Under article 71 of the Sales Convention, a party may be entitled to suspend the perform-

⁶ See paras. 43 and 44 below.

ance of his obligations in case of bankruptcy of the other party.⁷

48. In some cases a party may even be entitled to declare the contract avoided if the other party becomes bankrupt prior to the date for performance. This right may arise under article 72 of the Sales Convention* which states as follows:

"If prior to the date for performance of the contract it is clear that one of the parties will commit a fundamental breach of contract, the other party may declare the contract avoided."

49. Some of the complex issues arising from the bankruptcy of one of the parties are the validity of payments made by the bankrupt, the possibility of set-off by the party not in bankruptcy, the legal position of the bankrupt in respect of his obligations, the effects on contracts entered into prior and subsequent to the bankruptcy. Most of the questions related to bankruptcy are closely connected to bankruptcy proceedings which are outside the scope of this study.

B. Provisions on bankruptcy in forms under study

50. FIDIC-EMW deals with bankruptcy in clause 45 which reads as follows:

"45. If the Contractor shall become bankrupt or insolvent, or have a receiving order made against him, or compound with his creditors, or being a corporation commence to be wound up, not being a members' voluntary winding up for the purpose of amalgamation or reconstruction, or carry on its business under a receiver for the benefit of its creditors or any of them, the Employer shall be at liberty

(a) To terminate the Contract forthwith by notice in writing to the Contractor or to the receiver or liquidator or to any person in whom the Contract may become vested, and to act in the manner provided in Clause 44 (Contractor's Default) as though the last-mentioned notice had been the notice referred to in such Clause and the Works had been out of the Contractor's hands; or

(b) To give such receiver, liquidator or other person the option of carrying out the Contract subject to his providing a guarantee for the due and faithful performance of the Contract up to an amount to be agreed."

51. The recourses provided for in paragraph (a) and (b) of clause 45 are not exhaustive and they do not seem to affect the other remedies available to the purchaser under the applicable law.

52. FIDIC-CEC deals with bankruptcy in clause 63(1) which reads as follows:

"If the Contractor shall become bankrupt, or have a receiving order made against him, or shall present his petition in bankruptcy, or shall make an arrangement with or assignment in favour of his creditors, or shall agree to carry out the contract under a committee of inspection of his creditors or, being a corporation, shall go into liquidation (other than a voluntary liquidation for the purposes of amalgamation or reconstruction), . . . or shall have an execution levied on his goods . . . then the Employer may, after giving fourteen days' notice in writing to the Contractor, enter upon the Site and the Works and expel the Contractor therefrom without thereby voiding the Contract, or releasing the Contractor from any of his obligations or liabilities under the Contract, or affecting the rights and powers conferred on the Employer or the Engineer by the Contract, and may himself complete the Works or may employ any other contractor to complete the Works. The Employer or such other contractor may use for such completion so much of the Constructional Plant, Temporary Works and materials, which have been deemed to be reserved exclusively for the execution of the Works, under the provisions of the Contract, as he or they may think proper, and the Employer may, at any time, sell any of the said Constructional Plant, Temporary Works and unused materials and apply the proceeds of sale in or towards the satisfaction of any sums due or which may become due to him from the Contractor under the Contract."

53. The bankruptcy of the purchaser is dealt with in clause 69(1) of FIDIC-CEC. If the purchaser becomes bankrupt or, being a company, goes into liquidation other than for the purpose of a scheme of reconstruction and amalgamation, the contractor is entitled to terminate his employment under the contract after giving fourteen days' prior written notice to the purchaser with a copy to the engineer. FIDIC-EMW has a similar provision (clause 51.1).

54. Where the contractor has become insolvent or has "committed an Act of Bankruptcy" the purchaser is entitled under article 33.7 both of UNIDO-TKL and UNIDO-CRC to cancel the contract.

XX. NOTIFICATION

A. General remarks

55. This chapter considers the modes of notification, time when notice takes effect, functions and effects of notices in the various forms under study. It is not intended to deal exhaustively with these topics, but only to give some illustrative examples. When a "request" is made, or an "advice", an "approval" or a "consent" is sought, notification is required.

* Yearbook . . . 1980, part three, I, B.

⁷ See Part Two, XV, *Payment Conditions*, para. 63.

B. Modes of notification

56. There are two main modes of notification, i.e. oral and written. The latter is more commonly required in the forms under study. The means of communication regarding a notice to be given are specifically indicated in most of the forms under study. However, article 27 of the Sales Convention* speaks of "means appropriate in the circumstances."⁸

57. The UNIDO model contracts set out the means by which notices are to be served. Thus, article 39.1 of both UNIDO-CRC and UNIDO-TKL provides:

"Any notice to be given to or served upon either party under this Contract shall be deemed to have been properly served in the following circumstances:

39.1.1: Provided that:

"39.1.1.1: Any notice to be given to the CONTRACTOR is to be conveyed by registered airmail post, or left at the address stated below, followed thereafter by the transmission of the same notice by cable or telex with a copy to be delivered to the CONTRACTOR's office at (town). (CONTRACTOR's address, cable address and telex number) (marked for the attention of (designation)).

"39.1.1.2: In the case of a notice to be served on the PURCHASER it is to be sent by registered airmail post to or left at the address stated below, followed thereafter by the transmission of the same notice by cable or telex. (PURCHASER's address, cable address and telex number) (marked for the attention of (designation)).

"39.1.1.3: In the case of a notice of information to be sent to the Technical Advisor by the CONTRACTOR, or to be sent by the Technical Advisor to the CONTRACTOR, such notice shall be delivered to the respective Site offices at (town)"

58. Under article 39.1.1.1 and 39.1.1.2, unlike 39.1.1.3, two notices are required. The first is to be conveyed by registered airmail post or left at the address. The second is the transmission of the same notice by cable or telex. A notice conveyed by post would not be deemed to have been "properly served" if it is not followed by cable or telex.

59. Both FIDIC-CEC and FIDIC-EMW also lay down the means of communication to be used in all written notices. Clause 68 of FIDIC-CEC provides:

"68(1) All . . . , notices . . . to be given by the Employer or by the Engineer to the Contractor under the terms of the Contract shall be served by sending by post to or delivering the same to the Contractor's principal place of business, or such other address as the Contractor shall nominate for this purpose.

(2) All notices to be given to the Employer or to the Engineer under the terms of the Contract shall be served by sending by post or delivering the same to the respective addresses nominated for that purpose in Part II of these Conditions."

60. Unlike the UNIDO model contracts there is no general requirement that the notice be sent by registered airmail. A similar provision is contained in clause 50 of FIDIC-EMW. However, in addition to post as a means of communication, cable and telex are expressly provided. It may be noted that article 13 of the Sales Convention states that "writing" includes telegram and telex.

61. Most of the notices that are to be given in ECE 188A/574A are required to be in writing. However, the actual means of communication, for example, whether it is to be by registered post, cable or telex, are not expressly set out.

C. Time notice takes effect

62. Some forms under study expressly link the question as to when notice takes effect with the means of communication. In this connection it may be noted that article 27 of part III of the Sales Convention* reads:

"Unless otherwise expressly provided in this Part of the Convention, if any notice, request or other communication is given or made by a party in accordance with this Part and by means appropriate in the circumstances, a delay or error in the transmission of the communication or its failure to arrive does not deprive that party of the right to rely on the communication."

63. Under the approach in article 27, a notice is effective if it is despatched provided the means of communication is "appropriate in the circumstances"; a delay or error in the transmission of the communication or its failure to arrive would still entitle the addressor to rely on the communication.

64. Some exceptions to article 27, where the receipt rather than despatch approach is envisaged, are to be found in a number of provisions in the Sales Convention.

65. For example, article 48 of the Sales Convention* provides that a request or notice from the seller is not effective unless received by the buyer — where the seller requests the buyer to make known whether he will accept performance by the seller to remedy his failure to perform.

66. Similarly, article 79 (4), which requires notification to be given by a party who fails to perform on account of an impediment, envisages the receipt approach to the extent that he is liable for damages resulting from the non-receipt of such a notice.

* Yearbook . . . 1980, part three, I, B.

⁸ See para. 62 below.

* Yearbook . . . 1980, part three, I, B.

67. It may also be noted that a number of provisions in Part II (Formation of Contract) of the Sales Convention* adopt the receipt approach for notification of an intention, and article 24 provides:

"For the purposes of this Part of the Convention, an offer, declaration of acceptance or any other indication of intention 'reaches' the addressee when it is made orally to him or delivered by any other means to him personally, to his place of business or mailing address or, if he does not have a place of business or mailing address, to his habitual residence."

68. Article 39.1.2 of both UNIDO-CRC and UNIDO-TKL deals with the time when notice is deemed to take effect.

"When any such notice is sent by registered mail post it shall be deemed to have been duly served⁹ following the expiration of () days following the date of posting and in proving such services it shall be sufficient to show that the letter containing the notice was properly addressed and conveyed to the postal authorities for transmission by registered airmail."

69. ECE 188A/574A do not appear to provide expressly for the time when notice takes effect.

D. Functions of notification

70. The main purpose of notification is to communicate with the other party, often in order to provide him with information. An analysis of the various provisions on notices found in the forms under study shows that in many instances, apart from simply providing information, a notice may serve a particular function. The function of a notice is often dependent on the kind of situation in which the notice is required. An attempt is made to classify these functions. But the functions may overlap in some of the categories suggested.

1. Notification to enable co-operation and execution of contract.

71. The co-operation of the other party to a works contract may be required for its due execution. The party whose co-operation is sought must then be provided with the necessary information so that he can act upon it. There are many instances where a party's co-operation is required. Below are some examples.

(a) Approval of drawings, equipment specifications and other documents

72. Documents drawn up in a works contract such as drawings, equipment specifications and instructions are necessary for determining the scope of the work, its proper

and adequate execution and maintenance. Thus, approval of the purchaser to such documents is often required.¹⁰ Most of the forms under study require the contractor to submit such documents for approval by the purchaser requiring the latter to respond with such approval or disapproval.

(b) Inspection and tests

73. In all works contracts, there are to be found provisions that give the purchaser a right of participation in the inspection and tests of the plant.¹¹ The contractor is required to notify the purchaser or his agent as to when the inspection and tests are to take place. This is to enable the purchaser to make arrangements to participate in them.

74. In the forms under study, a notice informing the purchaser or the contractor of inspection and tests must be given in sufficient time. Some forms specify the minimum number of days' notice which the contractor must give to the purchaser. Other forms simply require that notice be given within a reasonable time.

(c) Laws and regulations

75. The contractor has to comply with the laws and regulations affecting the performance of his obligations under the contract, and is generally liable to indemnify the purchaser against all penalties and liability for all statutory breaches. Where the works contract is carried out in the country of the purchaser, it is reasonable to expect the purchaser to inform the contractor of the relevant laws or to assist him in ascertaining the nature and extent of the laws and regulations that govern the contract.

76. Some forms under study require the purchaser to inform the contractor of the provisions of local laws and regulations while others do not.¹² In addition, clause 15.1 of ECE 188A/574A requires the purchaser to notify the contractor in full of the safety regulations which the purchaser imposes on his own employees. Clause 15.2 provides that if breaches of these regulations come to the notice of the purchaser, he must inform the contractor in "writing forthwith".

2. Notification to enable a party to take action

77. In certain situations the other party to a contract, be he purchaser or contractor, has to be notified before a certain course of action can be taken. These are usually situations which affect the liabilities of the parties.

¹⁰ See A/CN.9/WG.V/WP.4/Add.1, I. *Drawings and Descriptive Documents*, para. 12 (Yearbook . . . 1981, part two, IV, B, 1).

¹¹ See A/CN.9/WG.V/WP.4/Add.3, VIII, *Inspection and Tests*, paras. 21-22, 27-28 and 63-65 (Yearbook . . . 1981, part two, IV, B, 1).

¹² See A/CN.9/WG.V/WP.4/Add.7, > XVIII, *Applicable Law*, paras. 101-104 (Yearbook . . . 1981, part two, IV, B, 1).

* Yearbook . . . 1980, part three, I, B.

⁹ This article speaks of a notice being "duly served" whereas article 39.1, "properly served" (see para. 57 above).

(a) *Assignment of contract*

78. In some forms under study, the written consent of the purchaser is required for an assignment by the contractor of the liabilities of a contract.¹³ It follows that the purchaser has to have prior notification of the intended assignment.

(b) *Defects*

79. The contractor is required to notify the purchaser of defects due to his fault requiring repair, rectification or modification, before taking over.¹⁴ Where the purchaser is in a position to know of the defects, then he must notify the contractor so that the defects can be remedied.¹⁵

80. The purpose of notification is to give the contractor an opportunity of remedying the defects. If the contractor fails to remedy the defects, the purchaser may do so himself and recover the expenses incurred, or terminate the contract.¹⁶

(c) *Claim based on industrial or other intellectual property*

81. Where a third party makes a claim against the purchaser based on infringement of industrial or other intellectual property rights, notice to the contractor of such claim may assist the contractor to conduct negotiations for the settlement of the claim and to act on behalf of the purchaser, or to the extent permitted by the applicable law, to join in such litigation.

3. *Notification as prerequisite to exercise of a right*

82. In some circumstances notification of certain events is considered of such importance that it is a prerequisite to the acquisition of a right. However, the approaches in the forms under study are not uniform.

(a) *Claim for personal injury and damage to property*

83. Where an injured person brings a claim in respect of personal injury against the purchaser or the contractor, or a third party brings an action in respect of damage to his property against either party, clause 24.1(c) and (d) of ECE 188A/574A, depending on the circumstances, gives one party a right to indemnity from the other party. However, clause 24.2 provides that:

"In order to avail himself of his rights under subparagraphs (c) and (d) of paragraph 24.1 the party against whom a claim is made must notify the other of such claim . . ."

¹³ Part Two, V, *Assignment or Transfer of Contract*, paras. 1-4.

¹⁴ See A/CN.9/WG.V/WP.4/Add.6, XVI, *Rectification of Defects*, paras. 78, 92 and 107 (Yearbook . . . 1981, part two, IV, B, 1).

¹⁵ *Ibid.*, paras. 75-77, 86, 95 and 103-106.

¹⁶ *Ibid.*, paras. 110-114.

(b) *Right to rely on exonerating event*

84. Not all provisions on exoneration in the forms under study require notifications as a prerequisite to reliance on it, although all require prompt notice to be given. However, the UNIDO model contracts make notification a prerequisite to exemption from liability as a result of *force majeure*.¹⁷ Article 34.2 of UNIDO-TKL reads:

"If either party is prevented or delayed in the performance of any of his obligations under this Contract by circumstances of *Force Majeure*, and if the affected party has given written notice thereof to the other party within (15) days of the happening of such event, specifying the details constituting *Force Majeure*, with necessary evidence that a contractual obligation is thereby prevented or delayed, and that the anticipated period (estimated) during which such prevention, interruption or delay may continue, then the affected or obligated party shall be excused from the performance or punctual performance (as the case may be) of such obligation as from the date of such notice for so long as may be justified."

(c) *Termination of contract*

85. In most provisions on the termination of a contract based on breaches of contract such as delay in completion and non-conformity of work two notices are required. The first notice is to give an opportunity to the party in breach to remedy it.¹⁸ Where the breach is not or cannot be remedied a second notice is required to declare the contract avoided or terminated, if the injured party so wishes to terminate.

86. As termination is considered a remedy of last resort every effort is to be made to rescue the contract. Although the additional period for the rectification of defects is to enable the party to make good the defects, there is, nevertheless, a breach of contract which at the time of the first notice does not justify termination but only gives rise to an action for damages. The first notice serves as a prerequisite to the acquisition of the right to terminate.¹⁹

87. In the case of an exonerating event, the party wishing to claim relief must notify the other party of the event. If the event subsequently makes it impossible to perform the contract within a given time, either party is entitled to terminate by giving notice to the other party.

¹⁷ See A/CN.9/WG.V/WP.4/Add.5, XIII, *Exoneration*, para. 36 (Yearbook . . . 1981, part two, IV, B, 1). A similar provision is contained in the ICC *force majeure* clause. *Ibid.*, para. 38. But compare art. 79 of the Sales Convention (Yearbook . . . 1980, part three, I, B) (see para. 66 above).

¹⁸ See A/CN.9/WG.V/WP.4/Add.7, XVII, *Termination*, paras. 7-9 and 14-15 (Yearbook . . . 1981, part two, IV, B, 1).

¹⁹ The same approach has been adopted as regards non-delivery of the goods in the Sales Convention (art. 49 (1) (b); see, however, art. 49 (1) (a)) (Yearbook . . . 1980, part three, I, B).

88. Only in exceptional cases, such as bankruptcy, may a party terminate a contract by serving only one notice.²⁰

4. Notification of variation

89. Variation of a contract may involve additions or reductions to the work, and may therefore result in a change of the contract price, construction schedule or contract guarantees. Generally a variation would require mutual agreement, and notices of variation given by one party to the other may precede the reaching of such mutual agreement.²¹ These notices have the character of an offer and acceptance for the variation of the contract.

90. However, some provisions analysed in this study seem to enable the purchaser or the engineer to vary the contract unilaterally.²²

E. Legal effects of failure to notify

91. The legal effects of failure to notify are often dependent on the purpose of the duty to notify in the specific circumstances. The following are the main effects.

1. Loss of right

92. A right may be lost if no notice is given²³ within a certain period of time.

2. Liability for damages resulting from failure to notify

93. Failure to notify may result in liability for damages resulting from such failure.²⁴

94. Article 69(3) of the GCD-CMEA provides another example where a party is liable to pay damages caused by failure to notify the other party of an exonerating event.²⁵

F. Failure to respond to notice

95. Failure to respond to a notice given by a party may result in certain consequences. For example, where a purchaser is required to approve or disapprove documents drawn up by the contractor and he does not respond within a given period of time after he has been notified of the documents, a presumption of approval may be raised.²⁶ Such

a case, however, must be distinguished from the foregoing (section E above) as the consequences do not arise from the notification but from the failure to respond to it.

XXI. SETTLEMENT OF DISPUTES

A. General remarks

96. The comprehensive and complex nature of works contracts, their long-term character and the fact that disputes often concern technical issues, require the parties to pay special attention to the way in which disputes are to be settled. If a dispute arises before the construction of the works is completed, the work should continue to prevent damages which may be caused by any interruption of the construction. Parties are therefore interested in a speedy settlement of disputes.

97. In most cases, the first step in the settlement of such disputes is to endeavour to resolve them by negotiation and agreement. In some contracts there are procedures provided for in this respect, in particular a requirement that the parties are not to initiate legal proceedings without attempting first to settle their disputes or differences by an amicable arrangement.

98. Article 37.1 of UNIDO-TKL provides:

"In the event of any dispute, difference or contention in the interpretation or meaning of any of the Articles to this Contract or reasonable inference therefrom, both parties shall promptly make endeavour to resolve the dispute or differences by mutual discussion and agreement."

99. And article 37.3 of UNIDO-TKL further provides:

"Subject to the provisions of this Article, either the PURCHASER or the CONTRACTOR may demand Arbitration with respect to any claim, dispute or other matter that has arisen between the parties.

"37.3.1 However, no demand for Arbitration of any such claim, dispute or other matter shall be made until the later of (a) the date on which the PURCHASER or the CONTRACTOR, as the case may be, has indicated his final position on such claim, dispute or matter, or (b) the twentieth Day after the CONTRACTOR or PURCHASER, as the case may be, has presented his grievance in written form to the other, and no written reply has been received within twenty Days after such presentation of the grievance.

"37.3.2 No demand for Arbitration shall be made after the () Day following the date on which the PURCHASER or the CONTRACTOR, as the case may be, has rendered his written final decision in respect of the claim, dispute or other matter as to which Arbitration is sought. The PURCHASER or CONTRACTOR, as the case may be, shall be obliged to specify that the written

²⁰ See Part Two, XIX, *Bankruptcy*, para. 50.

²¹ See Part Two, III, *Variations*, paras. 26-27 and 43.

²² See Part Two, III, *Variations*, paras. 29-30 and 38-42.

²³ See A/CN.9/WG.V/WP.4/Add.5, XIII, *Exoneraton*, paras. 33 and 38 (Yearbook . . . 1981, part two, IV, B, 1). See also, articles 39 (1) and 43 of the Sales Convention (Yearbook . . . 1980, part three, I, B); A/CN.9/WG.V/WP.4/Add.2, VI, *Transfer of Technology*, para. 35 (Yearbook . . . 1981, part two, IV, B, 1); and clause 19.2 of FIDIC-EMW.

²⁴ See A/CN.9/WG.V/WP.4/Add.5, XIII, *Exoneraton*, para. 37 (Yearbook . . . 1981, part two, IV, B, 1).

²⁵ See also, para. 66 above.

²⁶ See A/CN.9/WG.V/WP.4/Add.1, I, *Drawings and Descriptive Documents*, para. 12 (Yearbook . . . 1981, part two, IV, B, 1). See also, articles 5.6, 6.12 and 27 of UNIDO-TKL. See also, A/CN.9/WG.V/WP.4/Add.3, VIII, *Inspection and Tests*, paras. 49 and 89 (Yearbook . . . 1981, part two, IV, B, 1).

decision is in fact the final decision within the meaning of this Sub-Article. Failure to demand Arbitration within said () Days period shall result in the decision being final and binding upon the other party."

Similar provisions are contained in article 37.1 and 37.3 of UNIDO-CRC.

100. The purpose of article 37.3 of UNIDO-TKL is evidently to speed up the settlement of disputes. The failure to demand arbitration within the time-limit agreed upon under article 37.3 is perhaps regarded as a consent of one party with the proposal made by the other party.²⁷

101. A provision for amicable settlement of disputes is also contained in clause 49.2 of FIDIC-EMW which provides that no dispute between the contractor and the purchaser shall be referred to arbitration unless an attempt has first been made to settle the dispute amicably.

102. Many disputes between parties to works contracts arise from disagreement concerning quality and other technical questions. It is advisable to settle these differences as soon as possible and not to wait for an arbitration award or a court decision. Technical questions in legal proceedings come before the arbitrators or judges long after the technical differences arose. This may have an undesirable influence on the implementation of a contract and even if technical experts are called upon to give their opinion in such proceedings the on-the-spot verification may become more difficult.

103. A technical expert may be appointed directly by the parties, or by a special institution selected by agreement between the parties, to give an opinion on a technical dispute. The parties may specify in their contract whether such a technical opinion should be considered as binding, or whether they should merely constitute evidence to which an arbitrator or judge should attach a certain weight without being bound by it. In clause 49.2 of FIDIC-EMW there is a reference to technical expertise to be used in connection with an amicable settlement of disputes. The engineer's position in settlement of disputes is dealt with in paragraphs 138-143.

B. Conciliation

104. If the parties fail to settle their dispute by themselves they may attempt to settle it by conciliation. As the parties are interested in solving their dispute without having to resort to costly and time-consuming proceedings they may agree upon conciliation before commencing court or arbitration proceedings.

105. The purpose of conciliation is to achieve an amicable settlement of the dispute with the assistance of an independent third party. The settlement of the dispute is based on the agreement of the parties as conciliators do not

adjudicate but only assist the parties in an impartial manner in their attempt to reach an agreement.

106. Taking into consideration the value of conciliation as a method of amicable settlement of disputes arising in the context of international commercial relations, UNCITRAL adopted at its thirteenth session, after consideration of the observations of Governments and interested organizations, the Conciliation Rules of the United Nations Commission on International Trade Law.²⁸ The use of these Rules was recommended by resolution 35/52 adopted by the General Assembly on 4 December 1980.²⁹

107. The UNCITRAL Conciliation Rules are designed to give guidance and settle problems arising in conciliation proceedings, in particular as regards the commencement of conciliation proceedings, appointment of conciliators, role of conciliators, settlement agreement and termination of conciliation proceedings. Under article 16 of these Rules the parties undertake not to initiate, during the conciliation proceedings, any arbitral or judicial proceedings in respect of a dispute that is the subject of the conciliation proceedings, except that a party may initiate arbitral or judicial proceedings where, in his opinion, such proceedings are necessary for preserving his rights.

108. There is a model conciliation clause by which the parties would agree on the application of the UNCITRAL Conciliation Rules. This clause reads:

"Where, in the event of a dispute arising out of or relating to this contract, the parties wish to seek an amicable settlement of that dispute by conciliation, the conciliation shall take place in accordance with the UNCITRAL Conciliation Rules as at present in force."

109. The UNCITRAL Conciliation Rules are suitable for all kinds of contracts in international trade, including works contracts.

110. In some general conditions and model contracts analysed in this study there are clauses which envisage conciliation without solving questions connected with conciliation proceedings.

111. Article 37.1.1 of UNIDO-TKL and UNIDO-CRC provides:

"Should the dispute or differences continue to remain unresolved both parties may each nominate a person to negotiate and reconcile the dispute or differences to resolve thereby the matter of contention between the parties arising out of the Contract. In the event that these two persons referred to cannot agree, they shall nominate a third Neutral Person to reconcile the dispute or difference. In case the two persons cannot agree on

²⁷ See Part Two, XX, *Notification*, para. 95.

²⁸ *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, paras. 105 and 106 (Yearbook ... 1980, part one, II, A).

²⁹ The Resolution and the Rules are set out in *UNCITRAL Conciliation Rules* (United Nations publication, Sales No. E.81.V.6).

a third Neutral Person or in case the efforts of the Neutral Person nominated by the two parties fail to resolve the difference within (6) months, both parties to the Contract shall proceed to Arbitration as provided for herein."

C. Arbitration

112. Works contracts like other contracts in international trade often contain an arbitration clause. International commercial arbitration is today a preferred method of settling disputes arising out of international trade. It is widely assumed that arbitration proceedings offer advantages over judicial proceedings as they are better adapted to the specific features of international trade. On the basis of international conventions, in particular the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958, the arbitral awards can be recognized and enforced abroad often more easily than court decisions.

113. Two kinds of international commercial arbitration are used in practice. The parties may choose either a permanent arbitration institution or an *ad hoc* arbitration. All arbitration institutions have rules according to which they become seized, the arbitrators are appointed, the arbitration proceedings are conducted and the awards are made. If the parties submit their dispute to an arbitration institution they are considered to agree upon the application of rules of such an institution.

114. Difficulties may arise if an *ad hoc* arbitration is chosen by the parties and they have not solved questions concerning arbitration proceedings in their arbitration agreement. A similar situation may also arise in cases where such questions are not settled in the rules of arbitration institutions. National legislation and international treaties may help to overcome some of those difficulties. The European Convention on International Arbitration of 1961 makes provisions for the regulation of various aspects of arbitration proceedings, including appointments of arbitrators, the procedure to be followed, the conflict of law rules to be applied and the recognition and enforcement of the award.

115. In 1966, the United Nations Economic Commission for Europe and the United Nations Economic Commission for Asia and the Far East (now the United Nations Economic and Social Commission for Asia and the Pacific) developed rules providing answers to most questions concerning arbitration proceedings. Particularly important and widely used are, however, the UNCITRAL Arbitration Rules, the use of which was recommended by the General Assembly in its resolution 31/98 of 15 December 1976.^{*30}

116. Arbitration proceedings can be effected in most cases only on the basis of a valid arbitration clause. However, disputes between organizations of the member countries of the Council for Mutual Economic Assistance (CMEA), arising in the international trade, are settled in arbitration proceedings without the need to conclude individual arbitration agreements. Such disputes are subject to arbitration, in an arbitration tribunal established for such disputes in the country of the defendant or, by agreement of the parties, in a third member-country of the CMEA. A counter-claim or set-off based on the same relationship as the original suit is subject to consideration in the same arbitration tribunal in which the original suit is considered. Arbitration awards are final.

117. These consequences follow from GCD-CMEA, GCA-CMEA and GCTS-CMEA. In 1972, Member States of the CMEA concluded a Convention on the Settlement by Arbitration of Civil Law Disputes Arising out of Relations Concerned with Economic, Scientific and Technological Co-operation, which requires, generally, obligatory arbitration proceedings for settlement of all disputes arising between organizations of CMEA countries from commercial relationships aimed at international economic, scientific and technical co-operation.

118. The parties when drafting an arbitration clause shall take into consideration the form of arbitration to be chosen (i.e. institutional arbitration or *ad hoc* arbitration) and determine which disputes are to be covered by the clause. The arbitration clause recommended for the application of the UNCITRAL Arbitration Rules reads as follows:

"Any dispute, controversy or claim arising out of or relating to this contract, or the breach, termination or invalidity thereof, shall be settled by arbitration in accordance with the UNCITRAL Arbitration Rules as at present in force."³¹

119. It appears that this clause covers disputes concerning questions as to

- (a) Whether the contract is valid or not;
- (b) What are the legal consequences of invalidity of contract;
- (c) The interpretation of the contract, in particular determining what are the duties and rights of the parties;
- (d) What are the legal consequences of the breach of contract including questions concerning exonerating circumstances;
- (e) When the contract is terminated (in cases where a party declares the contract avoided or where the con-

* Yearbook . . . 1976, part one, II, A).

³⁰ The Resolution and the Rules are set out in *UNCITRAL Arbitration Rules* (United Nations publication, Sales No. E.77.V.6).

³¹ *Official Records of the General Assembly, Thirty-first Session, Supplement No. 17 (A/31/17), Chap. V., para. 57 (Yearbook . . . 1976, part one, II, A).*

tract is terminated *ipso iure*) and what are the legal consequences thereof; and

(f) Other issues relating to the contract.

120. The attention of the parties is drawn to the possibility of inclusion, in the arbitration clause, of the appointing authority, the number of arbitrators, the place of arbitration and the language to be used in the arbitral proceedings. But if the parties fail to solve these questions in the arbitration clause, the UNCITRAL Arbitration Rules* provide for ways of settling these issues.

121. The scope and nature of the arbitration clauses, contained in the forms analysed in this study, are varied and some of them do not cover all disputes to which the UNCITRAL model arbitration clause applies.

122. Clause 28.1 of ECE 188A reads:

"Any dispute arising out of the contract shall be finally settled in accordance with the Rules of Conciliation and Arbitration of the International Chamber of Commerce, by one or more arbitrators designated in conformity with those Rules."

It may be doubtful whether this clause covers disputes concerning the validity of the contract and what the legal consequences of its invalidity are, as well as the legal consequences of its termination.

123. ECE 574A deals with settlement of disputes in arbitration proceedings in clause 28.1 which provides:

"Any dispute arising out of or in connection with the contract shall be finally settled by arbitration without recourse to the Courts. The procedure shall be such as may be agreed between the parties."

124. The scope of this clause is broader than that in clause 28.1 of ECE 188A as it covers not only disputes arising out of the contract but also disputes which arise in connection with the contract. The clause seems to include disputes relating to the breach of the contract, but the question remains open, whether it also covers disputes concerning the validity of the contract and legal consequences of the invalidity. This clause unlike that of ECE 188A does not refer to a set of arbitration rules so that the parties would still have agreed on the arbitration procedure (see paragraph 114 above).

125. In FIDIC-EMW and FIDIC-CEC there are arbitration clauses formulated in connection with the legal position of a consulting engineer in the settlement of disputes. Disputes may be referred to arbitration if the consulting engineer fails to solve them.

126. Under clause 67 of FIDIC-CEC (see paragraph 142 below) such disputes are to be settled under the Rules of Conciliation and Arbitration of the International Chamber of Commerce. This clause covers "any dispute or difference

of any kind whatsoever between the Employer and the Contractor or the Engineer and the Contractor in connection with, or arising out of the Contract, or the execution of the Works." The clause also relates to disputes between the engineer and the contractor though the engineer does not seem to be a party to the contract.³²

127. Clause 67 of FIDIC-CEC also covers disputes arising in connection with the execution of the works in addition to disputes connected with the contract. The question may arise whether this clause also includes disputes of an extra-contractual nature, such as disputes concerning accidents occurring in connection with the construction of the works.

128. In FIDIC-EMW the settlement of disputes by arbitration proceedings is dealt with in clause 49.3 which reads:

"If at any time any question, dispute or difference shall arise between the Employer and the Contractor in connection with or arising out of the contract or the carrying out of the Works (whether during the progress of the Works or after their completion, and whether before or after the termination, abandonment or breach of contract) which cannot be settled amicably either party shall, as soon as reasonably practicable, but not earlier than three months after a request made to settle the dispute amicably has been made to the other party, give to the other notice in writing of the existence of such question, dispute or difference specifying the nature and the point at issue, and the same shall be finally settled by Arbitration under the Rules of Conciliation and Arbitration of the International Chamber of Commerce by one or more Arbitrators appointed in accordance with those Rules."

129. In UNIDO-TKL and UNIDO-CRC arbitration is dealt with in article 37.4 which provides:

"All claims, disputes and other matters in question arising out of or relating to this Contract or the breach thereof which cannot be resolved by the parties shall be decided by arbitration in accordance with the terms contained in Annexure () attached hereto.³³ This agreement so to arbitrate shall be enforceable under the prevailing arbitration law. The award rendered by the arbitrator shall be final and judgements may be entered upon it in any court having jurisdiction thereof."

130. Under article 37.3.1 (see paragraph 99 above) demand for arbitration can be made by either party only after the date on which the other party has indicated its final position on such dispute. In this provision there is another period of time during which arbitration proceedings cannot be initiated, namely the period of 20 days after the date

³² See Part Two, VIII, *Engineer*.

³³ According to the UNIDO model contracts, this annexure is to be agreed upon by the parties.

* Yearbook . . . 1976, part one, II, A.

on which a party has presented his grievance in written form to the other party and provided no written reply is received within this period.

131. The parties agreeing to an arbitration clause normally intend their dispute to be settled by arbitration instead of by a court. Some contracts contain provisions to this effect.

132. Clause 28.1 of ECE 574A states that the disputes are to be finally settled by arbitration without recourse to the courts.

133. The parties may, however, agree upon an option to the claimant to initiate either court or arbitration proceedings.

134. Such an option seems to be included in the UNIDO model contracts. Article 37.5 of UNIDO-TKL and UNIDO-CRC appears to allow the initiation of court proceedings even during the period of time when the initiation of arbitral proceedings is possible. This article reads:

"Notice of the demand for arbitration shall be filed in writing with the other party to the Contract in accordance with the conditions contained in the Annexure referred to in Article 37.4 above.³⁴ The demand for arbitration shall be made within the period specified in Article 37.3,³⁵ after the claim, dispute or other matter in question has arisen, and in no event shall the demand for arbitration be made after institution of legal or equitable proceedings based on such claim, dispute or other matter in question if it would be barred by the applicable statute of limitations."

135. It should be noted that not all provisions of the forms under study are considered. For example, article 37.7 of UNIDO-TKL and UNIDO-CRC provides that arbitrators shall have unrestricted access to the plant (notwithstanding secrecy provisions) for the purpose of arbitration.

D. Court proceedings

136. In some works contracts there are exclusive jurisdiction clauses in which the parties determine the court of a particular place to which the parties should submit their disputes. The laws of most countries give effect, though under varying conditions, to such agreements in international trade contracts.

137. The certainty of the court which is to have jurisdiction in the dispute is useful for determining contractual rights and duties of the parties. Courts of all countries apply in principle conflict rules of their country and, in agreeing on the jurisdiction of the court, the parties indirectly determine what conflict of law rules are to apply to their contract. This is important even in the case of the choice by the parties of the applicable law as the extent of the admissibility of such a choice is to be judged on the basis of the

private international law of the country where the legal proceedings are taking place.

E. Engineer in settlement of disputes

138. Some works contracts provide that the consulting engineer may make observations or technical approvals or even take decisions on certain issues without prejudice to subsequent arbitration or other legal proceedings.

139. The procedure concerning the engineer's decision is provided for in clause 11 of FIDIC-EMW:

"The contractor shall proceed with the Works in accordance with the decisions, instructions and orders given by the Engineer in accordance with these conditions, provided always that:

"(a) if the Contractor shall, without undue delay after being given any decision, instruction or order otherwise than in writing, require it to be confirmed in writing, such decision, instruction or order shall not be effective until written confirmation thereof has been received by the Contractor, and

"(b) if the Contractor shall by written notice to the Engineer within 21 days after receiving any decision, instruction or order of the Engineer in writing or written confirmation thereof, dispute or question the decision, instruction or order, giving his reasons for so doing, the matter shall be referred to the Engineer who shall within a further period of 21 days by notice in writing, with reasons therefor, to the Contractor and the Employer, confirm, reverse or vary such decision."

140. In FIDIC-EMW, the legal nature of the engineer's decision is provided for in clause 49.1, which is as follows:

"If either the Employer or the Contractor is dissatisfied with a decision, instruction or order of the Engineer as confirmed, reversed or varied in accordance with Clause 11 (Engineer's Decisions) either party may subject to Sub-Clause 2³⁶ of this Clause refer the matter to arbitration pursuant to Sub-Clause 3 of this Clause,³⁷ but such reference shall not relieve the Contractor of his obligation to proceed with the Works in accordance with the decision, instruction or order as so confirmed, reversed or varied nor relieve the Employer of any of his obligations under the Contract. The Contractor shall be at liberty in any such Arbitration to rely on reasons additional to the reasons stated in the written notice given pursuant to Clause 11."

141. It would therefore appear that:

(a) The engineer is entitled to interpret the contract in connection with its implementation;

(b) Such an interpretation is binding on both parties, if the procedure provided for in the general conditions is

³⁴ Article 37.4 is quoted in para. 129.

³⁵ Article 37.3 is quoted in para. 99.

³⁶ Sub-clause 2 is quoted in para. 101.

³⁷ Sub-clause 3 is quoted in para. 128.

complied with until such an interpretation is changed by an arbitral award.

142. In FIDIC-CEC, the legal position of the engineer is dealt with in clause 67, which is as follows:

"If any dispute or difference of any kind whatsoever shall arise between the Employer and the Contractor or the Engineer and the Contractor in connection with, or arising out of the Contract, or the execution of the Works, whether during the progress of the Works or after their completion and whether before or after the termination, abandonment or breach of the Contract, it shall, in the first place, be referred to and settled by the Engineer who shall, within a period of ninety days after being requested by either party to do so, give written notice of his decision to the Employer and the Contractor. Subject to arbitration, as hereinafter provided, such decision in respect of every matter so referred shall be final and binding upon the Employer and the Contractor and shall forthwith be given effect to by the Employer and by the Contractor, who shall proceed with the execution of the Works with all due diligence whether he or the Employer requires arbitration, as hereinafter provided, or not. If the Engineer has given written notice of his decision to the Employer and the Contractor and no claim to arbitration has been communicated to him by either the Employer or the Contractor within a period of ninety days from receipt of such notice, the said decision shall remain final and binding upon the Employer and the Contractor. If the Engineer shall fail to give notice of his decision, as aforesaid, within a period of ninety days after being requested as aforesaid, or if either the Employer or the Contractor be dissatisfied with any such decision, then and in any such case either the Employer or the Contractor may within ninety days after receiving notice of such decision or within ninety days after the expiration of the first-named period of ninety days, as the case may be, require that the matter or matters in dispute be referred to arbitration as hereinafter provided. All disputes or differences in respect of which the decision, if any, of the Engineer has not become final and binding as aforesaid shall be finally settled under the Rules of Conciliation and Arbitration of the International Chamber of Commerce by one or more arbitrators appointed under such Rules. The said arbitrator/s shall have full power to open up, revise and review any decision, opinion, direction, certificate or valuation of the Engineer. Neither party shall be limited in the proceedings before such arbitrator/s to the evidence or arguments put before the Engineer for the purpose of obtaining his said decision. No decision given by the Engineer in accordance with the foregoing provisions shall disqualify him from being called as a witness and giving evidence before the arbitrator/s on any matter whatsoever relevant to the dispute or difference referred to the arbitrator/s as aforesaid. The reference to arbitra-

tion may proceed notwithstanding that the Works shall not then be or be alleged to be complete, provided always that the obligations of the Employer, the Engineer and the Contractor shall not be altered by reason of the arbitration being conducted during the progress of the Works."

143. The consequences of the engineer's decision under the clause quoted in the previous paragraph are similar to those mentioned in paragraph 141. However, in addition, the parties seem to be limited in respect of initiating arbitration proceedings by time-limits stipulated therein.

F. *Effect of resort to dispute settlement proceedings on duty to perform*

144. The mere fact that the parties have commenced negotiations for the settlement of disputes, or arbitral or court proceedings does not by itself relieve either party from his contractual obligations or justify a postponement of performance. Moreover, in some contracts it is stressed that in case of a dispute both parties are obliged to continue with the performance of their obligations.

145. Article 37.2 of UNIDO-TKL and UNIDO-CRC stipulates in this respect:

"Notwithstanding the existence of a dispute, the CONTRACTOR and PURCHASER shall continue to carry out their obligations under the Contract, and payment(s) to the CONTRACTOR shall continue to be made in accordance with the Contract that in the appropriate cases qualify for such payment(s)."

146. Article 37.6 of UNIDO-TKL and UNIDO-CRC provides as follows:

"The CONTRACTOR and the PURCHASER shall continue the work and undertake their obligations under the Contract in accordance with Article 37.2 and the Contractor shall maintain the progress schedule during any arbitration proceedings, unless otherwise agreed by the PURCHASER in writing.

37.6.1 Before commencement or continuation of the work which is the subject of the dispute under arbitration, the CONTRACTOR may request, at his discretion, a bank guarantee from the PURCHASER to cover the CONTRACTOR's estimate of the additional costs involved. The bank guarantee shall be payable in part or in full only as a result of Arbitration proceedings in favour of the CONTRACTOR, and shall be valid until 30 days after the Arbitration Award."

147. Another provision concerning this subject is obtained in article 37.1.2. of UNIDO-TKL and UNIDO-CRC which reads:

"Pending resolution of any such claim or dispute pursuant to Article 37.1.1 the Contractor shall perform in accordance with the Contract without prejudice to

any claim by the CONTRACTOR for additional compensation and/or time to complete the work if such instructions (are in his opinion) above and beyond the requirements of the Contract."

148. Clause 49.4 of FIDIC-EMW, which deals with a relationship between the obligation to perform in case of arbitration and suspension of contract, reads:

"Performance of the Contract shall continue during Arbitration proceedings unless the Employer shall order the suspension thereof, and if any such suspension shall be ordered the reasonable expenses of the Contractor occasioned by such suspension shall be included in the Contract Price if the Arbitrators so decide. No payments due or payable by the Employer shall be withheld on account of pending reference to Arbitration."

149. It seems to follow from this provision that the obligation to proceed with the performance of the contract (by the contractor) does not apply if the purchaser suspends the performance of the contract irrespective of whether or not he was entitled to do so.

Part Three

[A/CN.9/WG.V/WP.7/Add.6*]

LIST OF QUESTIONS FOR CONSIDERATION BY THE WORKING GROUP

A. Introduction

The Working Group may wish to consider the questions listed below in its discussion of the topics in the light of Study II. As in Study I, the list is not intended to be exhaustive.

B. Questions

I. Feasibility studies

1. Should the contractor be obliged to verify the accuracy and adequacy of

(a) Feasibility studies, or

(b) Information on which these studies are based supplied to him by the purchaser? (See also question 55).

2. If question 1 is answered in the affirmative, should this obligation be limited to the discovery of evident errors or defects, or should it be wider?

3. If question 1 is answered in the affirmative, should this obligation be limited to feasibility studies and information which are to be used as a basis for the work to be performed by the contractor?

4. Should the contractor be obliged, independently of studies or information supplied by the purchaser, to make studies and obtain information necessary for him to carry out his obligations under the contract?

5. If question 1 or 4 is answered in the affirmative, how should the legal implications arising from a discrepancy between verification, studies made and information obtained by the contractor, and studies and information supplied by the purchaser, be settled?

6. When physical conditions are dealt with in feasibility studies, to what extent should the contractor be responsible for his performance under the contract when a change of physical conditions affects such performance?

7. If the contractor is to bear some responsibility in respect of feasibility studies or information supplied to him by the purchaser who had obtained them from a third party, should the purchaser be obliged to assign to the contractor his rights arising from a breach of obligation by the third party in preparing such study or obtaining such information?

II. Formation of contract

(Questions on the legal issues involved in tender procedure have not been formulated for the reasons indicated in A/CN.9/WG.V/WP.7/Add.1, paragraph 22**.)

8. Should the legal guide analyse legal problems connected with contractual terms which under the works contract are to be agreed upon in the future by the parties?

9. Should the legal guide analyse legal problems connected with contracts subject to condition (e.g. entry into force subject to condition)?

III. Variation

10. Should the purchaser be entitled unilaterally to vary the scope of the work undertaken by the contractor, if so, under what circumstances, and to what extent?

11. Should the contractor be entitled unilaterally to vary the scope of the work undertaken by him, and if so, under what circumstances, and to what extent?

12. If question 10 or 11 is answered in the affirmative, by what procedure should the scope of consequent variations in other contractual provisions (e.g. price, time schedule, performance guarantees) be determined?

IV. Interpretation

13. Should the contract include a provision on general rules of interpretation? If so, what principles should be reflected in these rules?

14. To what extent should the negotiations be taken into consideration in interpreting a contract (e.g. views

* 27 April 1982.

** Reproduced in this volume, part two, IV, B.

exchanged, statements made, or conduct during negotiations)?

15. Should the legal guide recommend definitions of certain terms often used in works contracts? Which terms should be defined?

16. Should the legal guide recommend rules to resolve conflicts between the contract, annexures thereto, and general conditions incorporated by reference?

V. *Assignment*

17. Should either party be allowed to assign the contract as a whole, and if so, under what conditions?

18. Should either party be allowed to assign his rights under the contract, and if so, to what extent?

19. Should either party be allowed to assign his obligations under the contract, and if so, to what extent?

VI. *Sub-contracting*

20. Should the ability of the contractor to sub-contract be restricted, and if so, to what extent?

21. When sub-contracting is permitted, to what extent should the purchaser participate in the selection of a sub-contractor by the contractor? (See also question 35).

22. To what extent should the terms of the sub-contract be determined in the main contract?

23. If the contractor is obliged to procure equipment or services for the purchaser, should he be obliged

(a) To conclude contracts with a third party in his own name on account of the purchaser; or

(b) To conclude contracts with a third party on behalf of the purchaser; or

(c) To assist the purchaser in his negotiations with a third party? (See also question 36).

24. Should the purchaser be entitled to pay the sub-contractor if the contractor fails to pay him, and if so, under what conditions?

25. Should the legal guide deal with contracts entered into by the purchaser with third parties in connection with the execution of the works?

26. If question 25 is answered in the affirmative, should the sub-contractors to be employed by the purchaser be agreed upon between the contractor and the purchaser, and if so, in which cases?

27. Should the legal guide deal with the consequences of failure of performance by the purchaser's suppliers affecting the execution of the contract by the contractor?

VII. *Co-ordination and liaison agents*

28. Should a liaison agent be designated by each party in the contract, and if so, should the scope of the agent's

authority be determined in the contract by the party designating him?

29. Should the contract include a provision on the duty of the parties to co-operate in the execution of the contract, and if so, how should this duty be defined?

30. What co-ordination procedure should be agreed upon in the contract?

VIII. *Engineer*

31. What should be the main functions and scope of authority of the engineer as the purchaser's representative?

32. In addition to his functions as the purchaser's representative, should the engineer be given the function of deciding certain issues affecting the parties as an impartial person? (See also questions 92 and 93).

33. If the answer to question 32 is in the affirmative, how should his duty to be impartial be defined?

IX. *Liabilities in respect of third parties*

34. In what cases, if any, should the contractor be fully responsible for failure to perform by a third party (e.g. employee, sub-contractor) whom the contractor has engaged for the fulfilment of his obligations under the contract and in what cases, if any, should the contractor's responsibility be limited?

35. Should the responsibility of the contractor for sub-contractors employed by him differ, depending on whether they have been chosen solely by the contractor, or on whether the purchaser has participated in their selection?

36. What should be the responsibility of the contractor

(a) If he concludes contracts as described in question 23 (a)?

(b) If he concludes contracts as described in question 23 (b)?

(c) If he assists in negotiations as described in question 23 (c)?

37. Should the legal guide deal with loss or damage caused to the purchaser in connection with the execution of the contract by employees or sub-contractors of the contractor, or loss or damage caused to the contractor in connection with the execution of the contract by employees or sub-contractors of the purchaser?

X. *Technical assistance*

38. What issues should be addressed in connection with the provision of training (e.g. place of training, payment conditions, type of training)?

39. What issues should be addressed in connection with the provision of management services (e.g. payment conditions, type of management, responsibility for operation of the works)?

40. What kinds of technical assistance other than the provision of training and management services should be dealt with in the legal guide?

41. If technical assistance other than training and management services are to be dealt with, what issues should be addressed in connection therewith?

42. Are there any special problems (other than those involved in the transfer of technology) in protecting confidential information conveyed through technical assistance? If so, how should such problems be solved?

XI. *Maintenance and spare parts*

43. Should the legal guide deal with the contractor's obligation to maintain the works?

44. If question 43 is answered in the affirmative, what should be the scope of the main obligations of the contractor in regard to the maintenance of the works after the expiry of the guarantee period?

45. What should be the obligations of the contractor in regard to the supply of spare parts manufactured by him? (See also question 8.)

46. Should the contractor be obliged to procure spare parts manufactured by third parties? (See also question 23.)

47. If question 46 is answered in the affirmative, what should be the extent of his obligation in connection with such procurement? (See also questions 23 and 26.)

XII. *Storage on site*

48. To what extent should either of the parties be obliged to provide storage facilities and to store materials and equipment on site?

49. Who should bear the costs connected with such provision of storage facilities and storing?

50. Who should bear the risks in respect of materials and equipment stored on site, and to what extent?

XIII. *Price*

51. What factors favour the adoption of

- (a) A lump-sum price, or
- (b) A price on the basis of time incurred and work done, or
- (c) A reimbursable price for a works contract, or certain items herein?

52. If the price is to be determined on the basis of time incurred and work done, what procedures are appropriate for measuring the time incurred and work done?

53. In the case of a reimbursable price, what procedures are appropriate for determining the price payable?

54. Should the legal guide deal with issues concerning price currency, and if so, which issues?

XIV. *Revision of price*

55. Should the contractor be entitled to an increase in price if the scope of the work has to be changed owing to the discovery of errors in the data supplied by the purchaser?

56. Should there be a revision of the price when a change in the laws in force on the site requires an alteration of the works? (See also question 12.)

XV. *Payment conditions*

57. How should the due date of an advance payment be determined?

58. What conditions should be required for payments to be made during the course of the execution of the contract?

59. What conditions should be required for payments to be made after completion of the works?

60. What conditions should be required for payments to be made after the expiration of the guarantee period?

61. Should the legal guide deal with issues relating to bonus stipulated for completion of the work by the contractor before the due date?

62. When the contractor has granted credit to the purchaser, should issues relating to the credit terms be analysed?

XVI. *Performance guarantees*

63. What should be the legal nature of the performance guarantee (e.g. independent, accessory, subsidiary)?

64. At what time should the performance guarantee be provided?

65. Should the contract provide for a reduction in the amount of the performance guarantee? If so, under what circumstances and to what extent should the amount of the guarantee be reduced?

66. When the performance guarantee is subsidiary, what steps should the purchaser take before he is entitled to claim under the guarantee?

67. Should the guarantor's obligations be limited to the payment of a sum of money, or might it also include other obligations?

68. What should be the effect upon the performance guarantee of variation of the contract?

69. Should the legal guide deal with the period to be covered by a performance guarantee?

XVII. *Insurance*

70. What risks should be covered by insurance of the materials and equipment to be incorporated in the works, and who should provide such insurance?

71. What period of time should be covered by the insurance mentioned in the previous question?

72. Should insurance of the materials and equipment cover the time during which the contractor bears the risks in respect of such materials and equipment?

73. What risks should be covered by insurance of the works during the construction, and who should provide such insurance?

74. Should the contractor's equipment be covered by insurance?

75. Should the legal guide deal with liability insurance of the purchaser and contractor?

76. What should be the consequences of failure to provide insurance in accordance with the contract?

XVIII. *Customs duties and taxes*

77. Should the legal guide deal with issues relating to customs duties?

78. Should the legal guide deal with issues relating to taxes and levies?

XIX. *Bankruptcy*

79. Should the bankruptcy of either party be dealt with only in chapters dealing with other topics when bankruptcy is relevant to such topics?

80. What should be the rights under a works contract of the purchaser on the bankruptcy of the contractor, and vice versa?

XX. *Notices*

81. In what contexts in works contracts should the despatch theory under article 27 of the Sales Convention be adopted?

82. In what circumstances should notice constitute a pre-requisite to the exercise of a right?

83. Should a failure to notify within a time-limit result in the loss of a right, and if so, in what circumstances?

84. In what situations, if any, should a presumption of approval or consent be raised upon failure to respond to a notice within a time-limit?

85. What consequences should the failure to notify have in cases not covered by questions 82 and 83 above?

XXI. *Settlement of disputes*

86. Should the parties be obliged to attempt to settle their disputes by negotiation before instituting legal proceedings?

87. If question 86 is answered in the affirmative, what procedure should be provided for such negotiation?

88. For the settlement of disputes concerning technical issues, should the parties be obliged to refer such disputes to a technical expert for his opinion prior to instituting legal proceedings?

89. Should the legal guide deal with conciliation as a means of dispute settlement?

90. In relation to the use of arbitration as a means of dispute settlement, should the legal guide only recommend the use of the UNCITRAL Arbitration Rules, or in addition analyse the special problems connected with the use of arbitration in works contracts?

91. Should the legal guide deal with clauses on court jurisdiction?

92. Should the engineer be authorized to settle disputes between the contractor and the purchaser and, if so, should such an authorization be limited to technical issues?

93. If question 92 is answered in the affirmative, what should be the legal nature of the engineer's decision given in the settlement of a dispute?

V. MOST-FAVOURED-NATION CLAUSES

Note by the Secretariat: most-favoured-nation clauses (A/CN.9/224)*

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INTRODUCTION

1. In resolution 36/111 of 10 December 1981 the General Assembly has requested *inter alia* the United Nations Commission on International Trade Law to submit any written comments and observations which it deems appropriate on chapter II of the report of the International Law Commission (ILC) on the work of its thirtieth session,¹ and in particular on the draft articles on most-favoured-nation clauses adopted by the International Law Commission and those provisions relating to such clauses on which the International Law Commission was unable to take a decision. The resolution is reproduced in the annex to this note.

I. BACKGROUND TO GENERAL ASSEMBLY RESOLUTION 36/111

2. At its nineteenth session in 1967, the International Law Commission decided to place on its programme of work the topic of "most-favoured-nation clauses in the law of treaties".² The title of the topic was shortened to "the most-favoured-nation clause" by the International Law Commission at its twentieth session in 1968.

3. The General Assembly, after considering the report of the International Law Commission on the work of its nineteenth session, recommended in resolution 2272 (XXII) of 1 December 1967 that the International Law Commission study the topic. From that time on, the topic was normally inscribed on the International Law Commission's agenda until its completion of the project in 1978.

4. At its thirtieth session in 1978, the International Law Commission finalized its draft articles on most-favoured-nation clauses and recommended to the General Assembly that the draft articles should be recommended to Member States with a view to the conclusion of a convention on the subject.³

5. After considering the report of the International Law Commission on the work of its thirtieth session, the General Assembly, by resolution 33/139 of 19 December 1978, invited all States, organs of the United Nations which had competence in the subject matter and interested inter-governmental organizations to submit their written comments and observations on the draft articles and on provisions on which the International Law Commission was unable to take a decision, and requested States to comment on the recommendation that the draft articles should be recommended to Member States with a view to the conclusion of a convention on the subject. Comments were received from 18 States and 5 intergovernmental organizations.⁴

* 20 May 1982.

¹ *Official Records of the General Assembly, Thirty-third Session, Supplement No. 10, A/33/10 and Corrigendum (Arabic only). (Yearbook of the International Law Commission 1978, vol. II, Part Two.)*

² Report of the International Law Commission on the work of its nineteenth session, 8 May-14 July 1967 (A/6709/Rev.1 and Rev. 1/Corr.1), para. 48 (*Yearbook of the International Law Commission 1967, vol. II.*)

³ Report of the International Law Commission on the work of its thirtieth session, note 1 above, para. 73.

⁴ These comments are collected in A/35/203 and Add. 1-3, and compiled analytically in A/35/443.

6. On 15 December 1980, the General Assembly, aware of the fact that more replies were needed, adopted resolution 35/161, reiterating the invitation contained in resolution 33/139. Comments were received from five States, one organ of the United Nations and five intergovernmental organizations.⁵ At its thirty-sixth session the General Assembly adopted resolution 36/111.

II. PURPOSE OF ILC DRAFT ARTICLES ON MOST-FAVOURLED-NATION CLAUSES

7. The ILC draft articles are not intended to interfere with or prejudice the agreement of States upon most-favoured-nation treatment; rather, they have a residual character. They are designed to assist in the interpretation and application of most-favoured-nation clauses to which States might wish to agree in their international relations.

"The [International Law] Commission was unanimous in the view that the granting and beneficiary States might agree on most-favoured-nation treatment in all matters that lent themselves to such treatment: they might specify the sphere of relations in which they undertook most-favoured-nation obligations and they might restrict *ratione materiae* their respective promises. The Commission also agreed that States might, in the clause itself or in the treaty containing the clause or otherwise, reserve their right to grant preferences, i.e. to except from the application of the most-favoured-nation clause favours that they granted to one or more States. It is understood, however, in this connection, that the present article should not be used as a pretext for discrimination."⁶

Pursuant to draft article 29, the draft articles would be without prejudice to any provision on which the parties to a most-favoured-nation clause may otherwise agree.

8. The draft articles, therefore, do not purport to prescribe the existence, nature or scope of most-favoured-nation treatment in relations among States. For example, the draft articles would not obligate States to grant most-favoured-nation treatment to any other State. Nor would they require the granting of any particular type of most-favoured-nation treatment (e.g. unconditional, conditional or reciprocal). Such matters would depend upon the agreement of States to a most-favoured-nation clause.

9. Nor do the draft articles purport to resolve concrete issues of international trade policy. The draft articles do not purport to establish the principles or rules under which trade occurs. The International Law Commission has recognized that such issues may be addressed by States in other fora.⁷

⁵ These comments are collected in A/36/145 and compiled analytically in A/36/146.

⁶ Report of the International Law Commission on the work of its thirtieth session, note 1 above, commentary to draft art. 29.

⁷ *Ibid.*, para. 62.

III. THREE ILLUSTRATIVE ISSUES RELEVANT TO INTERNATIONAL TRADE

10. The comments and observations on the ILC draft articles submitted in writing thusfar to the General Assembly by States and organizations, and expressed orally before the Sixth Committee during the thirty-fifth and thirty-sixth sessions of the General Assembly, do not reveal major disagreement on the principles behind many of the provisions in the International Law Commission's draft articles. There are, however, some significant issues in connection with the draft articles concerning which substantial differences of opinion have been expressed. The following are examples of such issues:⁸

(a) Whether a text on most-favoured-nation clauses should apply to most-favoured-nation clauses in relations involving economic groupings of States;

(b) Whether a text on most-favoured-nation clauses should imply an exception from the operation of a most-favoured-nation clause for benefits granted among members of a customs union or a free trade area;

(c) Whether a text on most-favoured-nation clauses should contain provisions for interpreting most-favoured-nation clauses which grant conditional most-favoured-nation treatment.

Even as to these issues, however, the Commission might consider it possible to agree on general comments and observations. The following observations concerning these issues might be helpful to the Commission in this regard.

A. Application of text on most-favoured-nation clauses to clauses in relations involving economic groupings of States

11. According to draft articles 1 and 6, the application of the ILC draft articles would be restricted to most-favoured-nation clauses in relations of States as between themselves. In previous comments and observations on the draft articles, several States and some intergovernmental organizations have pointed out that economic groupings of States are assuming greater importance in the international economy, and that one of these groupings in particular (the European Economic Community), which accounts for a significant portion of world trade, concludes trade treaties containing most-favoured-nation clauses. It has been suggested that a text on most-favoured-nation clauses should also apply to most-favoured-nation clauses in

⁸ In resolution 36/111 the General Assembly also requested States to comment on the recommendation of the International Law Commission that the draft articles on most-favoured-nation clauses should be recommended to Member States of the United Nations with a view to the conclusion of a convention on the subject. Since this request was directed to States, the Commission may consider it unnecessary to consider the question of the form that a text on most-favoured-nation clauses might take.

relations involving such economic groupings, in order to render the text complete and to have it accord with actual practice in international commerce.

12. The International Law Commission originally took up its study of most-favoured-nation clauses as an aspect of the general law of treaties, and its draft articles on most-favoured-nation clauses are designed to be interpreted in light of the Vienna Convention on the Law of Treaties.⁹ Accordingly, the International Law Commission has restricted the scope of application of its draft articles on most-favoured-nation clauses to correspond with a similar restriction in article 1 of the Vienna Convention.¹⁰

13. From a strictly legal viewpoint, however, a text on most-favoured-nation clauses need not necessarily be restricted to clauses in relations between States. A most-favoured-nation clause is normally only one provision in a trade agreement. Issues concerning the treaty as a whole (i.e. conclusion, entry into force, observance, application, interpretation, invalidity, termination etc.) would be governed by legal rules independent of a text on most-favoured-nation clauses. A text concerning the interpretation and application of most-favoured-nation clauses might be structured so as not to affect the law governing these issues.

14. One objection to the application of a text on most-favoured-nation clauses to clauses in relations involving economic groupings of States, expressed during consideration of the ILC draft articles in the Sixth Committee, was based on the view that "supranational organizations" should not be placed on the same level as sovereign States. In international practice, however, it may become more common for economic groupings to become parties to trade treaties with States. The application of a text on most-favoured-nation clauses to assist in the interpretation and application of most-favoured-nation clauses in relations involving such economic groupings need not presuppose or imply an equation of the economic grouping with sovereign States.

B. *Benefits granted among members of a customs union or a free trade area*

15. Several comments and observations on the ILC draft articles submitted thusfar have suggested that a text on most-favoured-nation clauses should exclude from the operation of a most-favoured-nation clause benefits which a contracting party to the clause accords pursuant to its membership in a customs union or free trade area. Proponents

of such an exception have argued that members of a customs union or a free trade area do not intend the benefits which members grant to each other to extend to non-members through most-favoured-nation clauses — that this would be inconsistent with the purpose of a customs union or a free trade area; and that without such an exception it would be impossible to create a customs union or a free trade area. It has also been contended that the existence of such an exception can be implied in customary international law.

16. An opposing view has argued that the existence of such an exception would favour one group of States at the expense of others, and that the exception does not constitute a generally recognized norm of international law.

17. A majority of commercial treaties containing a most-favoured-nation clause expressly excludes from the operation of the clause benefits granted by a contracting party pursuant to its membership in a customs union or a free trade area. Most world trade is conducted under rules providing for most-favoured-nation treatment which is subject to an express exception to that effect.¹¹ The underlying issue, therefore, is whether, with respect to those most-favoured-nation clauses which are silent as to the existence or non-existence of such an exception, the exception should be implied.

18. At its thirtieth session, the International Law Commission had before it a proposal to include in the draft articles a provision dealing with this issue in order to assist in the interpretation and application of such most-favoured-nation clauses.¹² The International Law Commission agreed not to include such a provision in the draft articles, citing the inconclusiveness of the comments made thereon and the lack of time to consider the matter. The International Law Commission emphasized, however, that the silence of the draft articles on this subject could not be interpreted as an implicit recognition of the existence or non-existence of such a rule but should, rather, be interpreted to mean that the ultimate decision was one to be taken by the States to which the draft was submitted at the final stage of the codification of the topic.¹³

19. In connection with this issue the following points may be noted:

(a) A term in a text on most-favoured-nation clauses providing for the implied exception would merely assist in the interpretation and application of those most-favoured-nation clauses in which the parties had not expressly stated whether customs union or free trade area benefits are to be included in or excluded from the operation of the clause. The parties to a most-favoured-nation clause could, if they so agreed, override this provision by stipulating in the clause

⁹ Report of the International Law Commission on the work of its thirtieth session, note 1 above, para. 59.

¹⁰ The International Law Commission is currently in the process of elaborating a new text dealing with treaties concluded between States and international organizations or between two or more international organizations. At its thirty-third session, the International Law Commission completed its second reading of 26 draft articles on this topic. Report of the International Law Commission on the work of its thirty-third session, 4 May-24 July 1981, para. 105. (*Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 10, A/36/10.*)

¹¹ E.g., art. XXIV of the General Agreement on Tariffs and Trade (GATT), which accounts for a major portion of world trade, and most-favoured-nation clauses in bilateral treaties.

¹² Report of the International Law Commission on the work of its thirtieth session, note 1 above, para. 57.

¹³ *Ibid.*, para. 58.

whether or not benefits granted pursuant to a customs union or a free trade area are to be included in the operation of the clause. Draft article 29 provides that the draft articles "are without prejudice to any provision on which the granting State and beneficiary State may otherwise agree";

(b) A text on most-favoured-nation clauses could be made non-retroactive (as are the ILC draft articles pursuant to draft article 28). Such a text would apply only to most-favoured-nation clauses in treaties which are concluded after the text became effective. Parties negotiating a most-favoured-nation clause subsequent to the coming into effect of a text on most-favoured-nation clauses which provides for the implied exception would therefore be able to take this provision into account in deciding whether to have the most-favoured-nation clause expressly include or exclude customs union or free trade area benefits;

(c) In most cases, a State which is a member of a customs union or a free trade area would take this membership, and its attendant obligations, into account in its subsequent negotiation of a most-favoured-nation clause with a non-member. A text on most-favoured-nation clauses might therefore provide for the implied exception only in respect of benefits accorded pursuant to a customs union or free trade area to which a party becomes a member after it enters into the treaty containing the most-favoured-nation clause. If this approach were adopted, and if a text on most-favoured-nation clauses were not to apply retroactively, then developing countries might conclude that the implied exception would not prejudice their interests. This would be true particularly if developing countries believe that they are more likely to engage in economic integration in the future than are developed countries;

(d) A provision in a text on most-favoured-nation clauses providing for the implied exception could be made subject to conditions, such as one providing for negotiations aimed at resolving the conflicting interests of the party which joins a customs union or free trade area, and the beneficiary of the most-favoured-nation clause. The implied exception might also be subject to provisions designed to accommodate the special circumstances of developing countries.

C. Conditional most-favoured-nation clauses

20. The ILC draft articles contain provisions designed to assist in the interpretation and application of most-favoured-nation clauses which are made subject to conditions of compensation and reciprocal treatment (draft articles 12 and 13). Many comments and observations on the draft articles submitted thus far have objected to such provisions, contending, in essence, that conditional most-favoured-nation clauses should not be used in international relations.

21. According to draft articles 11 and 15, most-favoured-nation clause make it conditional. The Interna-

tional Law Commission has concluded that the traditional type of conditional most-favoured-nation clause "has almost disappeared from the international scene"¹⁴ and "is now largely of historical significance".¹⁵ However, the International Law Commission included draft articles 12 and 13 to serve as an aid to interpreting clauses conditioned on compensation or reciprocity in case the parties to a treaty agree to a most-favoured-nation clause containing such conditions.¹⁶ If a text on most-favoured-nation clauses were to include provisions comparable to draft articles 12 and 13, the text could perhaps make it clear that such provisions are only to assist in the interpretation and application of a most-favoured-nation clause which the parties themselves have agreed to make conditional, and are not to be deemed to endorse the use of conditional most-favoured-nation clauses in international relations.

22. It might even be possible for a text on most-favoured-nation clauses to accomplish the interpretative objective of draft articles 12 and 13 without making specific reference to clauses conditioned upon compensation or reciprocity. The principle behind draft articles 12 and 13 is, in essence, that a beneficiary under a most-favoured-nation clause would be entitled to most-favoured-nation status only in accordance with the terms and conditions to which the parties to the clause have agreed. The statement of such a principle in general terms¹⁷ might make it possible to avoid the inclusion of provisions such as draft articles 12 and 13. Under this approach a text on most-favoured-nation clauses could accomplish the aims of draft articles 12 and 13 without appearing to sanction or endorse most-favoured-nation clauses conditioned on compensation or reciprocity.

IV. PROCEDURE FOR PREPARATION OF RESPONSE TO REQUEST OF GENERAL ASSEMBLY

23. The Commission, in response to the General Assembly's request to assist in the project of harmonizing and unifying the law relating to the interpretation and application of most-favoured-nation clauses, may wish to consider the formulation of comments and observations on the ILC draft articles from the point of view of the progressive harmonization and unification of this aspect of the law of international trade.

24. The General Assembly in resolution 36/111 has requested written comments and observations by 30 June 1983. Therefore, the substance of the response could be considered and finalized at the sixteenth session of the Commission. At the present session, the Commission may wish to consider how to proceed in the formulation of written comments and observations.

¹⁴ *Ibid.*, commentary to draft arts. 11, 12 and 13, para. 10.

¹⁵ *Ibid.*, commentary to draft arts. 11, 12 and 13, para. 11.

¹⁶ *Ibid.*

¹⁷ See draft art. 14.

25. The Commission may consider it appropriate to make general comments on the ILC draft articles, or on particular draft articles. This suggested approach was followed by intergovernmental organizations¹⁸ and the United Nations organ¹⁹ which have already submitted written comments and observations on the draft articles.

26. In deciding how to proceed in response to the request of the General Assembly, the Commission might wish to consider the following possibility. If the Secretariat were so authorized by the Commission at its fifteenth session, the Secretariat could, subsequent to that session, prepare a draft of comments and observations on the ILC draft articles. In doing so, the Secretariat would take into account the various views concerning the draft articles which have been expressed thusfar, and attempt to propose possibilities for agreement on general comments concerning the ILC draft articles which would be consistent with the interests of States and with the goal of the progressive harmonization and unification of this area of international trade law. The draft comments and observations could be issued in sufficient time for States to consider them prior to the sixteenth session of the Commission. The draft comments and observations could be placed before the Commission at its sixteenth session, at which time the Commission could consider and finalize the substance of any comments and observations that it deems appropriate.

ANNEX

Resolution adopted by the General Assembly

36/111. CONSIDERATION OF THE DRAFT ARTICLES ON MOST-FAVOURED-NATION CLAUSES

The General Assembly,

Recalling its resolution 33/139 of 19 December 1978 relating to the report of the International Law Commission on the work of its thirtieth session^a in particular section II of the resolution,

¹⁸ A/35/203 and Add.1 and 2; A/36/145.

¹⁹ A/36/145, section III.

^a *Official Records of the General Assembly, Thirty-third Session, Supplement No. 10 (A/33/10).*

Recalling also its resolution 35/161 of 15 December 1980, entitled "Consideration of the draft articles on most-favoured-nation clauses".

Reaffirming its appreciation of the high quality of the work done by the International Law Commission in elaborating a series of draft articles on most-favoured-nation clauses,

Bearing in mind the importance of facilitating international trade and development of economic co-operation among all States on the basis of equality, mutual advantage and non-discrimination in the establishment of the new international economic order,

Having considered the item entitled "Consideration of the draft articles on most-favoured-nation clauses", including the report of the Secretary-General^b and the analytical compilation of comments and observations from Governments, organs of the United Nations which have competence in the subject-matter and interested intergovernmental organizations,^c submitted pursuant to paragraphs 3 and 4 of General Assembly resolution 35/161,

Taking note of the comments and observations submitted, in particular those relating to outstanding issues,

Aware of the fact that more replies from States and interested intergovernmental agencies are needed,

1. *Requests* the Secretary-General to reiterate his invitation to Member States, interested organs of the United Nations, such as the regional commissions and the United Nations Commission on International Trade Law, as well as interested intergovernmental organizations, to submit or bring up to date, not later than 30 June 1983, any written comments and observations which they deem appropriate on chapter II of the report of the International Law Commission on the work of its thirtieth session, in particular on:

(a) The draft articles on most-favoured-nation clauses adopted by the International Law Commission;

(b) Those provisions relating to such clauses on which the International Law Commission was unable to take a decision;

and also requests States to comment on the recommendation of the International Law Commission that those draft articles should be recommended to Member States with a view to the conclusion of the convention on the subject;

2. *Decides* to consider the substance of the draft articles on most-favoured-nation clauses, together with any amendments thereto, at its thirty-eighth session with a view to taking a decision thereon;

3. *Decides* to include in the provisional agenda of its thirty-eighth session the item entitled "Consideration of the draft articles on most-favoured-nation clauses" and to consider it as a matter of priority.

92nd plenary meeting
10 December 1981

^b A/36/145.

^c A/36/146.

VI. CO-ORDINATION OF WORK

A. Note by the Secretary-General: co-ordination of activities (A/CN.9/226)*

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INTRODUCTION

1. In its resolution on the report of the Commission on the work of its fourteenth session, the General Assembly reaffirmed the mandate of the Commission to co-ordinate legal activities in the field of international trade law in order to avoid duplication of efforts and waste of resources (resolution 36/32 of 13 November 1981, paragraph 5). The main activities undertaken for the purpose of co-ordination since the fourteenth session of the Commission are set forth below.

CO-ORDINATION OF ACTIVITIES

2. Co-ordination continued with the International Institute for the Unification of Private Law (UNIDROIT) on the work undertaken by UNIDROIT for the preparation of a draft Uniform Law on Agency of an International Character in the International Sale of Goods. A session of a committee of governmental experts was convened by UNIDROIT (Rome, 2 to 13 November 1981) to revise the draft Law, and UNIDROIT invited all member States of the Commission which were not members of UNIDROIT to attend this session on an equal footing with the member States of UNIDROIT.¹ The scope of application of the draft Law prepared at that session is aligned to that of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). Furthermore, the draft Law deals mainly with the relationship between an agent and a third party and a principal and a third party. The Government of Switzerland has agreed to be the host to a Diplomatic Conference (Geneva, 31 January to 18 February 1983) to adopt a convention on the subject.

3. The Secretariat is collaborating with UNIDROIT in regard to the work of UNIDROIT on the liability of international terminal operators, and there is a possibility of a later co-ordination with the Commission on this subject in the light of its connection with the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg).²

4. Co-ordination continued with the International Chamber of Commerce (ICC) on the revision of the ICC Uniform Customs and Practice for Documentary Credits. It may be recalled that, as part of this co-ordination, a questionnaire of the ICC on the revision was circulated by the Secretary-General to all Governments. The Secretariat attended sessions of the ICC Working Party on the Revision of the Uniform Customs and Practice for Documentary Credits, and of the ICC Commission on Banking Technique and Practice.³ The consideration of stand-by letters of credit, which was referred by the Commission to the ICC, was also carried forward in the context of the revision of the Uniform Customs and Practice.

5. The ICC Commission on International Contract Practice is currently examining the relationship between the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) and the ICC INCOTERMS. The Secretariat is collaborating with the ICC to harmonize the application of these two attempts at unification.

6. Co-ordination continued with the Hague Conference on Private International Law (the Hague Conference) on the revision of the 1955 Hague Convention on the Law Applicable to International Sales of Goods. The Hague Conference will convene a session of the Special Commission (The Hague, 6 to 15 December 1982) to consider the preparatory work for the revision in the light of the adoption

* 17 June 1982.

¹ This invitation was welcomed by the General Assembly: resolution 36/32 of 13 November 1981, para. 5 (f).

² See A/CN.9/225 (reproduced in this volume, part two, VI, B).

³ See A/CN.9/229 (reproduced in this volume, part two, VI, C).

of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). The Hague Conference will invite all member States of the Commission who are not members of the Hague Conference to that session.⁴

7. As a result of the mandate given to the Commission by General Assembly resolution 34/142 of 17 December 1979 on co-ordination of work in the field of international trade law, the Secretariat of the Economic Commission for Europe requested assistance from the Commission or its Secretariat in relation to work undertaken by the Group of Experts No. 1: Data Elements and Automatic Data Interchange of the ECE Working Party on the Facilitation of International Trade Procedures on the coding of terms of payment in international sales ("PAYTERMS"). In view of the advanced stage of work within the Group of Experts it appeared that only assistance by the Secretariat was feasible. The Secretariat made extensive comments and suggestions on the draft coding made by the Group of Experts (TRADE/WP.4/R.102), and these suggestions were discussed at a meeting of the Group of Experts held in Vienna (19 to 20 November 1981), which was also attended by experts from interested facilitation bodies, and the UNCITRAL and UNCTAD/FALPRO Secretariats. The text of "PAYTERMS" agreed at that meeting is contained in document TRADE/WP.4/R.160. The final text will be issued as Recommendation No. 17 of the ECE Working Party.

8. The ECE Working Party on the Facilitation of International Trade Procedures is also considering problems arising from the use of general conditions of contract. The Secretariat has suggested that work should be undertaken by the Working Party to align the ECE General Conditions with the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980).⁵

9. Co-ordination is being developed with the United Nations Industrial Development Organization (UNIDO) in related fields of activity, and informal contacts continue between the Secretariats of the Commission and of UNIDO. The Secretariat was invited to participate in a Working Group meeting organized by UNIDO on Long-term Contracts of Purchase/Supply of Iron Ore and Coking Coal (Bratislava, 16 to 18 March 1982).⁶ It is proposed to invite UNIDO to comment on draft chapters of the legal guide on works contracts when they are prepared by the Secretariat.

10. Discussions are being held at Secretariat level with the Centre for Transnational Corporations on assistance the Centre might be able to give towards the preparation of the legal guide on works contracts.

11. As regards the project to be undertaken in the field of electronic funds transfer⁷ it is proposed to collaborate

with the Bank for International Settlements, Basle, the Secretariat of the Council of Europe, and with such other international organizations as are interested in the project.

12. The work on the establishment of a universal unit of account for international conventions has proceeded with the collaboration of the International Monetary Fund. Co-ordination is also being arranged with the International Law Association (ILA) in the establishment of a unit of account and in other areas related to the work of the Commission. The International Monetary Law Committee of the ILA has for the past ten years been engaged in work directed to the establishment of a universal unit of account. At the 60th Conference of the International Law Association (Montreal, 29 August to 4 September 1982) the Secretariat proposes to enlist support for the recommendation to be made in this field by the Commission at its fifteenth session. Support will also be enlisted for the work of the Commission in the field of international commercial arbitration.

13. Promotion of the UNCITRAL Arbitration Rules is being undertaken in collaboration with the International Council for Commercial Arbitration, the Kuala Lumpur Regional Arbitration Centre, and other interested arbitral institutions. The Kuala Lumpur Regional Arbitration Centre and the Tokyo Maritime Arbitration Commission have reached an agreement for co-operation in the field of maritime arbitration with effect from 23 April 1982. The Secretariat co-operated in the drafting of this agreement.

14. The UNCTAD Secretariat has placed before the tenth session of the UNCTAD Committee on Shipping (Geneva, 14 June 1982) the current status of the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) with a request that the Committee consider what action it might take to facilitate the early coming into force of the Convention (TD/B/C.4/249). The Secretariat intends to consult with the UNCTAD Secretariat in promoting the wider acceptance of this Convention.

15. Further collaboration is envisaged with the Asian-African Legal Consultative Committee, the Council for Mutual Economic Assistance and the Organization of American States and other bodies on training and assistance in the field of international trade law.⁸

16. In General Assembly resolution 36/107 of 10 December 1981 the Commission was requested to submit relevant information to, and to co-operate fully with, the United Nations Institute for Training and Research (UNITAR) in its study on the progressive development of the principles and norms of international law relating to the new international economic order. Information on relevant activities of the Commission supplied by the Secretariat is reflected in document A/36/143. The Secretariat has again recently consulted with the UNITAR Secretariat on this subject, and will continue to co-operate with UNITAR by supplying information concerning the activities of UNCITRAL.

⁴ This proposed invitation was welcomed by the General Assembly; resolution 36/32 of 13 November 1981, para. 5 (e).

⁵ The text of the letter from the Secretary of the Commission is contained in TRADE/WP.4/R.179.

⁶ The report of this meeting is contained in ID/WG.360/4.

⁷ See A/CN.9/221 (reproduced in this volume, part two, II, C).

⁸ See A/CN.9/228 (reproduced in this volume, part two, VIII).

**B. Report of the Secretary-General: international transport documents
(A/CN.9/225* and Corr. 1 – French only)**

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INTRODUCTION

1. The Commission, at its fourteenth session, decided that, to further strengthen the co-ordinating role of the Commission, the Secretariat should select a particular area of international trade law for consideration and submit a report on the work of other organizations in that area.¹ The subject of international transport documents has been chosen for the fifteenth session in response to the decision of the Commission. Because of the developments in transport and data communication technology, the manner in which transport documents are prepared and issued is changing rapidly with consequent effects on the governing legal regime.

2. In the past, each mode of transport was independent of the others. If the goods had to move by several different modes from the point of origin to the ultimate destination, each portion of the total journey was treated as a separate journey to be governed by its own legal regime. These legal regimes were established by national law, by bilateral agreements where trade between two adjoining States was involved, or by multilateral agreements where many States were affected.

3. The multilateral agreements, with which this report is concerned, can be divided into two major groups. There

are world-wide agreements covering two major forms of transportation, sea and air. The acceptance of these conventions is so extensive that for all practical purposes they establish the documentary requirements for all international transport carried by them. Land-based transport is by its nature a regional affair. The only major multilateral international agreements governing rail or road transport are in Europe with, in the case of rail transport, extensions into Asia and North Africa.

4. All of these conventions have two basic purposes. They establish the responsibility of the carrier to the shipper for loss or damage to the goods. They also establish the requirements as to the transport document to be issued in connection with the carriage of the goods. Although the main lines of these conventions are similar, reflecting the similarity of problems to be considered in the carriage of goods by any mode of transport, the fact that each form of transportation was considered to be independent of the others and in large measure served a different market led to a separate evolution of the information to be contained in the transport document and the significance of the document as a means of controlling the goods.

5. This situation, which basically continues today, has been disturbed by a number of developments, of which four deserve mention here. The first is the use of unitizing devices, and especially of containers, to consolidate break-bulk cargo. In order to obtain maximum benefit from the use of a container, cargo is consolidated as close as possible to the place of origin of the goods and delivered to a container yard as

* 16 July 1982.

¹ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 100 (Yearbook ... 1981, part one, A).

close as possible to the ultimate destination before the container is opened. What previously had been a series of separate journeys has become — from the point of view of the shipper at any rate — one continuous journey over several modes of transport. Mechanisms have had to be found to issue documents satisfactory to the commercial parties in this situation.

6. A second development arising out of the use of containers is that in certain trades the turn-around time from the loading of a ship in one port to the unloading of it in another has been shortened to such an extent that the goods often are ready for delivery before the bill of lading has arrived authorizing release of the goods. The resulting terminal delay adds extra costs and reduces the value of containerization. There have been similar, though not identical, problems with clearing air freight out of the airport of destination.

7. A third development to affect the documentary requirements has been the trade facilitation movement. A series of studies had shown that a single shipment of goods might require the seller to create as many as 40 separate documents for a domestic trade transaction and over 100 for an international trade transaction. Other studies had shown that the cost of documentation for international sales ran about 7 per cent of the selling price of the goods.² The purpose of the trade facilitation movement has been to reduce this cost by reducing the number of required documents and to simplify the preparation of those documents which remain. The central organ for international trade facilitation is the Working Party on Facilitation of International Trade Procedures, a joint effort of the Economic Commission for Europe (ECE) and of UNCTAD.³

8. The first major accomplishment of the trade facilitation effort was the publication in 1963 of a basic standard for the layout of information that is repeated on most of the forms needed to initiate and complete an international trade transaction. In 1973 the standard was formally recommended by the Working Party as the ECE Layout Key for Trade Documents. It was re-named in 1978 as United Nations Layout Key for Trade Documents.⁴

9. The development of the United Nations Layout Key is having a profound effect on the documentation aspects of international trade. As various national and international organizations have aligned their documents on the Layout Key, it has become possible for the seller-shipper to type the basic information on a master copy or into automatic data processing equipment and from that single typing to produce a series of documents needed for the sale and

shipment of the goods. The un-needed data for any given document is blocked out through masking or similar devices. These techniques of document production permit a significant saving in the cost of producing the documents and reduce the number of possible clerical errors. Moreover, any clerical errors which are made are reproduced systematically throughout all the documents produced from the master. Rather than increasing difficulties, a consistent error is easier to find and to correct than is a haphazard error.

10. A fourth development is the use of computers for the preparation of transport documents and telecommunications for their transmission. This development goes hand in hand with the trade facilitation movement since the full benefits of neither computers nor telecommunications can be realized without the standardization of the data required for different purposes and standardization of the format for entry of the data. This pressure for standardization is accentuated when the information is sent by telecommunications since, in an effort to reduce transmission costs, as much data as possible is sent by code. For example, it would be impractical to send in full by telecommunications the standard conditions of carriage now found on the back of most transport documents. It would be cheaper to refer to them by a single word or, better yet, a single letter or number in the appropriate location.

I. THE LEGAL REGIME

A. Existing multilateral conventions

11. There follows below a chart showing the major transportation conventions in force, awaiting ratification or in draft which govern the documentary requirements. Those protocols to the existing conventions which do not affect the documentary requirements are not listed.

Mode of transport	Name of convention	Date of adoption/ Date in force	Preparing organization	Geographical coverage
Sea	International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading (Hague Rules)	25 August 1924/2 June 1931	Comité Maritime International	World-wide
Sea	United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules)*	31 March 1978/not yet in force	United Nations Commission on International Trade Law (UNCITRAL)	World-wide

² Cited in E. du Pontavice, "L'informatique et les documents du commerce extérieur", *Revue de jurisprudence commerciale*, special issue (November 1979), pp. 435 and 445-446.

³ See Facts about the Working Party on Facilitation of International Trade Procedures, TRADE/WP.4/INF.68, TD/B/FAL/INF.68.

⁴ The United Nations Layout Key for Trade Documents with explanatory material is contained in document ECE/TRADE/137 (United Nations publication, Sales No. E.81.II.E.19).

* Yearbook . . . 1978, part three, I, B.

Mode of transport	Name of convention	Date of adoption/ Date in force	Preparing organization	Geographical coverage
Air	Convention for the Unification of Certain Rules Relating to International Carriage by Air (Warsaw Convention)	12 October 1929/13 February 1933	Comité international technique d'experts juridiques aériens, absorbed by International Civil Aviation Organization	World-wide
Air	Hague Protocol	28 September 1955/ 1 August 1963	ICAO	World-wide
Air	Montreal Protocol No. 4	25 September 1975/ not yet in force	ICAO	World-wide
Rail	International Convention Concerning the Carriage of Goods by Rail (CIM)	7 February 1970/ 1 January 1975	Central Office for International Railway Transport (Berne)	Europe, North Africa, Western Asia
Rail	Convention Concerning International Transport by Rail (COTIF) Appendix B (CIM)	9 May 1980/ not yet in force	Central Office for International Railway Transport (Berne)	Europe, North Africa, Western Asia
Rail	Agreement Concerning the International Carriage of Goods by Rail (SMGS)	1 November 1951/current revision in force since 1 July 1966	Organization for the Collaboration of Railways	Eastern Europe, East Asia
Road	Convention on the Contract for the International Carriage of Goods by Road (CMR)	19 May 1956/ 2 July 1961	Economic Commission for Europe	Europe
Multi-modal	United Nations Convention on International Multimodal Transport of Goods (Multimodal)	24 May 1980/ not yet in force	United Nations Conference on Trade and Development (UNCTAD)	World-wide
Inland waterways	Draft Convention on the Contract for the Carriage of Goods by Inland Waterways (CMN)	Draft of 1973	International Institute for the Unification of Private Law, Economic Commission for Europe	Europe
Terminal operations	Preliminary draft Convention on the Liability of International Terminal Operators (ITO)	Draft of October 1981	International Institute for the Unification of Private Law	World-wide

12. *Sea.* The Hamburg Rules* are intended to replace the Hague Rules. Although the Hamburg Rules have more detailed provisions governing the bill of lading and accommodate the use of non-negotiable transport documents better than do the Hague Rules, they contain no fundamental changes in the law governing the documentary aspects of the carriage of goods by sea.

13. *Air.* The Hague Protocol of 1955 amended, *inter alia*, article 8 of the Warsaw Convention by reducing the number of items of required information on an air consignment note. Since several countries have not ratified the Hague Protocol, any uniform air consignment note must be based upon the requirements of the original Warsaw Convention as well as the less extensive requirements of the Protocol.

14. Article 8 of the Convention as amended by the Hague Protocol would in turn be amended, though in a minor way, by Montreal Protocol No. 4 of 1975. More importantly, article 5 of the Convention would be amended by this Protocol to permit the use of computer communication technology in place of a paper air consignment note.

15. *Rail.* The 1980 COTIF will replace the 1970 CIM concerning the carriage of goods by rail as well as the 1970 CIV concerning the carriage of passengers and luggage by rail. The 1970 CIM currently in force is the eighth version of the original CIM which came into force in 1893. Based upon past experience the 1980 version could be expected to come into force about 1985. In contrast to the earlier versions of CIM, which were separate conventions, the CIM provisions in the 1980 COTIF are contained in an annex to the main convention.

16. The original text of SMGS of 1951 was similar in structure and content to the CIM. However, the differences between the two texts have increased as each has been revised since that time.

17. Several countries in Eastern Europe are parties to both the CIM and SMGS. This has greatly facilitated through traffic between those States which are parties to only one or the other agreement. It has not, however, prevented divergence in the texts of the two conventions.

18. *Multimodal.* The documentary provisions of the Multimodal Convention are modelled on those of the Hamburg Rules. At its tenth session in June 1982, the UNCTAD Committee on Shipping, which sponsored the Multimodal Convention, requested the Secretary-General of UNCTAD to bring the Hamburg Rules to the attention of those member States that had not yet become Contracting Parties and to suggest the desirability of bringing it into force at an early date.⁵

19. The International Chamber of Commerce has published rules for a Combined Transport Document.⁶

* Yearbook . . . 1978, part three, I, B.

⁵ The draft resolution as adopted by the Committee is found in TD/B/C.4/L.162.

⁶ ICC Publication No. 298.

Although these rules have no binding force, several organizations which have prepared model combined (multimodal) transport documents have secured the endorsement of the ICC that the form in question conformed to the ICC rules, thereby introducing a degree of uniformity into the nature of the document.

20. The acceptability of combined transport documents is also affected by their acceptability as a transport document for purposes of a letter of credit under the Uniform Customs and Practice for Documentary Credits (UCP).⁷

21. *Inland waterways.* UNIDROIT is considering a fully revised version of the draft of CMN. The Governing Council was informed at its 61st session in April 1982 that some progress had been made in resolving differences of opinion among the Rhine States regarding the exoneration of the carrier for fault in the navigation of the vessel, but it was not clear whether final agreement seemed likely.⁸

22. *Terminal operators.* A preliminary draft Convention was approved by the UNIDROIT Study Group on the Warehousing Contract at its third session in October 1981. It was reported to the 61st session of the UNIDROIT Governing Council in April 1982 that some opposition to the draft had been voiced by certain terminal operators who saw it as an invasion of their contractual freedom.⁹

23. The Governing Council requested the Secretariat to give wide publicity to the draft rules so as to bring criticisms out into the open where any misconceptions could be dispelled and legitimate concerns taken into account.¹⁰

B. Documentary regime under the conventions

1. Requirement to issue a document

(a) Paper document

24. All of the conventions under consideration require the issue of a transport document or provide that a transport document can be required by either the shipper or the carrier.

25. The conventions governing the two forms of land-based transport, rail and road, require the issue of a con-

signment note and prescribe its contents in some detail.¹¹ The Multimodal Convention requires the multimodal transport operator to issue a multimodal transport document, but the convention permits the document to be either negotiable or non-negotiable.¹² Similarly, the draft CMN would require that either a bill of lading or a consignment note be issued for carriage on inland waterways.¹³ The bill of lading could be in nominative form, or to order or to bearer.

26. The Warsaw Convention gives both the air carrier and the consignor the right to require the issue of a consignment note, and assures that the air carrier will do so by withdrawing the benefits of provisions which exclude or limit its liability if a consignment note is not issued containing certain data.¹⁴ This rule is continued under the Hague Protocol of 1955.

27. Under Montreal Protocol No. 4 the issue of a transport document, now called an air waybill, would be required by the Convention. However, failure to do so would not affect the carrier's liability under the Convention.¹⁵

28. Both the Hague Rules and the Hamburg Rules allow the shipper to require the carrier to issue a bill of lading once the carrier has received the goods into his charge.¹⁶ Furthermore, once the goods are loaded on board, the shipper has the right to have a "shipped" bill of lading, which may be in the form of a notation on the bill of lading already issued indicating the name or names of the ship or ships upon which the goods have been loaded and the date or dates of loading.¹⁷

29. Neither the Hague Rules nor the Hamburg Rules* require that a bill of lading be issued if the shipper does not require one. However, the liability regime of the Hague Rules, including the exonerations from liability and the limits of liability, applies only if there has been a contract of carriage "covered by a bill of lading or any similar document of title."¹⁸ The Hamburg Rules on liability on the other hand apply to "any contract whereby the carrier undertakes against payment of freight to carry goods by

* Yearbook ... 1978, part three, I, B.

¹¹ CIM 1970, art. 8; CIM 1980, art. 11, SMGS, art. 6; CMR, art. 4. The CMR goes on to provide that "The absence, irregularity or loss of the consignment note shall not affect the existence or the validity of the contract of carriage which shall remain subject to the provisions of this Convention."

¹² Art. 5 (1).

¹³ Art. 3 (1). The draft CMN contains the same provision as does the CMR quoted in note 11 as to the absence, irregularity or loss of the transport document.

¹⁴ Arts. 5 (1) and 9. The Warsaw Convention contains in art. 5 (2) the same provision as does the CMR quoted in note 11 as to the absence, loss or irregularity of the air consignment note.

¹⁵ Arts. 5 (1) and 9 of the Convention as amended by Montreal Protocol No. 4.

¹⁶ Hague Rules, art. 3 (3); Hamburg Rules, 14 (1) (Yearbook ... 1978, part three, I, B).

¹⁷ Hague Rules, art. 3 (7); Hamburg Rules, 15 (2) (Yearbook ... 1978, part three, I, B).

¹⁸ Art. 1 (b). See also art. 2. For the possibility of incorporating the liability regime of the Hague Rules into the contract of carriage by a clause on a sea waybill, see para. 70 below.

⁷ The current (1974) version of the UCP is found in ICC Publication No. 290. For discussion of the progress made in revising the UCP, see A/CN.9/229, and of its effect on transport documents, paras. 71, 72 and 80 below.

⁸ Report of the 61st session of the Governing Council (15 and 16 April 1982), UNIDROIT 1982 C.D. 61st session, agenda item 5 (f).

⁹ *Ibid.*, agenda item 5 (h).

¹⁰ The Council was informed by the Secretary of the United Nations Commission on International Trade Law (UNCITRAL) of the interest of the Commission in the subject, which might perhaps at some time in the future be translated into positive action, given its close relationship with the international conventions relating to the carriage of goods and in particular the Hamburg Rules, as well as its relevance to the needs of a number of developing countries.

sea from one port to another."¹⁹ Therefore, while the right of the shipper to demand a bill of lading remains the same under the Hamburg Rules* as it is under the Hague Rules, the Hamburg Rules* are more open to the use of sea waybills and other forms of non-negotiable transport documents or to paperless documentation techniques.

30. The draft ITO is the least demanding of all the texts under consideration in that it would require that a document be issued only if requested by the customer, and it is not anticipated that one would be issued in all cases.²⁰

(b) *Issuance of paper document by automatic data processing*

31. The Multimodal Convention permits the multimodal transport operator, if the consignor so agrees, to preserve a record of the data required under the convention by making use of any mechanical or other means, e.g. a computer. In such a case the consignor must be furnished a readable document, in non-negotiable form, which document is deemed to be the multimodal transport document.²¹

32. The draft ITO provides that nothing contained therein prevents the issuing of documents by any mechanical or electronic means, if not inconsistent with the law of the country where the document is issued.²²

(c) *Issuance of transport document at destination*

33. It has long been technically possible to issue the necessary transport documents at destination by wiring the relevant information to the carrier or its agent at the destination.²³ With the standardization of the data entries on transport documents and with the development of computer telecommunication networks, direct production of the documents at destination is now feasible.

34. Issue of the transport document at destination is not permitted by the CIM and SMGS for rail, CMR for road or the Warsaw Convention for air, all of which require a copy of the consignment note to travel with the goods.²⁴

* Yearbook . . . 1978, part three, I, B.

¹⁹ Art. 1 (6). See also art. 2 (Yearbook . . . 1978, part three, I, B).

²⁰ UNIDROIT 1982, study XLIV, doc. 14, art. 4.

²¹ Art. 5 (4).

²² Art. 4 (4).

²³ At least as early as the 1958 edition of the Uniform Commercial Code of the United States of America, sec. 7-305 authorized the carrier at the request of the consignor to issue the transport document at destination.

²⁴ CIM 1970, art. 16 (1); CIM 1980, art. 28; SMGS, art. 6 (1); CMR, art. 5 (2); Warsaw Convention, art. 6 (2). Under Montreal Protocol No. 4 the second original must be marked "for the consignee", but the Convention would no longer specifically require that it travel with the goods or be handed over to the consignee. Under resolution 600k of the International Air Transport Association when teletype or other electronic means are used to transmit an air waybill for international carriage, a paper waybill must first be made. Whenever a consignment is transferred to a subsequent carrier, the second original for the consignee and copies of the transmittable air waybill must be provided to the subsequent carrier.

35. Since neither the Hague Rules nor the Hamburg Rules* require the issue of any transport document, there appears to be no obligation on the carrier as to the place of issue under these rules. If the carrier and shipper agreed, either a sea waybill or bill of lading could be issued by the carrier at the destination. The same result would appear to be possible under the Multimodal Convention and the draft CMN.

(d) *Substitution for paper document*

36. Under Montreal Protocol No. 4 in place of the paper air waybill the carrier could substitute "any other means which would preserve a record of the carriage to be performed".²⁵ In that case the shipper must be furnished a paper receipt for the goods.

37. Under the draft CMN electrical or automatic means of recording the transaction may be used.²⁶ In contrast to Montreal Protocol No. 4, no paper receipt is required.

38. Since neither the Hague Rules nor the Hamburg Rules* require the issue of a transport document unless the shipper requests a bill of lading, neither convention precludes the use of paperless documentation techniques.

2. *Control of the goods through the document*

39. One of the traditional functions of an ocean bill of lading is to serve as a document of title whereby the possessor of the bill of lading has symbolic possession of the goods. This function is effectuated by the rule that the carrier can hand over the goods only against surrender of the bill of lading. This rule is assumed, but not stated, in the Hague Rules. It is specifically stated in the Hamburg Rules, the draft CMN and the Multimodal Convention.²⁷

40. The draft ITO would allow for the same result by providing that:

"The document issued by the ITO may, if the parties so agree, and the applicable law so permits, contain an undertaking by the ITO to deliver the goods against surrender of the document".²⁸

41. The conventions which specifically mention a consignment note as the only transport document also provide a mechanism for the shipper to order the carrier not to hand over the goods to the consignee. Under the Warsaw Convention the consignment note must be made out in three originals. The third original is given to the shipper.²⁹ Until the goods arrive at the place of destination, the shipper can exercise the right of disposition over the

* Yearbook . . . 1978, part three, I, B.

²⁵ Art. 5 (2) of the Convention as modified by the Protocol.

²⁶ Art. 3 (5).

²⁷ Hamburg Rules, art. 1 (7) (Yearbook . . . 1978, part three, I, B); draft CMN, art. 4 (1); Multimodal, art. 6 (2).

²⁸ Art. 4 (4).

²⁹ Art. 6.

goods upon surrender to the carrier of the third original of the consignment note.³⁰ The rule is essentially the same for goods carried by road under the CMR, except that the copy to be given to the shipper and which is to be surrendered to the carrier in case of any stoppage in transit is the first original.³¹ For rail carriage under either the CIM or the SMGS, any diversion of the goods by the shipper must be noted on the duplicate of the consignment note.³² Therefore, the consignor loses his right of disposition of the goods once he has given over his "original" or duplicate of the consignment note to the consignee or to a bank under a documentary credit.

42. The Multimodal Convention states that if the goods are carried under a non-negotiable multimodal transport document, the multimodal transport operator is discharged from his obligation to deliver the goods if he makes delivery to the consignee "or to such other person as he may be duly instructed, as a rule, in writing".³³ Since the consignor's right to order the multimodal transport operator to deliver the goods to a person other than the consignee is not based upon possession of a copy of the non-negotiable document, the Convention appears to offer no means of precluding the consignor from exercising a right of disposition over the goods until the goods have been delivered. The same conclusion would seem to apply to a shipment under a sea waybill since neither the Hague Rules nor the Hamburg Rules* govern the documentary aspects of such a shipment.

43. The draft CMN provides that the carrier can deliver only to the person designated on the bill of lading if it is issued in nominative form.³⁴ The draft provides no rule as to the right of the shipper to control the goods if the carriage is under a consignment note.

3. Data requirements

44. In order for the transport document to fulfil its various functions, it must contain a certain amount of data. Much of this data is the same no matter what the means of carriage. In fact, much of it is the same data as is needed on other documents concerned with the sale and shipment of the goods. However, each of the conventions prescribes a certain number of data elements which must appear on the particular transport document.

45. The minimum number of data elements required by any convention is three by the Hague Rules and by the Hague Protocol and Montreal Protocol No. 4 to the Warsaw Convention.³⁵ The maximum number of required data

elements is seventeen in the original Warsaw Convention followed by fifteen for the Hamburg Rules and the Multimodal Convention.³⁶

46. There is no discernible trend towards either increasing or decreasing the number of required data elements. The 1955 Hague Protocol reduced the number of required data elements from the original seventeen of the Warsaw Convention to three. This decision was confirmed by the 1975 Montreal Protocol No.4, although one of the required data elements is different from that in the Hague Protocol. On the other hand the Hamburg Rules* in 1978 increased the required number of data elements from the three contained in the Hague Rules to fifteen. This was followed by the Multimodal Convention in 1980.

4. Requirement of a signature

47. Most, but not all, of the conventions require that the transport document be signed by the shipper or the

Convention	Signature required		Permitted form			Law of place of issue relevant of Article of Convention
	Shipper	Carrier	Stamped	Printed	Other means	
Hague Rules	No	No				
Hamburg Rules*	No	Yes	Yes	Yes	Yes ^a	Yes ^a 14
Warsaw Convention	Yes	Yes	Yes	Yes-shipper	No	No 6
Hague Protocol	Yes	Yes	Yes	Yes-shipper	No	No 6
Montreal Protocol No. 4	Yes	Yes	Yes	Yes	No	No 6
CIM-1970	Yes ^b	Yes ^c	Yes	Yes-shipper	No	Yes ^b 6, 8
CIM-1980	Yes ^b	Yes ^c	Yes	Yes-shipper	No	Yes ^b 13, 11
SMGS	Yes	Yes ^c	Yes	Yes-shipper	No	No 6, 7
CMR	Yes	Yes	Yes ^d	Yes ^d	No	Yes ^d 5
Multimodal	No	Yes	Yes	Yes	Yes ^a	Yes ^a 5
Draft CMN	Yes	Yes	Yes	Yes	Yes ^e	Yes ^e 6
Draft ITO	No	No				

^a "The signature on the [bill of lading] [multimodal transport document] may be in handwriting, printed in facsimile, perforated, stamped, in symbols, or made by any other mechanical or electronic means, if not inconsistent with the law of the country where the [bill of lading] [multimodal transport document] is issued."

^b "If the laws and regulations in force at the forwarding station so require, the sender shall add to his name and address, his written, printed or stamped signature."

^c Neither the CIM nor the SMGS requires the carrier's "signature". However, both require the carrier to affix its stamp to the consignment note.

^d "These signatures may be printed or replaced by the stamps of the sender and the carrier if the law of the country in which the consignment note has been made out so permits."

^e The rule is similar to that in note d with the addition that any other mark of authenticity may also be used if permitted by the law of the country of issue.

³⁶ Warsaw Convention, art. 8; Hamburg Rules, art. 15 (Yearbook ... 1978, part three, I, B); Multimodal Convention, art. 8.

* Yearbook 1978, part three, I, B.

* Yearbook ... 1978, part three, I, B.

³⁰ Arts. 12 and 13.

³¹ Art. 12 (5).

³² CIM 1970, art. 21 (2); CIM 1980, art. 30 (2); SMGS, art. 19

³³ Art. 7 (2).

³⁴ Art. 4 (1). The draft also gives specific rules for bills of lading in order or bearer form.

³⁵ Hague Rules, art. 3 (3); Hague Protocol and Montreal Protocol No. 4, art. 8 of the Warsaw Convention as modified. The data elements required by the two protocols are not completely identical.

carrier, or both. All of the conventions which require a signature permit the signature to be applied in some mechanical way.

48. The ECE/UNCTAD Working Party on Facilitation of International Trade Procedures has recommended

"to Governments and international organizations responsible for relevant intergovernmental agreements to study national and international texts which embody requirements for signature on documents needed in international trade and to give consideration to amending such provisions, where necessary, so that the information which the documents contain may be prepared and transmitted by electronic or other automatic means of data transfer, and the requirement of a signature may be met by authentication guaranteed by the means used in the transmission".³⁷

C. Organizations which prepare transport document forms

49. Under some transport conventions it is considered important that all carriers use a transport document with a uniform format. In these cases one organization may be charged with designing the required document. Where such uniformity is not as highly regarded, the carriers may be free to design their own documents, so long as they contain the information required by the convention.

50. The rail consignment note for use under SMGS is prescribed by the States as an annex to the Convention. The form of the note has been recently revised and it is now aligned to the United Nations Layout Key.

51. Until the 1970 version of CIM came into force in 1975, the railway consignment note under that Convention was also contained in an annex to the Convention. Under the 1970 version of CIM the railways have the authority to prescribe a model consignment note.³⁸ The proposed model note must be communicated to the Central Office for International Railway Transport (Berne) which communicates it to the Contracting States. If no State has objected within one month, the proposal goes into effect. If there is an objection, the Central Office tries to resolve the differences. Under the 1980 CIM annexed to COTIF, expected to come into force about 1985, the railways will have full authority to establish a model consignment note without governmental approval.³⁹ The reform of the railway consignment note under CIM has been undertaken by the

International Rail Transport Committee (CIT). The railway consignment note for use under CIM has been aligned to the United Nations Layout Key since 1969.

52. None of the other conventions prescribe either the organization charged with designing the document or that the document in use must be uniform in format. Nevertheless, the desirability of using documents which are uniform in format has led to the design of model transport documents by different organizations.

53. The International Air Transport Association (IATA) has designed an air consignment note which is mandatory for use by IATA members and is widely used by non-members. A new Universal Air Waybill/Consignment Note which is closely aligned to the United Nations Layout Key has been adopted for optional use as from 1 April 1982 and mandatory use as from 1 January 1984.⁴⁰

54. A CMR consignment note which is aligned to the United Nations Layout Key has been designed by the International Road Transport Union (IRU) and is in general use. Other organizations, such as the Simplification of International Trade Procedures Board (SITPRO) in the United Kingdom, have also designed CMR consignment notes which are in use. The SITPRO CMR consignment note is also aligned to the United Nations Layout Key.

55. There is not the same degree of standardization of the transport documents for carriage of goods by sea that is found in other forms of transport. The tradition that each carrier had its own form of bills of lading, and often different forms for different commodities or routes, has persisted to this day. Similarly, as new transport documents have been developed in the nature of sea waybills, they have often been individually designed by each carrier.

56. Nevertheless, some degree of standardization has been achieved. The model bill of lading proposed by the International Chamber of Shipping, which is aligned to the United Nations Layout Key, is widely followed. Various trade associations and shipping conferences have proposed model shipping documents of various kinds. These models often follow the format proposed by the International Chamber of Shipping.

57. The least uniform of all transport documents is undoubtedly the combined transport or multimodal document. Because of the diversity of situations which fall under the rubric of combined or multimodal transport, it is likely that uniformity of the document will not be achieved for some time, if at all. Nevertheless, combined transport documents aligned to the United Nations Layout Key have been adopted by such organizations as the Baltic International Maritime Conference (BIMCO), International Chamber of Shipping (ICS) and International Federation of Freight Associations (FIATA).

³⁷ Recommendation No. 14, TRADE/WP.4/INF.63, TD/B/FAL/INF.63.

³⁸ Art. 6 (1).

³⁹ Art. 12 (2). See also, E. Bertherin, "La réforme de la lettre de voiture internationale", 88 *Bulletin des transports internationaux par chemins de fer* 47 (1980).

⁴⁰ IATA Resolution 600j (III).

II. SOME CURRENT DEVELOPMENTS

A. Blank-back, short-form and shipper-supplied documents

58. Transport documents are often designed as multi-leaf forms with carbon inserts which permit the shipper to fill out all originals and copies by a single typing. The originals usually carry on the reverse side the general conditions of carriage of the carrier.

59. The development of series of forms for international trade transaction which are aligned to the United Nations Layout Key for Trade Documents has made possible the use of modern reprographic one-run methods of document preparation for all of the documents necessary for the sale and shipment of the goods. However, the document preparation equipment often does not accommodate multi-leaf forms and in some cases requires the use of continuous feed paper which must, therefore, have no printing on the reverse side.

60. Even where this is not the case it would be simpler for the shipper if he were permitted to use a standard form for any given mode of transport which could be used with any carrier.

61. To accommodate such shipper-supplied forms or blank-back documents the ECE/UNCTAD Working Party on Facilitation of International Trade Procedures has recommended that the following clause should be used on the face of the document:

"The terms of the transport operator's/carrier's standard conditions of carriage (including those relating to pre-carriage and on-carriage) and tariff applicable on the date of taking charge of the goods for transportation are incorporated herein as well as any international convention or national law which is compulsorily applicable to the contract evidenced in this document.

"A copy of the transport operator's/carrier's standard conditions of carriage applicable hereto may be inspected or will be supplied on request at the office of the transport operator/carrier or their principal agents".⁴¹

62. The extent to which the courts in various countries will accept such a general incorporation clause depends on the attitude of the legal system towards contracts of adhesion and the use of general conditions as well as the text of the individual carrier's standard conditions of carriage and the availability of that text to the shippers who are to be made subject to its terms.⁴²

63. Blank-back or short-form transport documents are acceptable for documentary credits issued under the Uniform Customs and Practice for Documentary Credits.⁴³

B. Universal or multipurpose transport documents

64. The alignment of the various transport documents to the United Nations Layout Key has demonstrated that the data requirements for the carriage of goods by different modes of transport are similar. The development of blank-back and short-form transport documents with a clause similar to that suggested by the ECE/UNCTAD Working Party on Facilitation of International Trade Procedures has made it possible for the conditions of carriage of any carrier by any mode of transport to be incorporated into the transport document.

65. A Working Group of the Swedish Trade Procedures Council (SWEPRO) has combined these two features in a draft blank-back multipurpose transport document.⁴⁴ The document has been designed to replace the

Sea waybill, date freight receipt;
Bill of lading, waterways bill of lading, through bill of lading;
Combined transport document;
Rail consignment note;
Road consignment note;
Air waybill, house airbill;
FCT (forwarding agent's certificate of transport);
FCR (forwarding agent's certificate of receipt).

66. When the multipurpose transport document is to be used as a bill of lading, the two letters "BL" are to be typed in a specific box on the form. Although the report of the Working Group does not discuss the issue, it seems to be thought that this is a sufficient indication that "the carrier undertakes to deliver the goods against surrender of the document".⁴⁵

67. The draft multipurpose transport document has been used successfully in an experimental manner by several firms in Sweden. The report of the SWEPRO Working Group was issued in November 1981 in English and has been distributed widely so as to stimulate international understanding of the concept. As noted by SWEPRO "there is no point in starting local introduction in Sweden alone since this would become difficult without international understanding for this new idea".⁴⁶ Moreover, there may be difficulties in using the document with those modes of international transport, such as rail and air, in which a prescribed form is required for use by all carriers.⁴⁷

⁴³ Art. 19 (b) (ii).

⁴⁴ SWEPRO, *Multi-Purpose Transport Document (MPT)* (Göteborg, 1981), reprinted in TRADE/WP.4/R.165.

⁴⁵ Part of definition of a bill of lading in Hamburg Rules, art. 1 (7).

⁴⁶ SWEPRO News, No. 3, February 1982, p. 7.

⁴⁷ "The consignment note shall not be replaced by other documents or supplemented by documents other than those prescribed or allowed by this Convention or by the tariffs." CIM 1970, art. 6 (8). See also, CIM 1980, art. 13 (4).

⁴¹ Recommendation no. 12, para. 16, TRADE/WP.4/INF.61, TD/B/FAL/INF.61.

⁴² One observer has remarked that the case law on the validity of short-form and blank-back transport documents is confusing and difficult to interpret in a certain number of important maritime countries. E. du Pontavice, *op. cit.*, p. 441.

C. Sea waybill in place of bill of lading

68. The only transport documents which must be sent by the shipper separately from the goods are the bill of lading and the negotiable multimodal transport document. The special handling these documents require increases in costs for all parties. Moreover, the documents frequently arrive later than do the goods, causing port congestion with the associated costs.

69. In some trades it has been found that the majority of all shipments are made between customers of long standing or between different plants of a multinational group. In these cases a bill of lading serves no commercial function that would not be served as well by a non-negotiable transport document such as a sea waybill.

70. At the present time the major legal difficulty presented by the use of sea waybills in shipment between related parties lies with the liability regime of the Hague Rules which applies only if the carriage is covered by a bill of lading or similar document of title. Therefore, sea waybills frequently incorporate the Hague Rules into the contract of carriage. There is some doubt as to whether such an incorporation is effective.⁴⁸ The Hamburg Rules* obviate this legal question since they apply to "any contract whereby the carrier undertakes against payment of freight to carry goods by sea from one port to another".⁴⁹

71. Although sea waybills are most frequently used when the goods are not to be sold afloat and no documentary credit is to be issued, the cost advantages arising out of the simplification of documentary procedures when no bill of lading has been issued has led the ECE/UNCTAD Working Party on Facilitation of International Trade Procedures to recommend that:

"Carriers should always offer a non-negotiable transport document, bearing in mind that these can be utilized under documentary credits if stipulated by the applicant for the credit".⁵⁰

72. The current draft revision of the Uniform Customs and Practice for Documentary Credits accepts the use of non-negotiable sea waybills under documentary credits. Whereas the 1974 version of UCP referred extensively to marine bills of lading, the current draft refers to "transport documents".⁵¹ It is the responsibility of the applicant for the credit to specify any particular transport documents he may wish to require. It is also the responsibility of the bank which issues the credit to decide whether the transport documents specified in the application for the credit are sufficient for its purposes.

73. The concern which has been expressed over the use of sea waybills under documentary credits lies in the fact

that they do not assure the bank or the consignee that the goods will not be diverted by the consignor after he has received payment under the credit. An identical problem would arise where the transport documentation was in paperless form.

74. Several studies have been undertaken to develop approaches to this problem which would give the same legal assurance to the consignee and to the bank as would possession of a bill of lading but which would be administratively more efficient. The project which is the most advanced was sponsored by the Swedish Council for Transport Research. It has been put into experimental use as the ACL Cargo Key Receipt System.⁵² The System is a merger of the sea waybill and automatic data processing. It relies upon an in-house computer system operating between the ports of shipping and destination. The carrier furnishes the shipper with a print-out of the shipping data which it authenticates as the first copy. This print-out contains, *inter alia*, the following elements:

(a) The buyer's bank, which has opened the letter of credit, is named as the consignee;

(b) The shipper's declaration that he has irrevocably abrogated his right of disposal to the goods during the transit in favour of the consignee;

(c) The carrier's declaration that it holds the consignment specified on the receipt in security and as collateral for the bank named as consignee.

75. No other project appears to have reached the level of practical experimentation and use. However, one paperless transport documentation proposal which has been put forward for use with public data communication systems is the use of a public key crypto system whereby the data content of a computer message would, by means of the cryptology involved, authenticate the source and the content of the message.⁵³ This proposal would also rely on declarations similar to those contained in the ACL Cargo Key Receipt System.

76. Yet another approach which has been suggested is to rely upon a registration system. Under one proposal, the carrier would register in its computers any sales or security interests given in the goods.⁵⁴ Under another proposal which has been advanced for bulk cargoes, and especially for the tanker trade, the registry would be kept either in a central registry in a convenient location or by a bank.⁵⁵

⁵² K. Grönfors, *Cargo Key Receipt and Transport Document Replacement* (Göteborg, 1979); K. Grönfors, "The legal aspects and practical implications of non-documentary (paperless) cargo movement", *BIMCO Bulletin* (1981), p. 6180.

⁵³ R. Henriksen, *The Legal Aspects of Paperless International Trade and Transport* (Copenhagen, 1982).

⁵⁴ K. H. Reinskou, "Bills of lading and ADP: description of a computerized system for carriage of goods by sea", *Journal of Media Law and Practice*, No. 2 (1981), reprinted in *TRADE/WP.4/R.159*.

⁵⁵ P. Gram, Chairman, INTERTANKO Documentary Committee, *Delivery of Cargo without Presentation of Bills of Lading*, report dated 16 November 1980. Compare the suggestion made at the

* Yearbook... 1978, part three, I, B.

⁴⁸ See note 42 above.

⁴⁹ Art. 1 (6).

⁵⁰ Recommendation No. 18, Facilitation Measure 7.2, ECE/TRADE/141.

⁵¹ See para. 80 below.

D. *Legal value of computer records*

77. As paper records and documentation, including transport documents are increasingly replaced by records stored in computers, concern has been expressed as to the legal value of those records. In spite of the widespread use of computers in all fields of commercial activity, there remains a hesitancy in some countries to admit computer records as evidence before courts and arbitral tribunals. It is thought that the current state of techniques in the matter of recordings on computers does not give sufficient guarantees against falsification. In addition there are classical legal barriers concerning the use of such recordings as evidence, particularly in countries of common law tradition.

78. The report on electronic funds transfers submitted to the Commission at this session sets out a number of international actions which have been taken to facilitate the use of automatic data processing.⁵⁶ Several of those actions in the field of transport documents have already been noted above. The report also sets out international actions which have been taken in respect of the evidential value of computer records.

79. The report concludes that:

"Harmonized rules as to the conditions under which computer records must be produced to be admissible as evidence and the evidential value of computer records are necessary to give legal security to international electronic funds transfers. The problem, however, goes beyond electronic funds transfers and concerns all aspects of international trade in which computers might be used. Since rules of evidence are part of the procedural law, and are linked to the rest of the legal structure in a State, uniformity of law would be difficult to attain at present. However, if guidelines are established as to the conditions under which computer records are admitted in evidence, it may influence the legal development in this field".⁵⁷

E. *Documentary letters of credit*

80. One of the principal concerns of the International Chamber of Commerce in the current revision of the Uniform Customs and Practice for Documentary Credits is to adjust the rules to the changes in transport documentation which have occurred recently.⁵⁸ Four points are of particular interest in the context of this report:

(a) The new draft version of the UCP uses the term "transport documents" and mentions a particular form of transport document only in those rare cases when the intended

rule applies uniquely to that one document. This allows for a more uniform approach to documentary credits involving goods shipped by different modes of transport, by combined or multimodal transport, or under different types of documentation using the same mode of transport;

(b) Unless otherwise stipulated in the credit, banks will accept as originals documents produced or appearing to have been produced by data processing or photographic systems if, after their production, such documents have been marked as originals and signed or otherwise authenticated by their issuers. This will allow for the production of documents based upon a standard layout key, such as the United Nations Layout Key, using photographic or automatic data processing techniques;

(c) Unless a credit specifically calls for an on-board transport document, banks will accept a transport document which indicates that the goods have been taken in charge or received for shipment. This has always been the rule in regard to all means of transport other than carriage of goods by sea. With the advent of containerization and multimodal transport, it may not be feasible or necessary for an on-board document to be issued. However, the applicant for the credit/buyer of the goods will retain the right to require an on-board bill of lading under the credit and the shipper/seller of the goods retains the right to require such a document from the carrier under both the Hague Rules and the Hamburg Rules;

(d) The rules in respect of trans-shipment have been expanded to reflect the nature of combined and multimodal transport.

CONCLUSION

81. The law and practices in regard to international transport documents are changing rapidly. The distinctions between the different modes of transport of goods and the needs of the shippers and banks, as well as the carriers, in respect of the documentation arising out of such transport are becoming less pronounced. As a result there may be a greater need in the future than there has been in the past for harmonization of the rules governing such transport documentation.

82. The Secretariat intends to remain informed of developments in this field. When the time seems mature, the Secretariat may suggest to the Commission a future course of action taking into account the views expressed by the Commission.

⁵⁶ eighth session of the Commission that "if it were considered desirable that any security interest for the financing of international trade should have as one element a system of registration, the possibility of a world-wide computer-assisted registration system should be explored". Report of the United Nations Commission on International Trade Law on the work of its eighth session, *Official Records of the General Assembly, Thirtieth Session, Supplement No. 17 (A/10017)*, para. 60 (Yearbook . . . 1975, part one, II, A).

⁵⁷ A/CN.9/221, paras. 70 to 81 (reproduced in this volume, part two, II, C).

⁵⁸ *Ibid.*, para. 88.

⁵⁹ The progress made by the International Chamber of Commerce in revising UCP is described in A/CN.9/229 (reproduced in this volume, part two, VI, C). The most recent draft of the revision at the time of writing is found in ICC document No. 470/394. The provisions on transport documents are found in articles 22 to 33.

C. Note by the Secretariat: documentary credits (A/CN.9/229)*

1. The Commission at its first session in 1968 placed the subject of bankers' commercial credits on its priority list of topics. In view of the previous work done by the International Chamber of Commerce (ICC) in this field, through its publication of the Uniform Customs and Practice for Documentary Credits, the Commission requested the Secretary-General to inquire whether the ICC would be prepared to undertake a study of the subject.¹

STUDY BY THE ICC

2. The study of the ICC, submitted to the Commission at its second session in 1969 as annex I to document A/CN.9/15,** described the manner in which documentary credits were used and the history in the ICC of the preparation of the Uniform Customs and Practice for Documentary Credits (UCP) from the initial "Uniform Regulation on Documentary Credits" adopted in 1929 through the then current 1962 version of UCP.

3. The study also pointed out that the ICC kept UCP under constant review to make sure that it did not drop behind current changes in international trade and shipping practice. The study closed by saying that:

"It would, however, be of considerable help to have the United Nations, through UNCITRAL, commend this Code to all Member nations, including, if possible, those where these rules are not yet applied".²

4. In response to this request of the ICC, the Commission at its second session commended to Governments the use of the 1962 version of UCP.³ At the same time it decided to keep the item on its agenda.

1974 REVISION OF UCP

5. At its third session the Commission was informed that the ICC had appointed a working party for the revision of the 1962 version of UCP.⁴ The Commission welcomed the work of revision to be undertaken by the ICC and, in order to permit interested circles in countries not represented in the ICC to make observation on the operation of

the 1962 version of UCP, it was decided that the Secretary-General should invite Governments and interested trade and banking institutions to communicate their observations to the Secretary-General for transmission to the ICC. In response to his invitation the Secretary-General received a number of replies, which were transmitted to the ICC for consideration along with the replies received by it from its National Committees.

6. At its seventh session in 1974, the Commission took note of the fact that the Commission on Banking Technique and Practice of the ICC had adopted a draft revised text of UCP.⁵ The Commission also noted that the text submitted to it was subject to further revision and that a final text was expected to be adopted by the Council of the ICC later in that year. There was general agreement in the Commission that, while the Commission could not itself adopt the revised text of UCP, it should consider at its following session the desirability of commending the use of UCP in transactions involving the establishment of a documentary credit.

7. As had been expected, between the seventh and eighth sessions of the Commission, the Executive Committee of the ICC adopted the 1974 version of UCP for use in transactions involving the establishment of a documentary credit as from 1 October 1975. In conformity with the view expressed at its seventh session the Commission, at its eighth session, decided to commend the use of the 1974 version of UCP.⁶ This decision of the Commission was adopted in the form normally used for resolutions and was reprinted by the ICC in its brochure containing the text of UCP.⁷

CURRENT REVISION

8. The 1974 version of UCP has been considered to have been generally successful in eliminating certain problems arising under the 1962 version and to have allowed for developments in transport technology and commercial practice. However, since 1974 there have been further developments which have affected the use of documentary credits. In particular these developments are to be found in the use of and documentation for unitized cargo, especially in connection with multimodal transport, the establishment of documentary credits by tele-transmission, and certain recent changes in marine insurance.

⁵ Report of the United Nations Commission on International Trade Law on the work of its seventh session, *Official Records of the General Assembly, Twenty-ninth Session, Supplement No. 17*, (A/9617), paras. 30-35 (Yearbook . . . 1974, part one, II, A).

⁶ Report of the United Nations Commission on International Trade Law on the work of its eighth session, *Official Records of the General Assembly, Thirtieth Session, Supplement No. 17*, (A/10017), para. 41 (Yearbook . . . 1975, part one, II, A).

⁷ The text of the decision is contained in the annex to this report. The 1974 version of UCP is contained in ICC publication No. 290.

* 3 June 1982.

** Yearbook . . . 1968-1970, part three, III, B.

¹ Report of the United Nations Commission on International Trade Law on the work of its first session, *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16*, (A/7216), para. 48 (28) (Yearbook . . . 1968-1970, part two, I, A).

² A/CN.9/15, annex I, para. 26 (Yearbook . . . 1968-1970, part three, III, B).

³ Report of the United Nations Commission on International Trade Law on the work of its second session, *Official Records of the General Assembly, Twenty-fourth Session, Supplement No. 18*, (A/7618), para. 95 (Yearbook . . . 1968-1970, part two, II, A).

⁴ Report of the United Nations Commission on International Trade Law on the work of its third session, *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17*, (A/8017), paras. 119-126 (Yearbook . . . 1968-1970, part two, III, A).

9. Furthermore, in certain countries the use of stand-by letters of credit had become of great economic significance and it was desirable to specify their legal characteristics. As a result, the Commission at its eleventh session in 1978 placed on its priority list of subjects the topic of "stand-by letters of credit, to be studied in conjunction with the International Chamber of Commerce".⁸ The topic was further discussed at the Commission's twelfth session where it was noted that the work of the ICC in respect of documentary letters of credit had a direct bearing on work in respect of stand-by letters of credit.⁹ For this reason, there was general agreement that the ICC should be encouraged to continue its work on stand-by letters of credit in co-operation with the Commission's Secretariat.

10. As a result of these developments, in 1979 the ICC created a working party to consider a further revision to UCP. It was thought that the desirability of revisions in the following respects might particularly be examined:

UCP provisions relating to the presentation of transport documentation bearing especially in mind development in techniques such as combined transport;

The responsibilities of banks, and the relationships between banks, and between banks and other parties;

The possible introduction of specific provisions relating to stand-by letters of credit.¹⁰

11. As a first step the working party sent a questionnaire to its National Committees to inquire as to the desirability of revising the 1974 version of UCP. At the request of the ICC, the Commission's Secretariat sent the same questionnaire by means of a note verbale to all Governments.¹¹ The replies received by the Commission's Secretariat were transmitted to the ICC for consideration by the working party. In addition, the Commission's Secretariat has been represented at the meetings of the working party.

⁸ Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17*, (A/33/17), para. 67 (Yearbook . . . 1978, part one, II, A).

⁹ Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17*, (A/34/17), paras. 45-48 (Yearbook . . . 1979, part one, II, A). The Commission had before it a report of the Secretary-General entitled "Stand-by letters of credit" (A/CN.9/163) (Yearbook . . . 1979, part two, II, B).

¹⁰ At its meeting of 14 March 1977 the Commission on Banking Technique and Practice of the ICC had given its opinion that a stand-by credit fell within the definition of a documentary credit contained in UCP. However, it was felt that a specific reference to stand-by letters of credit within the text of UCP would make this point clearer. Moreover, because of the somewhat different nature of a stand-by credit as compared to a documentary credit used in connection with a sale of goods, it was expected that some changes might need to be made to the text of UCP to accommodate better the stand-by letter of credit.

¹¹ The Commission was informed at its fourteenth session of the planned revision of the 1974 version of UCP (A/CN.9/202/Add.1, paras. 131-132 [Yearbook . . . 1981, part two, V, A] and A/CN.9/203, para. 22 [Yearbook . . . 1981, part two, V, D] and that the Commission's Secretariat had sent the questionnaire to all Governments at the request of the ICC (*ibid.*).

12. The working party has prepared a draft revision of UCP which was considered by the Commission on Banking Technique and Practice of the ICC at its meeting of 24-25 May 1982. The Banking Commission accepted the major proposals of the working party, including a specific reference to the applicability of UCP to stand-by letters of credit and a major renovation of the articles on transport documents. It also requested the working party to reconsider several points for further clarification.

13. It is now anticipated that the Banking Commission will be in a position to approve a final text of the newly revised version of UCP before the spring of 1983.

CONCLUSION

14. The Commission may wish to take note of the work undertaken by the ICC to keep UCP abreast of developments in international trade and shipping practice and of its actions in response to the view expressed by the Commission at its twelfth session that the ICC should be encouraged to continue its work on stand-by letters of credit in conjunction with the Commission's Secretariat. The Commission may also wish to note that, as was the case with the 1974 revision of UCP and in order to permit interested circles in countries not represented in the ICC to make observations on the operation of UCP so that these could be taken into account in its revision, the Secretary-General has already addressed to all Governments the same questionnaire as was sent by the ICC to its National Committees and has transmitted the replies received to the ICC for its consideration.

15. The Commission may, therefore, wish to consider at its sixteenth session the possibility of commending the use of the revised text of UCP, as it did in respect of the 1962 and 1974 versions of UCP.

ANNEX

Decision of the United Nations Commission on International Trade Law, adopted on 17 April 1975

The United Nations Commission on International Trade Law,

Expressing its appreciation to the International Chamber of Commerce for having transmitted to it the revised text of "Uniform Customs and Practice for Documentary Credits", which was approved by the Commission on Banking Technique and Practice of the International Chamber of Commerce on 14 October 1974 and adopted by the Executive Committee of the International Chamber of Commerce on 3 December 1974,

Congratulating the International Chamber of Commerce on having made a further contribution to the facilitation of international trade by bringing up to date its rules on documentary credit practice to allow for developments in transport technology and changes in commercial practice,

Having regard to the fact that, in revising the 1962 text of "Uniform Customs", the International Chamber of Commerce has taken into account the observations made by Governments and banking and trade institutions of countries not represented within it and transmitted to it through the Commission,

Noting that "Uniform Customs" constitutes a valuable contribution to the facilitation of international trade,

Commends the use of the 1974 revision, as from 1 October 1975, in transactions involving the establishment of a documentary credit.

VII. STATUS OF CONVENTIONS

Note by the Secretary-General: status of conventions (A/CN.9/227)*

1. At its fourteenth session the Commission decided that the Secretariat should inform the Commission at its next session on the status of conventions that were the outcome of its work.¹

2. The present note is submitted pursuant to that decision. The annex hereto sets forth the status of signatures, ratifications and accessions as at 15 May 1982 to the following conventions: Convention on the Limitation Period in the International Sale of Goods (New York, 1974);** Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980);*** United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg);**** and United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980).*****

3. The Commission agreed that in addition to the Commission noting, at each session, the status of the conventions, more effective action should be taken to promote earlier acceptance of the conventions.²

4. On the recommendation of the Commission the General Assembly in paragraph 8 of its resolution 36/32 of 13 November 1981 requested the Secretary-General to bring those conventions to the notice of all States which had not ratified or acceded to them, and to provide those States with appropriate information as to the mode of their entry into force and the current status of ratifications and accessions, and to draw the attention of those States to the view of the Commission that an early entry into force and a wide acceptance of the instruments mentioned would be of great value for the unification of international trade law.³ Pursuant to that resolution the Secretary-General by a note verbale transmitted information as to the mode of entry into force and the status of signatures, ratifications, and accessions to the conventions.

ANNEX

1. Convention on the Limitation Period in the International Sale of Goods (New York, 1974)*

State	Signature	Ratification	Accession
Argentina			9 October 1981
Brazil	14 June 1974		
Bulgaria	24 February 1975		
Byelorussian SSR	14 June 1974		
Costa Rica	30 August 1974		
Czechoslovakia	29 August 1975	26 May 1977	
Dominican Republic			23 December 1977
German Democratic Republic	14 June 1974		
Ghana	5 December 1974	7 October 1975	
Hungary	14 June 1974		
Mongolia	14 June 1974		
Nicaragua	13 May 1975		
Norway	11 December 1975	20 March 1980	
Poland	14 June 1974		
Ukrainian SSR	14 June 1974		
USSR	14 June 1974		
Yugoslavia			27 November 1978

Signatures only: 11; ratifications and accessions: 6.

Declarations and reservations

Upon signature Norway declared that in accordance with article 34 the Convention would not govern contracts of sale where the seller and the buyer both had their relevant places of business within the territories of the Nordic States (i.e. Norway, Denmark, Finland, Iceland, and Sweden).

2. Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980)**

No accessions to date

* Yearbook . . . 1974, part three, I, B.
** Yearbook . . . 1980, part three, I, C.

* 3 June 1982.
** Yearbook . . . 1974, part three, I, B.
*** Yearbook . . . 1980, part three, I, C.
**** Yearbook . . . 1978, part three, I, B.
***** Yearbook . . . 1980, part three, I, B.
¹ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)* para. 117 (Yearbook . . . 1981, part one, A).
² *Ibid.*, para. 114.
³ *Ibid.*, para. 118.

3. United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg)*

State	Signature	Ratification	Accession
Austria	30 April 1979		
Barbados			2 February 1981
Brazil	31 March 1978		
Chile	31 March 1978		
Czechoslovakia	6 March 1979		
Denmark	18 April 1979		
Ecuador	31 March 1978		
Egypt	31 March 1978	23 April 1979	
Finland	18 April 1979		
France	18 April 1979		
Germany, Federal Republic of	31 March 1978		
Ghana	31 March 1978		
Holy See	31 March 1978		
Hungary	23 April 1979		
Madagascar	31 March 1978		
Mexico	31 March 1978		
Morocco			12 June 1981
Norway	18 April 1979		
Pakistan	8 March 1979		
Panama	31 March 1978		
Philippines	14 June 1978		
Portugal	31 March 1978		
Romania			7 January 1982
Senegal	31 March 1978		
Sierra Leone	15 August 1978		
Singapore	31 March 1978		
Sweden	18 April 1979		
Tunisia			15 September 1980
Uganda			6 July 1979
United Republic of Tanzania			24 July 1979
United States of America	30 April 1979		
Venezuela	31 March 1978		
Zaire	19 April 1979		

Signatures only: 26; ratification and accessions: 7.

Declarations and reservations

Upon signing the Convention the Czechoslovak Socialist Republic declared in accordance with article 26 a formula for converting the

* Yearbook . . . 1978, part three, I, B.

amounts of liability referred to in paragraph 2 of that article into the Czechoslovak currency and the amount of the limits of liability to be applied in the territory of the Czechoslovak Socialist Republic as expressed in the Czechoslovak currency.

4. United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980)*

State	Signature	Ratification	Accession
Austria	11 April 1980		
Chile	11 April 1980		
China	30 September 1981		
Czechoslovakia	1 September 1981		
Denmark	26 May 1981		
Finland	26 May 1981		
France	27 August 1981		
German Democratic Republic	13 August 1981		
Germany, Federal Republic of	26 May 1981		
Ghana	11 April 1980		
Hungary	11 April 1980		
Italy	30 September 1981		
Lesotho	18 June 1981	18 June 1981	
Netherlands	29 May 1981		
Norway	26 May 1981		
Poland	28 September 1981		
Singapore	11 April 1980		
Sweden	26 May 1981		
United States of America	31 August 1981		
Venezuela	28 September 1981		
Yugoslavia	11 April 1980		

Signatures only: 20; ratification: 1.

Declarations and reservations

Upon signing the Convention the Governments of Denmark, Finland, Norway and Sweden declared in accordance with Article 92 (I) that they would not be bound by Part II of the Convention (Formation of the Contract).

* Yearbook . . . 1980, part three, I, B.

VIII. TRAINING AND ASSISTANCE

Note by the Secretariat: training and assistance (A/CN.9/228)*

1. The Commission, at its fourteenth session,¹ agreed that it should continue to sponsor symposia and seminars on international trade law. It was considered desirable for these seminars to be organized on a regional basis. In this way, it was felt, a larger number of participants from the region could attend and the seminars would themselves help to promote the adoption of the texts emanating from the work of the Commission. The Commission welcomed the possibility that regional seminars might be sponsored jointly with regional organizations. The Secretariat was requested to make such arrangements as it found desirable in this regard.

2. By its resolution 36/32 of 13 November 1981, the General Assembly reaffirmed the importance, in particular for the developing countries, of the work of the United Nations Commission on International Trade Law concerned with training and assistance in the field of international trade law and welcomed the initiatives being undertaken to sponsor regional seminars jointly with regional organizations, such as the Asian-African Legal Consultative Committee and the Inter-American Juridical Committee. The resolution also invited Governments, relevant United Nations organs, organizations, institutions and individuals to assist the Secretariat of the Commission in financing and organizing symposia and seminars.

3. The Inter-American Juridical Committee of the Organization of American States (OAS) has included in its 1982 annual seminar the subject of international sale of goods. The programme for the Ninth Course on International Law, to be held from 2 to 27 August 1982, in Rio de Janeiro, includes a lecture and a discussion on the subject. The United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) and the Convention on the Limitation Period in the International Sale of Goods (New York, 1974) have been chosen for the seminar because of the likelihood of their coming into force in the near future.

4. The Secretary-General of the Asian-African Legal Consultative Committee (AALCC) has also agreed to organ-

ize, jointly with the UNCITRAL Secretariat, two-day seminars on trade law subjects in conjunction with its annual sessions, whenever feasible. This arrangement will enable delegates attending the meetings of the AALCC's Sub-Committee on International Trade Law Matters to participate in the seminars.

5. The UNCITRAL Secretariat also co-operated with the Stockholm Chamber of Commerce, the American Arbitration Association, and the USSR Chamber of Commerce and Industry by participating in a symposium on international commercial arbitration which was held from 4 to 5 March 1982, in Stockholm. This symposium was organized to celebrate the fifth anniversary of the entering into force of the "Optional Arbitration Clause for Use in Contracts in USA-USSR Trade - 1977", under which the Stockholm Chamber of Commerce is to administer arbitrations under the UNCITRAL Arbitration Rules. At this symposium, one day was devoted to the activities of the Commission in the field of settlement of international commercial disputes.

6. With respect to the financing of the training and assistance programme, a contribution of \$US 3,000 was received from the Government of Yugoslavia.

7. In addition, some bar associations have informally indicated their willingness to provide lecturers, at their expense, to service seminars which are to be held in developing countries. The Secretariat is also negotiating with a particular Government, which has funds for educational institutions in developing countries, to assist in the financing of regional seminars on a regular basis.

8. While the possibility of holding independent seminars is remote unless substantial financial contributions are received, the Secretariat is exploring various possibilities of collaborating with organizations and institutions in the organization of seminars of two- to three-day duration on various aspects of international trade law. Such seminars could also be used as a forum for the promotion of legal texts emanating from the work of the Commission.

9. During the past year, one intern received practical training at the UNCITRAL Secretariat under the United Nations/UNITAR fellowship programme in international law.

*17 June 1982.

¹ Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 109 (Yearbook ... 1981, part one, A).

I. RECOMMENDED PROVISIONS ON UNIVERSAL UNIT OF ACCOUNT FOR USE IN INTERNATIONAL CONVENTIONS ADOPTED AT THE FIFTEENTH SESSION OF THE COMMISSION*

[The text of these Provisions is contained in paragraph 63 of the Report which is reproduced in this volume, part one, A.]

*With regard to the endorsement by the General Assembly of these Provisions, see General Assembly resolution 37/107 of 16 December 1982 reproduced in this volume, part one, D.

II. RECOMMENDATIONS TO ASSIST ARBITRAL INSTITUTIONS AND OTHER INTERESTED BODIES WITH REGARD TO ARBITRATIONS UNDER THE UNCITRAL ARBITRATION RULES ADOPTED AT THE FIFTEENTH SESSION OF THE COMMISSION

INTRODUCTION

1. The UNCITRAL Arbitration Rules* were adopted by the United Nations Commission on International Trade Law in 1976, after extensive consultations with arbitral institutions and arbitral experts. In the same year, the General Assembly of the United Nations, by its resolution 31/98,** recommended the use of these Rules in the settlement of disputes arising in the context of international commercial relations. This recommendation was based on the conviction that the establishment of rules for *ad hoc* arbitration that were acceptable in countries with different legal, social and economic systems would significantly contribute to the development of harmonious international economic relations.

2. Since then, the UNCITRAL Arbitration Rules have become well known and are widely used around the world, not only in *ad hoc* arbitrations. Contracting parties increasingly refer to these Rules in their arbitration clauses or agreements, and a substantial number of arbitral institutions have, in a variety of ways, accepted or adopted these Rules.

3. One way in which the UNCITRAL Arbitration Rules have been accepted is that arbitral bodies have drawn on them in preparing their own institutional arbitration rules. This has taken two different forms. One has been to use the UNCITRAL Arbitration Rules as a drafting model, either in full (e.g., the 1978 Rules of Procedure of the Inter-American Commercial Arbitration Commission) or in part (e.g., the 1980 Procedures for Arbitration and Additional Rules of the International Energy Agency Dispute Settlement Centre).

4. The other form has been to adopt the UNCITRAL Arbitration Rules as such, maintaining their name, and to include in the statutes or administrative rules of an institution a provision that disputes referred to the institution shall be settled in accordance with the UNCITRAL Arbitration Rules, subject to any modifications set forth in those statutes or administrative rules. Prime examples of institutions adopting this approach are the two arbitration centres established under the auspices of the Asian-African Legal Consultative Committee (see Rule I of the Rules for Arbitration of the Kuala Lumpur Regional Arbitration

Centre; articles 4 and 11 of the Statutes of the Cairo Centre for International Commercial Arbitration). In addition, a provision similar to the one described above was included in the "Declaration of the Government of the Democratic and Popular Republic of Algeria concerning the settlement of claims by the Government of the United States of America and the Government of the Islamic Republic of Iran" of 19 January 1981 (article III, paragraph 2).

5. In addition to the above cases, which concern an arbitral body's own and only rules, a great number of institutions which have their own established arbitration rules have accepted, in a variety of ways, the use of the UNCITRAL Arbitration Rules if parties so wished. Some institutions have, for example, embodied that option into their established institutional rules (e.g. London Court of International Arbitration, 1981 International Arbitration Rules; Foreign Trade Arbitration of the Economic Chamber of Yugoslavia, 1981 Rules). Another form of acceptance has been to offer the administrative facilities of an arbitral institution in co-operation agreements between arbitration associations or chambers of commerce and in recommendations or model clauses providing for the use of the UNCITRAL Arbitration Rules. The prime example, which was also the first international agreement to include the UNCITRAL Arbitration Rules, is the "Optional Arbitration Clause for use in contracts in USA-USSR Trade - 1977 (prepared by American Arbitration Association and USSR Chamber of Commerce and Industry)", with the Stockholm Chamber of Commerce acting as appointing authority.

6. Of the many other institutions that have declared their willingness to act as appointing authority and to provide administrative services in arbitration cases under the UNCITRAL Arbitration Rules only one should be mentioned here. The American Arbitration Association (AAA) has adopted a specific set of administrative "Procedures for Cases under the UNCITRAL Arbitration Rules" setting forth in detail how the AAA would perform the functions of an appointing authority and provide administrative services in conformity with the UNCITRAL Arbitration Rules.

7. In view of the promising trend in favour of the use of the UNCITRAL Arbitration Rules, these recommendations are intended to provide information and assistance to arbitral institutions and other relevant bodies, such as

* Yearbook . . . 1976, part one, II, A, para. 57.

** Yearbook . . . 1977, part one, I, C.

chambers of commerce. As the above examples indicate, there are a number of ways in which the UNCITRAL Arbitral Rules and their use in arbitration proceedings may be accepted.

A. ADOPTION OF UNCITRAL ARBITRATION RULES AS INSTITUTIONAL RULES OF AN ARBITRAL BODY

8. Arbitral institutions, when preparing or revising their institutional rules, may wish to consider the advisability of adopting the UNCITRAL Arbitration Rules. While it would clearly be in the interest of the desired unification of the rules on arbitral procedure that arbitral institutions adopt these Rules in full, some institutions may have reasons for incorporating, at least for the time being, only some of the provisions of these Rules. Even such adoption in part would constitute a step towards the harmonization of the rules on arbitral procedure.

9. However, if an institution intends to adopt such provisions and to maintain the name UNCITRAL Arbitration Rules, special considerations come into play which relate to the interest and expectations of the parties to an arbitration agreement or to a contract including an arbitration clause. Parties, and their lawyers, who have gained familiarity with and confidence in the use of the UNCITRAL Arbitration Rules tend to rely on the uniform and full application of these Rules by any arbitral institution which in its rules provides for the application of the UNCITRAL Arbitration Rules.

10. Therefore, an arbitral institution which intends to refer in its institutional rules to the UNCITRAL Arbitration Rules should take into account this interest of the parties in having certainty about which procedures to expect. Accordingly, it is recommended that institutions, when adopting the UNCITRAL Arbitration Rules and maintaining their name, refrain from modifying them.

11. This appeal to leave the UNCITRAL Arbitration Rules unchanged does not mean, of course, that the particular organizational structure and needs of a given institution should be neglected. Such specific features normally relate to matters not regulated in the UNCITRAL Arbitration Rules. For example, there are no special provisions in these Rules concerning the various facilities and procedures relating to administrative services or on such particular matters as fee schedules. It should, therefore, be possible to adopt institutional rules consisting of the UNCITRAL Arbitration Rules and some administrative rules which are tailored to the particular organizational structure and needs of the institution and are in conformity with the UNCITRAL Arbitration Rules.

12. If, in exceptional circumstances, an institution deems it necessary, for administrative purposes, to adopt a rule which modifies the UNCITRAL Arbitration Rules, it is strongly recommended to clearly indicate that modification. An appropriate way of doing so is to specify the

provision of the UNCITRAL Arbitration Rules involved, as done, for example, in the Rules for Arbitration of the Kuala Lumpur Regional Arbitration Centre (opening words of Rule 8: "In lieu of the provisions of article 41 of the UNCITRAL Arbitration Rules the following provisions shall apply: . . ."). This indication would be of great help to the reader and potential user who would otherwise have to embark on a comparative analysis of the administrative procedures and all provisions of the UNCITRAL Arbitration Rules in order to discover any disparity between them.

B. ARBITRAL INSTITUTION OR OTHER BODY ACTING AS APPOINTING AUTHORITY OR PROVIDING ADMINISTRATIVE SERVICES IN *AD HOC* ARBITRATION UNDER THE UNCITRAL ARBITRATION RULES

1. *Offer of services*

13. *Ad hoc* arbitrations conducted under the UNCITRAL Arbitration Rules may be facilitated by a body acting as appointing authority or providing administrative services of a secretarial, technical nature. These kinds of assistance could be rendered not only by arbitral institutions but also by other bodies, in particular chambers of commerce or trade associations.

14. Such institutions and bodies are invited to consider offering their services in this regard. If they decide to do so, they may wish to make that willingness known to the interested public. It is advisable that they describe in detail the services offered and the relevant administrative procedures.^a

15. In devising these administrative procedures or rules, the institutions should have due regard to the interests of the parties. Since the parties in these cases have agreed that the arbitration is to be conducted under the UNCITRAL Arbitration Rules, their expectations should not be frustrated by an administrative rule which is in conflict with the UNCITRAL Arbitration Rules. Thus, the considerations and the appeal expressed above in the context of adopting these Rules as institutional rules (see paragraphs 9-12) apply here with even greater force.

16. The following remarks and suggestions are intended to assist any interested institution in taking the necessary organizational measures and in devising appropriate

^a In an introductory part, the institution may wish to provide, in addition to the customary description of its aims and traditional activities, some information regarding the UNCITRAL Arbitration Rules. In particular, it may state that these Rules were adopted in 1976, after extensive deliberations, by the United Nations Commission on International Trade Law, that this Commission consists of 36 member States representing the different legal, economic and social systems and geographic regions of the world; that in the preparation of these Rules, various interested international organizations and leading arbitration experts were consulted; that the General Assembly of the United Nations has recommended the use of these Rules for inclusion in international commercial contracts; and that these Rules have become widely known and been accepted around the world.

administrative procedures in conformity with the UNCITRAL Arbitration Rules.

17. It is recommended that the administrative procedures of the institution distinguish clearly between the functions of an appointing authority as envisaged under the UNCITRAL Arbitration Rules and other administrative assistance of a technical, secretarial nature. The institution should declare whether it is offering both or only one of these types of service. When offering both types the institution may declare its willingness to provide only one of these services in a given case, if so requested.

18. The distinction between these two types of services is also of relevance to the question of which party may request these services. On the one hand, an institution may act as appointing authority under the UNCITRAL Arbitration Rules only if it has been so designated by the parties, whether in the arbitral clause or in a separate agreement. An institution should so state in its administrative procedures, possibly with the additional provision (as a rule of interpretation) that it would also act as appointing authority if the parties submit a dispute to it under the UNCITRAL Arbitration Rules without specifically designating it as the appointing authority. On the other hand, administrative services of a technical, secretarial nature might be requested not only by the parties, but also by the arbitral tribunal (cf. article 15, paragraph (1) and article 38, paragraph (c) of the UNCITRAL Arbitration Rules).

19. In order to assist parties, the institution may wish to set forth in its administrative procedures model arbitration clauses covering the above services. The first part of any such model clause should be identical with the model clause of the UNCITRAL Arbitration Rules:

"Any dispute, controversy or claim arising out of or relating to this contract, or the breach, termination or invalidity thereof, shall be settled by arbitration in accordance with the UNCITRAL Arbitration Rules as at present in force".

The agreement as to the services which are requested should follow. For example:

"The appointing authority shall be the XYZ-Institution".
or:

"The XYZ-Institution shall act as appointing authority and provide administrative services in accordance with its administrative procedures for cases under the UNCITRAL Arbitration Rules".

As suggested in the UNCITRAL Model Arbitration Clause, the following note may be added:

"Note—Parties may wish to consider adding:

"(a) The number of arbitrators shall be . . . (one or three);

"(b) The place of arbitration shall be . . . (town or country);

"(c) The language(s) to be used in the arbitral proceedings shall be . . ."

20. In view of the considerations and concerns expressed above in paragraphs 12 and 15, if the administrative procedures of the institution are such as to lead to a modification in substance of the UNCITRAL Arbitration Rules, it may be advisable that this modification be reflected in the model clause.

2. *Functions as appointing authority*

21. An institution which is willing to act as appointing authority under the UNCITRAL Arbitration Rules should specify in its administrative procedures the various functions of an appointing authority envisaged by these Rules which it will perform. It might also describe the manner in which it intends to perform these functions.

(a) *Appointment of arbitrators*

22. The UNCITRAL Arbitration Rules envisage various possibilities concerning the appointment of an arbitrator by an appointing authority. Under article 6, paragraph 2, the appointing authority may be requested to appoint a sole arbitrator, in accordance with certain procedures and criteria set forth in article 6, paragraphs 3 and 4. Further, it may be requested, under article 7, paragraph 2, to appoint the second of three arbitrators. Finally, it may be called upon to appoint a substitute arbitrator under articles 11, 12 or 13 (successful challenge and other reasons for replacement).

23. For each of these cases, the institution may indicate details as to how it would select the arbitrator in accordance with the UNCITRAL Arbitration Rules. In particular, it may state whether it maintains a panel or list of arbitrators, from which it would select appropriate candidates, and may provide information on the composition of such panel. It may also specify which person or organ within the institution would in fact make the appointment (e.g. president, director, secretary or a committee).

(b) *Decision on challenge of arbitrator*

24. Under article 10 of the UNCITRAL Arbitration Rules, any arbitrator may be challenged if circumstances exist that give rise to justifiable doubts as to his impartiality or independence. When such a challenge is contested (e.g. if the other party does not agree to the challenge or the challenged arbitrator does not withdraw), the decision on the challenge is to be made by the appointing authority according to article 12, paragraph 1. If the appointing authority sustains the challenge, it may also be called upon to appoint the substitute arbitrator.

25. The institution may indicate details as to how it would make the decision on such a challenge in accordance

with the UNCITRAL Arbitration Rules. In particular, it may state which person or organ within the institution would make the decision. The institution may also wish to identify any code of ethics or other written principles which it would apply in ascertaining the independence and impartiality of arbitrators.

(c) *Replacement of arbitrator*

26. In the event that an arbitrator fails to act or in the event of the *de jure* or *de facto* impossibility of his performing his functions, the appointing authority may, under article 13, paragraph 2, be called upon to decide on whether such a reason for replacement exists, and it may be involved in appointing a substitute arbitrator. What has been said above in regard to the challenge of an arbitrator applies also to such cases of replacement of an arbitrator.

27. The situation is different with regard to those cases of replacement covered by paragraph 1 of article 13. In the event of the death or resignation of an arbitrator during the course of the arbitral proceedings, the only task which may be entrusted to an appointing authority is to appoint a substitute arbitrator.

(d) *Assistance in fixing fees of arbitrators*

28. Under the UNCITRAL Arbitration Rules, the arbitral tribunal fixes its fees, which shall be reasonable in amount, taking into account the amount in dispute, the complexity of the subject-matter, the time spent by the arbitrators and any other relevant circumstances of the case. In this task, the arbitral tribunal may be assisted by an appointing authority in three different ways:

(i) If the appointing authority has issued a schedule of fees for arbitrators in international cases which it administers, the arbitral tribunal in fixing its fees shall take that schedule of fees into account to the extent that it considers appropriate in the circumstances of the case (article 39, paragraph 2);

(ii) In the absence of such a schedule of fees, the appointing authority may provide, upon a party's request, a statement setting forth the basis for establishing fees which is customarily followed in international cases in which the authority appoints arbitrators (article 39, paragraph 3);

(iii) In cases referred to under (i) and (ii), when a party so requests and the appointing authority consents, the arbitral tribunal shall fix its fees only after consultation with the appointing authority, which may make any comment it deems appropriate to the arbitral tribunal concerning the fees (article 39, paragraph 4).

29. An institution willing to act as appointing authority may indicate, in its administrative procedures, any relevant details in respect of these three possible ways of

assistance in fixing fees. In particular, it may state whether it has issued a schedule of fees as envisaged under (i). The institution might also declare its willingness to perform the function envisaged under (ii), if it has not issued a fee schedule, and to perform the function under (iii).

(e) *Advisory comments regarding deposits*

30. Under article 41, paragraph 3, of the UNCITRAL Arbitration Rules, the arbitral tribunal shall fix the amounts of any initial or supplementary deposits only after consultation with the appointing authority, which may make any pertinent comment it deems appropriate, if a party so requests and the appointing authority consents to perform this function. The institution may wish to indicate in its administrative procedures its general willingness to do so.

31. It should be noted that, under the UNCITRAL Arbitration Rules, this kind of advice is the only task relating to deposits which an appointing authority may be requested to fulfil. Thus, if an institution offers to perform any other function (e.g. to hold deposits, to render an accounting thereof), it should be pointed out that this is a modification of article 41 of the UNCITRAL Arbitration Rules.

3. *Administrative services*

32. An institution which is prepared to provide administrative services of a technical, secretarial nature may describe in its administrative procedures the various services offered. Such services may be rendered upon request of the parties or the arbitral tribunal.

33. In describing the various services, the institution should specify those services which would not be covered by its general administrative fee and which, therefore, would be billed separately (e.g. interpretation services). The institution may also wish to indicate which of the services it can provide itself, with its own facilities, and which it might merely arrange to be rendered by others.

34. The following list of possible administrative services, which is not intended to be exhaustive, may assist institutions in considering and publicizing which services it may offer:

(a) Forwarding of written communications of a party or the arbitrators;

(b) Assisting the arbitral tribunal in establishing the date, time and place of hearings, and giving advance notice to the parties (cf. article 25, paragraph 1 of UNCITRAL Arbitration Rules);

(c) Providing, or arranging for, meeting rooms for hearings or deliberations of the arbitral tribunal;

(d) Arranging for stenographic transcripts of hearings;

(e) Assisting in filing or registering arbitral awards in those countries where such filing or registration is required by law;

(f) Providing secretarial or clerical assistance in other respects.

4. *Administrative fee schedule*

35. The institution may wish to state the fees which it charges for its services. It might reproduce its administrative fee schedule or, in the absence thereof, indicate the basis for calculating its administrative fees.

36. In view of the two possible categories of services an institution may offer, it is recommended that the fee for each category be stated separately. Thus, if an institution offers both categories of service, it may indicate its fees for the following three functions:

(a) Acting as appointing authority and providing administrative services;

(b) Acting as appointing authority only;

(c) Providing administrative services without acting as appointing authority.

(In addition to the information and suggestions set forth herein, assistance may be obtained from the secretariat of the Commission (International Trade Law Branch, Office of Legal Affairs, United Nations, Vienna International Centre, P.O. Box 500, A-1400 Vienna, Austria). The secretariat could, for example, provide any interested institution with copies of the institutional rules or administrative procedures of a given other institution. It may also, if so requested, assist in the drafting of an administrative provision or make suggestions in this regard.)

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V. CHECK LIST OF UNCITRAL DOCUMENTS

List of documents before the Commission at its fifteenth session

<i>Title or description</i>	<i>Document symbol</i>	<i>Location in present volume</i>
A. GENERAL SERIES		
Provisional agenda	A/CN.9/209	Not reproduced
Report of the Working Group on International Negotiable Instruments on the work of its eleventh session (New York, 3-14 August 1981)	A/CN.9/210	Part two, II, A, 1
Draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles as adopted by the Working Group on International Negotiable Instruments: note by the Secretariat	A/CN.9/211	Part two, II, A, 3
Draft Convention on International Cheques: text of draft articles as adopted by the Working Group on International Negotiable Instruments: note by the Secretariat	A/CN.9/212 and Corr. 1 (Spanish only)	Part two, II, A, 5
Commentary on draft Convention on International Bills of Exchange and International Promissory Notes: report of the Secretary-General	A/CN.9/213	Part two, II, A, 4
Commentary on draft Convention on International Cheques: report of the Secretary-General	A/CN.9/214	Part two, II, A, 6
Report of the Working Group on International Negotiable Instruments on the work of its twelfth session (Vienna, 4-15 January 1982)	A/CN.9/215	Part two, II, B, 1
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Status of Conventions: note by the Secretary-General	A/CN.9/227	Part two, VII
Training and assistance: note by the Secretariat	A/CN.9/228	Part two, VIII
Co-ordination of work: documentary credits: note by the Secretariat	A/CN.9/229	Part two, VI, C
Report of the United Nations Commission on International Trade Law on the work of its fifteenth session	A/CN.9/230 and Corr. 1 (English only)	Part one, A

B. RESTRICTED SERIES

Draft report of the United Nations Commission on International Trade Law on the work of its fifteenth session	(A/CN.9/XV) CRP.1 and Add. 1 to 12	Not reproduced
Draft provision on universal unit of account	(A/CN.9/XV) CRP.2	Not reproduced
International commercial arbitration: revised draft text of recommendations relating to the use of the UNCITRAL Arbitration Rules	(A/CN.9/XV) CRP.3	Not reproduced

C. INFORMATION SERIES

List of participants	A/CN.9/XV/INF.2	Not reproduced
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Working Group on International Contract Practices, third session

A. WORKING PAPERS

Provisional agenda	A/CN.9/WG.II/WP.34	Not reproduced
Possible features of a model law on international commercial arbitration: questions for discussion by the Working Group; note by the Secretariat	A/CN.9/WG.II/WP.35	Part two, III, B

B. RESTRICTED SERIES

Draft report of the Working Group on International Contract Practices on the work of its third session (New York, 16-26 February 1982)	A/CN.9/WG.2/(III)/CRP.1 and Add. 1 to 5	Not reproduced
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C. INFORMATION SERIES

List of participants	A/CN.9/WG.2/(III)/INF.2	Not reproduced
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Working Group on International Negotiable Instruments, eleventh session

A. WORKING PAPERS

Provisional agenda	A/CN.9/WG.IV/WP.20	Not reproduced
Uniform rules applicable to international cheques: note by the Secretariat	A/CN.9/WG.IV/WP.21	Part two, II, A, 2, a
Draft Convention on International Bills of Exchange and International Promissory Notes: note by the Secretariat	A/CN.9/WG.IV/WP.22	Part two, II, A, 2, b
Uniform rules applicable to international cheques: note by the Secretariat; annex: note by the observer of the Hague Conference on Private International Law intended for the Working Group on International Negotiable Instruments	A/CN.9/WG.IV/WP.23	Part two, II, A, 2, c
Draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles as revised by the Drafting Group; note by the Secretariat	A/CN.9/WG.IV/WP.24	Part two, II, A, 2, d

B. RESTRICTED SERIES

Draft report of the Working Group on International Negotiable Instruments on the work of its twelfth session (Vienna, 4-12 January 1982)	A/CN.9/WG.IV(XII)/CRP.1 and Adds. 1 to 3	Not reproduced
Sample price index provision	A/CN.9/WG.IV(XII)/CRP.2 and Rev.1	Not reproduced
Sample amendment procedure for limit of liability	A/CN.9/WG.IV(XII)/CRP.3 and Rev.1	Not reproduced

Statement of the delegation of the Soviet Union	A/CN.9/WG.IV(XII)/CRP.4	Reproduced as annex to the document A/CN.9/215, part two, II, B, 1
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C. INFORMATION SERIES

List of participants	A/CN.9/WG.IV(XII)/INF.1	Not reproduced
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Working Group on the New International Economic Order, third session

A. WORKING PAPERS

Provisional agenda	A/CN.9/WG.V/WP.6	Not reproduced
Clauses related to contracts for the supply and construction of large industrial works: study II of the Secretary-General	A/CN.9/WG.V/WP.7 and Add. 1 to 6	Part two, IV, B

B. RESTRICTED SERIES

Draft report of the Working Group on the New International Economic Order on the work of its third session (New York, 12-23 July 1982)	A/CN.9/WG.V/III/CRP.1 and Add. 1 to 8	Not reproduced
Provisional list of participants	A/CN.9/WG.V/III/CRP.2	Not reproduced
Possible structure of the future legal guide: proposal by the German Democratic Republic	A/CN.9/WG.V/III/CRP.3	Not reproduced

C. INFORMATION SERIES

List of participants	A/CN.9/WG.V/III/INF.1	Not reproduced
Draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles as revised by the Drafting Group: corrections made by the Drafting Group to articles 1-45: note by the Secretariat	A/CN.9/WG.IV/WP.24/ Add.1	Part two, II, A, 2, e
Draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles as revised by the Drafting Group: note by the Secretariat	A/CN.9/WG.IV/WP.24/ Add.2	Part two, II, A, 2, f
Draft Convention on International Cheques: text of draft articles as revised by the Drafting Group: note by the Secretariat	A/CN.9/WG.IV/WP.25	Part two, II, A, 2, g
Draft Convention on International Cheques: text of draft articles as revised by the Drafting Group: corrections made by the Drafting Group to draft articles 1-66: note by the Secretariat	A/CN.9/WG.IV/WP.25/ Add.1	Part two, II, A, 2, h

B. RESTRICTED SERIES

Draft report of the Working Group on International Negotiable Instruments on the work of its eleventh session (New York, 3-14 August 1981)	A/CN.9/WG.IV(XI)/CRP.1 and Add. 1 to 7	Not reproduced
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C. INFORMATION SERIES

List of participants	A/CN.9/WG.IV(XI)/INF.2	Not reproduced
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Working Group on International Negotiable Instruments, twelfth session

WORKING PAPERS

Provisional agenda	A/CN.9/WG.IV/WP.26	Not reproduced
Unit of account of constant value: report of the Secretary-General	A/CN.9/WG.IV/WP.27	Part two, II, B, 2